CT/19/72
Devon Pension Board
15th July 2019

LGPS UPDATE

Report of the County Treasurer

Please note that the following recommendations are subject to consideration and determination by the Board before taking effect.

Recommendation: The Committee notes the latest LGPS Update

1. Introduction

1.1. This report is brought to the Pension Board to provide an update on some of the latest issues affecting the LGPS. In particular, the report focuses on the Good Governance Project launched by the Scheme Advisory Board and various issues relating to actuarial valuations.

2. The Good Governance Project

2.1. The Good Governance Project is a project to look at the governance structures within LGPS and whether any changes to regulations are required to improve governance. The project has been initiated by the LGPS Scheme Advisory Board, with a view to addressing perceived conflicts of interest between the management of the pension fund and the management of the administering authority.

2.2. Despite the lack of objective evidence that the current arrangements have caused any significant governance issues, consultants Hymans Robertson have been asked to produce a report. The project is considering the four options set out below. It is concerning that the status quo is not being considered as an option. The four options are:

1) **Improved practice** - Introduce guidance or amendments to LGPS Regulations 2013 to enhance the existing arrangements by increasing the independence of the management of the fund and clarifying the standards expected in key areas.

2) **Greater ring-fencing of the LGPS within existing structures** - Greater separation of pension fund management from the host authority, including budgets, resourcing and pay policies.

3) **Use of new structures: Joint Committees (JC)** - Responsibility for all LGPS functions delegated to a JC comprising the administering authority and non-administering authorities in the fund. Inter-authority agreement (IAA) makes JC responsible for recommending budget, resourcing and pay policies.

4) **New local authority body** - An alternative single purpose legal entity that would retain local democratic accountability and be subject to Local Government Act provisions.

2.3. The first two options would result in the least change and would look to provide greater legal clarification on the fiduciary and statutory duties of key individuals within LGPS funds, as well as looking at issues such as:

- The separation of the Pension Fund's statement of accounts, such that it was no longer included in the administering authority's statement of accounts.

- New guidance on representation on pension committees and expected levels of training for those on pension committees and officers with an LGPS role.

- Greater transparency around charges to the fund in respect of support services provided by the host authority, for example legal support, HR and procurement.

- Delegation of polices over certain HR matters such as recruitment and the payment of market supplements to the pension committee, rather than being automatically aligned to the administering authority's HR policies.

2.4. Options 3 and 4 would involve setting up new structure, and in the case of option 4 would set up a new authority to manage the pension fund, outside of the existing administering authority. This would more clearly remove the perceived conflicts of interest, but the setting up of new structures would add significant costs to the management of the fund.

2.5. Both the County Treasurer and the Assistant County Treasurer, Investments have been interviewed by Hymans Robertson as part of the project. In addition, the Chairman, together with officers, has attended a seminar held by Hymans Robertson.

2.6. While clearer guidance and transparency in respect to some of the governance arrangements, as set out in paragraph 2.3 above, would be welcome, officers believe that options 3 and 4 would bring further significant change in addition to the ongoing change resulting from the investment pooling initiative. They would also add significant additional administrative costs at a time when the Government focus has been on reducing cost.

2.7. Hymans Robertson are due to present their report to the Scheme Advisory Board later in the year.

3. Actuarial Valuations

3.1. As the Committee will be aware, the Fund Actuary, Barnett Waddingham, is currently carrying out the 2019 triennial actuarial valuation of the Fund. There have a been a number of factors since 2016 that will impact the assumptions made by the Actuary – slowing of improvements in longevity, outperforming markets which may lead to lower returns in the future, a change in the assumptions used by government to cost unfunded schemes. Barnett Waddingham are currently reviewing these factors and propose to give us an early indication of the likely assumptions that they will adopt for the formal valuation. Any further information on this will be reported orally at the meeting.

3.2. Following the current valuation the Government is proposing to synchronise the timing of future valuations to coincide with the valuations of the unfunded public sector pension schemes. The other public sector schemes have a four year cycle of actuarial valuations and last had a valuation in 2016, at the same time as the LGPS. Their next valuation is therefore due in 2020, and the following one in 2024. The Government has therefore issued a consultation on moving to a four yearly cycle from 2024 onwards with an LGPS valuation in 2024.

3.3. There are two key elements of the Government's consultation:

- The Government has recognised that if the next LGPS valuation is in 2024, then that would leave a five year gap between the current 2019 valuation and the next one. It could be argued that five years is a long time and a lot can happen in relation to the funding position in that time. On the other hand, pensions is considered a long term issue and before triennial valuations were introduced valuations took place every five years. Therefore, the Government is consulting on whether to have a five year gap, or whether to have a valuation in 2022, on the basis of the current three year cycle, but then have just a two year gap in order to synchronise valuations in 2024. A two year gap between valuations would require more resources to administer.

- The Government also recognises that by extending the cycle to four years there may be circumstances in which that may be too long if issues arise that will impact the funding position. Therefore it is consulting on providing the option for Funds to decide to have an interim valuation between the scheduled four yearly valuations. This would only be allowed in exceptional circumstances and would require the permission of the Secretary of State.

3.4. The main motivation behind the move to synchronise the LGPS valuation cycle with the unfunded public sector schemes is the Government's cost cap mechanism. This is the mechanism by which the Government Actuary's Department (GAD) assesses the affordability of the pension scheme and whether any changes need to be made to bring the cost back in line with the Government's expectations. The Government wants to be able to conduct the assessments of all the public sector pension schemes at the same time.

3.5. GAD have published the results of their assessment of the affordability of the LGPS based on the 2016 Valuation. This indicated that the scheme was less expensive than the benchmark position, and as a result some improvements to benefits, and some reductions in employee contributions for low earners, were proposed to bring the cost of the scheme back in line with the benchmark. However, these changes have been put on hold as a result of a legal challenge to revised scheme regulations in the Judges' and Firefighters' pension schemes.

3.6. The legal challenges, known as the McCloud and Sargeant cases, are challenging the legality of protections put into revised scheme regulations in 2015 in the Judges' and Firefighters' pension schemes for those nearing retirement, on the basis that they are illegal due to age discrimination legislation. These cases are likely to have implications for the LGPS regulations which put in place similar protections for those nearing retirement when the CARE (Career Average) scheme was brought in in 2014.

3.7. The courts have ruled in favour of McCloud and Sargeant and the Government has been declined an appeal. We now await the outcome of negotiations and Employment Tribunal cases which will determine how the situation will be remedied. The final outcome of the case could result in the scheme rules being changed to remove the alleged discrimination, which would then result in additional liabilities for the LGPS. This would therefore increase the cost of the scheme above that assessed by GAD when they carried out their review. The Fund Actuary will take the recent rulings into account when he undertakes the 2019 valuation.

4. Further and Higher Education Employers

4.1. The consultation outlined in section 3 that largely focuses on the valuation cycle also includes a proposal to remove the requirement for further Education corporations, sixth form college corporations and higher education corporations in England to offer new employees access to the LGPS. Each corporation will have the flexibility to decide whether to offer the LGPS to all or some eligible employees.

4.2. In recent years there have been a number of changes to the further education and higher education sector. These have resulted in the sector being removed from the General Government Sector and a new statutory insolvency regime has been introduced meaning that, for the first time, corporations could become legally insolvent. These bodies are responsible for determining their own business models and ensuring that their financial positions are sound. It is therefore argued that these bodies may value greater flexibility over their pension arrangements.

4.3. Some of these bodies are among the largest employers in the Devon fund. Whilst the proposals provide protection and continued access to the LGPS for existing staff, there is no doubt that over time these potential changes could have an impact on the fund as the level of new members could fall in the future.

5. Conclusion

5.1. The Investment and Pension Fund Committee has resolved to submit a response to MHCLG highlighting concerns about the proposed changes to regulations with regard to further and higher education employers. The committee expressed a preference to go through to 2024 for the next actuarial valuation after 2019, rather than have a further valuation in 2022. A response will be submitted by the County Treasury in consultation with the chair of the Investment and Pension Fund committee following circulation to committee members for comment by the deadline 31st July 2019.

Mary Davis

Electoral Divisions: All
<u>Local Government Act 1972</u>
<u>List of Background Papers - Nil</u>
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