

# **LOCAL GOVERNMENT PENSION SCHEME**

## **(The Scheme)**

### **PREPAYMENT OF CONTRIBUTIONS**

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### **O P I N I O N**

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#### **INTRODUCTION**

1. I am instructed by Thelma Stober of the Local Government Association (the LGA) on behalf of the LGPS Scheme Advisory Board (England and Wales) (the Board). My advice is to be provided to LGPS “administering authorities”.

#### **THE SCHEME**

2. The Scheme is:-
- (1) A defined benefit funded pension scheme;
  - (2) Governed principally by the Local Government Pension Scheme Regulations 2013, S.I. 2013/2356, as amended (the Regulations).

#### **ADMINISTERING AUTHORITIES**

3. The capacities of administering authorities include that:-
- (1) They are scheme employers, as defined, for the purposes of the Regulations; and
  - (2) They have the General Power of Competence (GPOC), pursuant to Section 1 of the Localism Act 2011 (LA 2011), but subject to Sections 2-5 inclusive of LA 2011, and a power to be exercised reasonably, properly, and in accordance with the fiduciary duty to council tax payers.

#### **ADVICE SOUGHT**

4. I am asked whether prepaying both employer and employee primary contributions is in contravention of the Regulations and/or overriding legislation, such as the Pensions Act

1995 (PA 1995). This arises in the context that LGPS employers have expressed an interest in prepaying contributions, because the discount they would receive is likely to exceed any money market returns they could make. That would be a demonstration of “best value”.

5. My helpful Instructions observe that:-

- (1) It is quite common for employers to prepay secondary employer contributions;
- (2) It is less common for employers to prepay primary employer contributions; and
- (3) The LGA/the Board are not aware that any employers are prepaying employee contributions.

### **THE STARTING POINT**

6. There is a long established annual principle of local government finance. It stems from successive statutory frameworks under which local authorities both spend and raise money on an annual basis.

7. One aspect of the principle is that, subject to borrowing powers, to be exercised for future benefit, there is, *prima facie*, no right to charge future ratepayers/council tax payers with present expenditure. The other aspect of the principle is that there is no right, *prima facie*, to burden present ratepayers/council tax payers with future expenditure, i.e. no right to engage in forward funding.

8. The statutory provisions which currently give rise and/or effect to this annual principle are:-

- (1) The Local Government Finance Act 1992: council tax and precepts are based on a number of calculations which are to be made in relation to each financial year;
- (2) The Audit Commission Act 1988/Local Audit and Accountability Act 2014: local authority accounts are subject to annual audit: and

- (3) The Local Government Act 2003 (LGA 2003): a revenue account is an account for a financial year of the authority.

9. The application of the annual principle in practice is not straightforward. The decisions of the House of Lords in Manchester City Council v Greater Manchester Metropolitan County Council (1980) 78 LGR 560 and Re Westminster City Council [1986] 1 AC 668 are not readily reconcilable. The question appears to be whether, as a matter of fact and degree, there is some link between:-

- (1) The year in which the payment is made; and
- (2) The purpose for which the payment is made.

### **STATUTORY FRAMEWORK**

10. Pursuant to LGA 2003, there have been made the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, S.I. 2003/3146. As amended (the CFR).

11. Part 3 of the CPR relates to “credit arrangements”. Within Part 3, Regulations 3 and 4 specify arrangements which are not credit arrangements. Regulation 4, referring to Section 7 of LGA 2003, provides:-

- “(1) Liabilities for retirement benefits appropriated to a pension reserve in accordance with proper practices are liabilities specified for the purposes of Section 7(3)(c).
- (2) For the purposes of paragraph (1) and regulation 30, “retirement benefits” means benefits payable pursuant to statutory requirements under an arrangement accounted for as a defined benefit pension plan or as other long-term employee benefits (as defined in accordance with proper practices).”

12. Part 7 of the CFR relates to Accounts, and includes:-
- (1) Regulation 30 (retirement benefits); and
  - (2) Regulation 31 (proper practices).

13. Regulation 30 importantly provides:-

“For a financial year beginning on or after 1<sup>st</sup> April 2004, a local authority shall charge to a revenue account an amount equal to the retirement benefits payments and contributions to pension funds which are payable for that financial year in accordance with the statutory requirements mentioned in regulation 4(2).”

## **THE REGULATIONS**

14. Part 2 of the Regulations relates to Administration. Part 3 relates to Governance.

Within Part 2:-

- (1) Regulation 57 relates to the Pension Fund Annual Report; and
- (2) Regulation 58 relates to the Funding Strategy Statement (“FSS”).

15. Also within Part 2 of the Regulations:-

- (1) Regulation 62 relates to triennial Actuarial Valuations and Certificates;
- (2) Regulation 64 relates to special circumstances where revised actuarial valuations and certificates must be obtained, in particular where an employing authority ceases to be a scheme employer;
- (3) Regulation 67 relates to employer’s contributions, being in each year the amount calculated in accordance with a rates and adjustments certificate under Regulation 62 or 64; and
- (4) Regulation 69 relates to payment by employing authorities to appropriate administering authorities.

16. Regulation 62(1) provides (emphasis added):-

“Each administering authority must obtain-

- (a) an actuarial valuation of the assets and liabilities of each of its pension funds as at 31<sup>st</sup> March 2016 and in every third year afterwards;
- (b) a report by an actuary in respect of the valuation; and
- (c) a rates and adjustments certificate prepared by an actuary.”

17. Regulation 62(3) provides (emphasis added) that a “rates and adjustments certificate” is a certificate specifying –

- (a) the primary rate of the employer’s contribution, and
- (b) the secondary rate of the employer’s contribution,

for each year of the period of three years beginning with 1<sup>st</sup> April in the year following that in which the valuation date falls”. This is in accordance with the annual principle of local government finance. Regulation 62(5) provides that the primary rate of an employer’s contribution is the amount in respect of the cost of future accruals, expressed as a percentage of the pay of their employees who are “active members”.

18. Regulation 62(4), (5) and (6) provide (emphasis added):-

“(4) A rates and adjustments certificate is a certificate specifying –

- (a) the primary rate of employer’s contribution; and
- (b) the secondary rate of the employer’s contribution,

for each year of the period of three years beginning with 1<sup>st</sup> April in the year following that in which the valuation date falls.

(5) The primary rate of an employer’s contribution is the amount in respect of the cost of future accruals which, in the actuary’s opinion, should be paid to a fund by all bodies whose employees contribution to it so as to secure its solvency, expressed as a percentage of the pay of their employees who are active members.

(6) The actuary must have regard to –

- (a) the existing and prospective liabilities of the fund arising from circumstances common to all those bodies;
- (b) the desirability of maintaining as nearly constant a primary rate as possible;
- (c) the current version of the administering authority’s funding strategy statement mentioned in regulation 58; and

- (d) the requirement to secure the solvency of the pension fund and the long term efficiency of the Scheme, so far as relating to the pension fund.”

19. Regulation 62(7) provides (emphasis added):-

“The secondary rate of an employee’s contribution is any percentage or amount by which, in the actuary’s opinion, contributions at the primary rate should, in the case of a Scheme employer, be increased or reduced by reason of any circumstances peculiar to that employer.”

20. The important provisions of Regulation 67 include (emphasis added):-

“(1) An employing authority must contribute to the appropriate fund in each year covered by a rates and adjustments certificate under regulation 62 or 64 the amount appropriate for that authority as calculated in accordance with the certificate and paragraph (4).

(2) During each of those years an employing authority must make payments to the appropriate fund on account of the amount required for the whole year.

(3) Those payments on account must –

(a) be paid at the end of the intervals determined under regulation 69 (payment by Scheme employers to administering authorities); and

(b) equal the appropriate proportion of the whole amount due under paragraph (1) for the year in question.

(4) An employer’s contribution for any year is the primary percentage for that year of –

(a) the pensionable pay on which contributions have been paid into the fund by active members in accordance with regulations 9 to 12 and 14 (contributions), except where sub-paragraph (b) applies; and

(b) the assumed pensionable pay in respect of members on leave due to sickness or injury or reduced contractual pay or no pay or on child-related leave,

increased or reduced by any secondary rate adjustments specified for that employer for that year in the rates and adjustments certificate.

- (5) The primary percentage is the primary rate of the employer's contribution specified in that certificate expressed as a percentage of the pay of its employees who are active members."

21. Regulation 68 relates to employer's further payments; and Regulation 69 importantly relates to payment by "Scheme employers" to "administering authorities". Regulation 69(1) provides (emphasis added):-

"Every Scheme employer must pay to the appropriate administering authority on or before such dates falling at intervals of not more than 12 months as the appropriate administering authority may determine –

- (a) all amounts received from time to time from employees under regulations 9 to 14 and 16 (contributions);
- (b) any charge payable under regulation 68 (employer's further payments) of which it has been notified by the administering authority during the interval;
- (c) a contribution towards the cost of the administration of the fund; and
- (d) any amount specified in a notice given in accordance with regulation 70 (additional costs arising from Scheme employer's level of performance);  
..."

### **MECHANICS**

22. Every 3 years a Valuation is performed by the "Actuary". That Valuation concludes with a rates and adjustments certificate. This certificate specifies each Scheme employer's pension contributions over the following three years.

23. The certificate is made up of two parts:-

- (a) A percentage the employer applies to "pensionable pay", as defined; and
- (2) A cash sum which contributes to paying off the accumulated deficit.

### **ANALYSIS**

24. In my opinion:-

- (1) The relevant provision so far as powers are concerned is Regulation 30 of the CFR;
- (2) That enables (indeed requires) an authority to charge to its General Fund (GF) the amounts which are "payable for that financial year";

- (3) That begs the question as to what amounts are payable for “that financial year”;
- (4) For this one turns to Regulation 67(1) of the Regulations;
- (5) This provides that the amount is “as calculated in accordance with” the rates and adjustments certificate.
- (6) One therefore turns to the rates and adjustment certificate prepared by the Actuary;
- (7) What this is to contain is governed by Regulation 62(4)-(7) of the Regulations;
- (8) Whereas the Valuation is to be triennial, and, correspondingly, the certificate of rates and adjustments is to cover a period of three years, nonetheless the certificate itself must specify amounts “for each year”;
- (9) The Actuary can –
  - (i) specify deficit contributions as being payable in advance for three years; and
  - (ii) specify the payment as being net of a discount for accelerated payment; and
  - (iii) specify no definition contribution payment as being due in the second or third years; and
- (10) If the Actuary so certifies, an authority may, make payment and account for the payment in accordance with the Actuary’s certificate.

### **GPOC**

25. The provisions governing GPOC are Sections 108 inclusive in Chapter 1 of Part 1 of LA 2011. GPOC has the following features:-

- (1) The power is to do anything “that individuals generally may do”;
- (2) The breadth of “things that an individual may do” is emphasised by the statement that Section 1(1) applies to things which an individual may do even though they are “in nature, extent or otherwise … unlike anything” that the authority may do, apart from Section 1(1) or unlike anything that other public bodies may do (Section 1(2));

- (3) Subject to some exceptions, the power to do something is a power to do it “in any way whatever”, including power –
- (i) “to do it anywhere in the United Kingdom or elsewhere”,
  - (ii) “to do it for a commercial purpose or otherwise for a charge, or without charge, and
  - (iii) “to do it for, or otherwise than for, the benefit of the authority, its area, or persons resident or present in its area” (Section 1(4)).

26. GPOC is importantly expressed not to be limited by the existence of any power which to any extent overlaps it (Section 1(5)).

27. Limits are, however, placed on GPOC. Section 2 of LA 2011 expressly limits GPOC in several ways:-

- (1) If an authority exercises GPOC in a way which overlaps with a pre-commencement power the new power is subject to the same ‘restrictions’ as the pre-commencement power (Section 2(1));
- (2) GPOC does not enable a local authority to do anything which it is unable to do because of a –
  - (i) pre-commencement limitation (Section 2(2)(a)); or
  - (ii) a post-commencement limitation which is expressed to apply
    - (a) to GPOC;
    - (b) to all of the authority’s powers, or
    - (c) to all of the authority’s powers with exceptions which do not include GPOC.

28. The Regulations, however:-

- (1) Are post-commencement; and
- (2) Are not expressed to apply in any of the above ways.

29. The above provisions in the Regulations reflect a statutory regime which provides for a minimum of annual payments. The question is, for the purpose of the reasonable and proper exercise of power, whether these provisions prohibit exercise of GPOC by making advance payment of contributions.

30. As indicated above, Regulation 67:-

- (1) Provides for the minimum that must be paid; and
- (2) The latest time by which it must be paid; but
- (3) Is otherwise flexible, in particular as to intervals between payments, subject to the contributions for each year being met, and not being delayed, and subject to Regulation 69.

31. Regulation 69:-

- (1) Is an “on or before” provision, which therefore enables “before” as well as “on”, and prohibits only “after”; and
- (2) Requires payments to be made not more than 12 months after relevant events.

32. I for my part see no reason why a payment in one year cannot be counted as a payment for another year, provided that the payment is either in that year or before that year but not after it.

33. I do not regard there as being:-

- (1) Any limitation upon advance funding; or
- (2) Any improper circumvention of regulatory requirements.

34. I do regard the question as being one of reasonableness, proportionality and prudence.

### **EMPLOYEE CONTRIBUTIONS**

35. Employee contributions are deducted in accordance with Regulations 9-14 inclusive of the Regulations. The amount a member pays depends on what earning band they fall into.

36. It is Regulation 69, referred to above, that sets out when these contributions must be paid over to the appropriate “administering authority”. Regulation 69(1) is quoted above. Regulation 69(2) goes on to say that a Scheme employer must pay the contributions mentioned above within the prescribed period referred to in Section 49(8) of PA 1995, which provides:-

“Where on making a payment of any earnings in respect of any employment there is deducted any amount corresponding to any contribution payable on behalf of an active member of an occupational pension scheme, the amount deducted is to be paid, within a prescribed period, to the trustees or managers of the scheme.”

37. Regulation 16 of the Occupational Pension Schemes (Scheme Administration) Regulations 1996 (1996/1715) says:-

“(1) Save as provided in paragraph (2), the prescribed period for the purposes of section 49(8) of the 1995 Act (amount deducted from earnings to be paid to the trustees or managers of the scheme within a prescribed period) is –

- (a) where the contribution payable on behalf of an active member is paid to the trustees or managers of the scheme by means of an electronic communication, 22 days; or
- (b) in any other case, 19 days,

commencing on the day following the last day of the month in which the amount is deducted from the earnings in question.”

38. Regulation 69(3) requires that every payment must be accompanied by a statement showing the total pensionable pay received by members during the period covered by the statement, the total employee contributions deducted from the pensionable pay and so on.

## EMPLOYER CONTRIBUTIONS

39. Employer contribution rates are set every three years at the triennial fund valuation. There is no requirement under the Regulations for a different primary rate to be set for each employer in the fund.

40. Regulation 62 of the LGPS 2013 Regulations, referred to above, provides that on the valuation date (31 March) each administering authority must obtain:-

- (1) An Actuarial Valuation of the assets and liabilities of its pension fund;
- (2) A Report by an Actuary in respect of the Valuation; and
- (3) As noted above, a rates and adjustments certificate.

41. The rates and adjustment certificate will detail both the primary and secondary rate. The primary rate is the amount in respect of future accrual. The secondary rate represents the amount the primary is adjusted by for the circumstances peculiar to that employer, so usually the deficit contribution amount. The primary rate must be specified as a percentage, whereas the secondary rate can be a percentage or a monetary amount.

42. What Regulation 67 of the Regulations does is to provide that a Scheme employer must contribute to the appropriate fund in each year the appropriate amount that is covered by a rates and adjustment certificate under Regulations 62 or 64 (where the valuation certificate is revised). Regulations 67(2) and 3(3) say that during each of the three years a Scheme employer must make payments to the appropriate fund on account of the amount required for the whole year. The amounts must be paid in accordance with Regulation 69, and must equal the whole amount due for the year. Regulation 67(4) to (6) then go on to say how the amount is calculated; and Regulation 69 provides that employer contributions must be paid over to the appropriate administering authority at intervals determined by the administering authority, but at least every year.

## **THE QUESTIONS**

43. I am asked four questions. They are:-

- (1) Is the prepayment of primary employer and employee contributions permissible under the Regulations and overriding legislation?
- (2) If it is permissible what information should be provided, and when, under Regulation 69(3) of the Regulations?
- (3) If it is permissible for either primary employer and/or employee contributions to be pre-paid, how many years can be pre-paid in the three-year valuation period?

(4) What, if any, legal restrictions relating to accounting for contributions could be anticipated as a result of prepayment?

44. As my Instructions note, if the prepayment of contributions is permissible the LGPS administering authority will need to have robust internal controls in place to ensure the correct amounts are collected. They will need to project how much the total pensionable pay is likely to be in each year and ensure that is compared to the actual pensionable pay at the end of each year, with any necessary adjustments being made.

### **FIRST QUESTION**

45. My answer is: "Yes".

46. I do not distinguish for this purpose between employer contributions and employee contributions or amongst employer contributions. My opinion is that the source of vire for prepayment is GPOC and that there is no limitation for GPOC purposes by reference to other legislation. Employers can to my mind pursuant to GPOC pay not only employer contributions but also employee contributions, the latter being based on a reasonable estimate of pensionable pay. I do not see any requirement for the administering authority to have to agree. I consider that what needs to be put in writing for this to happen is for the employer to notify the administering authority of the payment being chosen to be made. In particular, I do not regard either PA 1995 and/or the Regulations referred to in para 37 above as prohibiting the use of GPOC or the prepayment of either employer or employee contributions

47. I for my part see no reason why a payment in one year cannot be counted as a payment for another year, provided that the payment is either in that year or before that year but not after it.

48. I do not regard there as being:-

(1) A limitation upon advance funding; or

(2) Any improper circumvention of regulatory requirements.

49. I do regard the question as being one of reasonableness, proportionality and prudence. I do not believe that a payment must be made in each of the three years covered by the rates and adjustment certificate.

50. I conclude that, in my opinion, the proposal is intra vires and lawful, subject to proper accounting treatment, addressed below.

### **SECOND QUESTION**

51. As regards what information should be provided, and when, under Regulation 69(3):-

- (1) Reference should be made to the detail in Regulation 69(3) as to what information should be provided; and
- (2) The information must be provided at the time of the statement.

### **THIRD QUESTION**

52. In my opinion, as to how many years can be pre-paid in the three-year valuation period, this is connected with accounting treatment. The timing of the payment affects both the level of discount and the risks associated with the payment, and therefore what is reasonable, proportionate and prudent. I do not believe that a payment must be made in each of the three years covered by the rates and adjustment certificate. However, I do not approve an arrangement by which the vast bulk of the monies is paid in year 1, with notional payment in years 2 and 3.

### **FOURTH QUESTION**

53. In my view, given that the total amount payable in advance is less than the estimated totals payable on a year basis, the rates and adjustment certificate should specify not only the primary and second rates for each year, but also the rate/amount for advance payments. Moreover, in my view the advance payment can be treated as a pure cash transaction, which does not result in all of the costs being accounted for as early revenue expenditure in the income and expenditure account, but would enable the expenditure to be accounted for in the relevant financial years. The advance payment is made to secure greater value for money, and

is not intended to change the accounting treatment of payments. Note “payable” in Regulation 30 of the CFR.

54. As to whether the charge to the GF should reflect the discount awarded for the payment, in my opinion it should. That is because I consider that:-

- (1) An Explanatory Note at the bottom of a certificate is part of the certificate;
- (2) The body of the Certificate and an Explanatory Note must be considered as a whole; and
- (3) The prepayment and discount should be apparent on a fair reading.

55. I do believe that it is better if the position with regard to the prepayment and discount are made as explicit as possible. Any rates and adjustment certificate should reflect the actual payment arrangements.

56. I also consider that any overpayment of contributions, resulting from actual pensionable pay being lower in the event than the forecast used when determining the prepayment figure, would be charged to the GF. I do not regard this feature as taking what is “payable” outside Regulation 30(1) of the CFR.

57. I do not consider that it is unreasonable in the Wednesbury sense, or contrary to fiduciary duty, or “best value”, to take the risk of actual pensionable pay over the period covered by the prepayment being significantly different from the forecast used when determining the prepayment figure. Necessarily the best estimate must be made after conducting all due diligence and adopting a prudent approach.

## **CONCLUSION**

58. I shall be happy to discuss any point that may arise and to advise further as required.

**JAMES GOUDIE Q.C.**

11 King's Bench Walk  
Temple  
London EC4Y 7EQ

9 March 2022

**LOCAL GOVERNMENT PENSION  
SCHEME**

**PREPAYMENT OF CONTRIBUTIONS**

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**OPINION**

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