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60-second summary

New Scottish LGPS exit credit regime

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New Scottish amendment regulations regarding exit credits have now been laid. These regulations outline how an administering authority must determine the amount of exit credit due to be paid to an exiting employer. The regulations are due to come into force from 2 April 2025. They do not apply to exit credits that have been paid on or after 1 June 2018 and before 2 April 2025.

How does the current exit regime operate?

Scottish funds are currently obliged to pay out any surplus identified in a cessation valuation **in full** as an exit credit. Funds have no discretion over the amount payable.

What's new?

From 2 April, funds will be required to exercise discretion over the amount of any exit credit payable to a ceasing employer. The new regulations mirror those currently in force in England & Wales with exception of an additional 'tartan' factor (see (d) below). When exercising its discretion, a fund must have regard to:

a. the extent to which there is an excess of assets in the fund relating to that employer over the liabilities;
b. the proportion of this excess of assets which has arisen because of the value of the employer's contributions;
c. any representations to the administering authority made by the exiting employer;
d. any guidance or statement specified under regulation 56(4), or any other guidance relating to the preparation of a funding strategy statement issued or endorsed by the Scottish Ministers; and
e. any other relevant factors.

Factor (d) refers to guidance that should be adhered to when preparing the Funding Strategy Statement (FSS). The current FSS guidance says relatively little about the determination of exit credits; it's mentioned under paragraphs 90 & 91 and focuses on the need for a fund to be clear about the process and decision-making principles. It's our understanding that further guidance from Scottish Ministers and/or the Scottish Scheme Advisory Board (SSAB) may be forthcoming – watch this space.

What does this mean in practice?

Scottish funds can look to their friends south of the border for insight about how these regulations are being applied in practice. The requirement to exercise discretion within exit credit regulations came into force in England and Wales around 5 years ago.

A diverse range of determination approaches has emerged in the south. In particular, factor (b) above can be interpreted in different ways. For example, some funds cap the exit credit amount at the level of contributions paid in by the ceasing employer over the period of its participation in a fund (often rolled up with interest). However, other approaches are valid – a common approach is to compare the total value of contributions paid by the ceasing employer to the total value of its assets at cessation and apply the resulting percentage to the cessation surplus to arrive at an exit credit amount. Some funds have also added exit credit principles to their FSS and cessation policies to help employers understand the sort of factors that may apply during the determination process.

Taking the time to identify which approach works for your fund is crucial. Please bear in mind that a 'one size fits all' approach may not work across all employers, and that each exit credit determination should reflect the circumstances of the departing employer. The fund's governance and approval process around the determination decision should also be considered.

Interaction with the 90-day cessation guarantee

As a reminder, recent changes to the Scottish Regulations (61(2A)) introduced a requirement for indicative cessation valuations to come with a 90-day guarantee. If an employer requests an indicative cessation and ceases participation in a fund within 90 days of the effective date of the request, the indicative position **must** be used in substitution for any valuation at the actual cessation date. Funds may want to manage any additional risks posed by the 90-day guarantee period via the exit credit determination process.

What should you do now?

There are a few steps we would recommend you do now in preparation for the new regulations coming into play on 2 April:

1. Familiarise yourself with the new regulations and references to exit credits in your FSS.
2. Agree and document your policy on determining exit credits – ensuring you update your FSS and any cessation policy.
3. Ensure you consider different employer types e.g. the approach you adopt for contractors may differ from other employer types. Make sure to document the approach for each.

Please speak to your fund actuary if you need implementation support.

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