MUNICIPAL YEAR 2019/2020 REPORT NO. 151

MEETING TITLE AND DATE:
Pension Policy & Investment Committee
21st November 2019

REPORT OF:
Director of Finance

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Agenda – Part: 1	**Item: 4.4**
Subject: LGPS (Local Government Pension Scheme) Current Issues **Wards: All** **Key Decision No:**	
Cabinet Member consulted:	

1. EXECUTIVE SUMMARY

i) This report provides an update on several general developments affecting the Local Government Pensions Scheme. One of the functions of the Committee is to meet the Councils duties in respect of the efficient management of the pension fund.

ii) The Committee's consideration of the information in the report contributes towards the achievement of the Council's statutory duties.

iii) This report outlined the Competition and Market's Authority (CMA) Order on Fiduciary Management and Investment Consultants. CMA has set a deadline of 10th December 2019 for funds to set their investment advisors these strategic objectives. If they are not in place by 10th December administering authorities could be open to being fined if they accept investment advice.

iv) It covers the Publication of the Good Governance (SAB Report), the legal opinion obtained by LGA on the potential transfer from Equitable Life, updates on McCloud and the recent Supreme Court announcement, several updates from the Pensions Regulator (TPR) and MHCLG are also noted.

2. RECOMMENDATIONS

Members are asked:

i) to note the contents of the report which covers the following matters:
- CMA Order on Fiduciary Management and Investment Consultants;
- The Pensions Regulator's LGPS Engagement Report;
- McCloud and Cost Management -Further Developments;
- Actuarial Valuation – Update;
- SAB Publishes Good Governance Report;
- Survivor Benefits;
- GAD Section 13 review and data collection;
- TPR proposes a single combined code of practice;
- Consultation on Future of Trusteeship;
- Update on MHCLG Consultations;
- PASA Launches DB Transfer Guidance; and
- AVC (Additional Voluntary Contribution) Updates

ii) to consider and approve the strategic objectives set for the Fund Investment Consultant as set out in Appendix 2.

3. BACKGROUND

CMA Order on Fiduciary Management and Investment Consultants

3.1 On 10 June the Competition and Market's Authority (CMA) published the Investment Consultancy and Fiduciary Management Market Investigation Order 2019. In summary, the Order defines Fiduciary Management (FM) services and obliges pension schemes to formally tender for such services. It also obliges pension schemes to set objectives for their Investment Consultancy (IC) providers as well as placing a variety of new obligations on FM and IC service providers.

3.2 In early July the LGPS SAB in England and Wales issued a briefing note to raise awareness of the Order. It refers to the potentially "significant consequences" for LGPS pools where the pool companies are caught by the definition of Fiduciary Management service providers and they cannot use the exclusion for pension scheme owned companies.

3.3 However, on 29 July, the Department of Work and Pensions (DWP) published a consultation on regulations to bring the recent CMA Order into legislation. That consultation, which runs to 2 September, states in Chapter 2 that the scope of the draft regulations does not include the LGPS in relation to Fiduciary Management (FM) service providers. The requirement to set objectives for Investment Consultancy (IC) providers remains, with a deadline for doing so of 10 December 2019.

3.4 Whilst the DWP regulations will not apply to LGPS, it is expected that similar regulations will be adopted by the Ministry for Housing, Communities and Local Government (MHCLG) in due course.

3.5 Once passed into law, the Pensions Regulator (tPR) will be able to oversee the new duties on Pension Scheme Trustees. It is currently expected that this will confirm the following requirements for Pension Scheme Trustees:

- Set objectives for their IC service.
- Review the performance of each IC provider at least every 12 months.
- Review the objectives themselves at least every three years, and without delay following any significant change in investment policy.

3.6 As explained in the Scheme Advisory Board's briefing note, dated 1 August 2019, the Order, when finalised, extended its application to the LGPS. Subsequently, the Scheme Advisory Board has stated that the requirement to set strategic objectives for the investment consultancy providers also will apply to the LGPS.

3.7 Further information is attached as Appendix 1 to this report, the Scheme Advisory Board's briefing note by way of background. In the absence of agreed objectives, continuing to obtain Investment Consultancy Services (as defined in the Order), from 10 December 2019, would place the

administering authority in breach and potentially liable to penalties. Given the short timeframe, it is therefore important to bring this matter to the Committee attention and hence officers are proposing a simplified set of strategic objectives relating to the services to which the Order applies.

3.8 We would need to engage with the IC further before and/or after 10 December to refine and develop the objectives to meet our requirements. Ultimately, the onus rests with the London Borough of Enfield, the administering authority of the Fund to set the appropriate objectives.

3.9 Officers recognised the basis of setting the strategic objectives for the investment consultancy provider would, as far as reasonably possible, align with the strategic objectives of the Fund. And so, it can be difficult to measure the value added by investment advice as this is closely linked to the Fund's own decision-making and the timing of implementing those decisions.

3.10 Having considered the draft guidance from The Pensions Regulator (tPR), which is attached to this report as Appendix 2. The Scheme Advisory Board understands that the MHCLG may come forward with some provisions for LGPS authorities, and their attached briefing note addresses this in more detail. It is therefore worth noting that whilst The Pensions Regulator's draft guidance does not specifically cover the LGPS, it does provide a useful guide in the absence of any specific LGPS regulation.

3.11 The Committee will need to agree the objectives prior to 10 December 2019. we have provided some relevant objectives for discussion.

3.12 It is therefore recommended that the Committee consider and ratify the objectives set out at Appendix 3 of this report. And if the Committee has any comments and or proposed changes to these objectives, this would be share with the current Investment Consultant for their review to ensure the objectives are consistent and practical.

The Pensions Regulator's LGPS Engagement Report

3.13 Earlier this month The Pensions Regulator (TPR) published its findings following engagement with 10 LGPS funds between October 2018 and July 2019. TPR indicated that they saw evidence of good practice across the LGPS funds. They also outline key areas for improvement across the scheme.

3.14 74% of schemes had all six of their key processes in place, an improvement on previous years. However, TPR found it disappointing that the remainder of schemes still did not have all six of these simple measures in place.

3.15 The six measures are:

- Pension Board meetings and Board membership
- Knowledge and understanding
- Risk registers

- Cyber security
- Collecting data and Data Quality
- Annual benefit statements

3.16 In conclusion, the pattern of findings this year indicates that while pension boards have managed to drive improvements in some areas, they continue to struggle in many others. The locally administered schemes appear to find it particularly hard to meet their responsibilities.

3.17 Pension boards have two fundamental responsibilities - to oversee both the governance and administration of the scheme. A board that is failing to meet its basic responsibilities by not having administration as a feature of every meeting is failing in one of its fundamental functions.

3.18 TPR are pleased to see that more schemes are giving administration the attention it deserves, with three-quarters of schemes considering it at every pension board meeting in the previous 12 months. TPR still see some space for improvement, however. It is notable that most of the complaints received by schemes continue to stem from poor administration.

3.19 This might be around disputes or queries about the amount of benefit paid, slow or ineffective communication, delays to benefit payments, or inaccuracies or disputes around pension value or definitions. TPR urges Pension boards to continue to ensure that administration performance indicators are considered on every agenda to identify persistent and emerging issues, and to advise the scheme manager to make improvements.

Actuarial Valuation - Update

3.20 Work is now in full swing for the 31 March 2019 actuarial valuations. Membership data has been submitted and most Funds will now have received snapshot figures providing an indication of what lies ahead.

3.21 Generally, it has been an improved funding levels, reflecting strong investment returns since the 2016 valuations and a slowdown in the rate of future improvements in life expectancy. However, the indications for lower expected investment returns going forwards, combined with the impact of the McCloud Judgment have tempered this and are likely to lead to a higher rate of primary (future benefit accrual) contributions, all else remaining equal. The actual position will depend on the specific circumstances of the Fund including any investment strategy changes and membership movements.

3.22 Whilst there have been further developments in relation to the McCloud Judgment (see article below), considerable uncertainty remains and a definitive conclusion on what this means for Scheme benefits and the impact on Cost Management is not expected ahead of the 2020 deadline for completing the 2019 valuations.

3.23 The SAB's view remains that the current benefit design as set out under the existing LGPS Regulations should be used to set employer contribution

rates, but that Funds and employers should be mindful of the potential extra liabilities when setting their contribution rates at the 2019 valuation. The full impact of McCloud/Cost Management would then be reflected in the next valuations (expected to be 2022). Funds will therefore need to consider their policy for dealing with the uncertainty and document this. Our Fund Actuary will be preparing figures showing the impact of a McCloud scenario in addition to providing results based on the current Scheme.

3.24 A key feature of the 2019 valuations will be one of uncertainty (particularly in light of Brexit and McCloud) and this serves to highlight the importance of considering overall risk as part of the valuation process. One area for consideration by Funds will be whether improved funding levels could provide an opportunity to reduce investment risk, leaving the Fund better protected in the future. Any investment strategy changes would need to be fully integrated with the funding strategy and our Consultant would work with us to achieve this.

3.25 There is a busy period ahead as we work with Funds to complete the 2019 valuations. As a reminder, the key next steps will be to:

i) arrange preliminary results meetings in September/October to discuss the preliminary valuation results and book meeting(s) for the Employer consultation exercise;

ii) draft updated Funding Strategy Statements (incorporating admission/termination/McCloud policies, etc.) and plan the forthcoming consultation exercise;

iii) review/develop the risk management framework, gather information and carry out additional analysis as needed, e.g. covenant assessments, asset/liability modelling, investment strategy reviews, etc.

McCloud and Cost Management -Further Developments

3.26 On 27 June, the Supreme Court denied the Government's request for an appeal in the McCloud and Sargeant age discrimination case ("McCloud") and the Government subsequently confirmed on 15 July that remedies relating to the McCloud judgment will need to be made in relation to all public service pension schemes. The SAB Q&A to the McCloud Judgment is below: http://lgpsboard.org/index.php/structure-reform/cost-management/ccmcloud

3.27 The details of how the Local Government Pension Scheme will need to be change are yet to be determined. It will return to the Employment Tribunal for remedy and so a final position may not be confirmed for months, if not years.

3.28 As stated above, Funds need to consider their policy on how the effects of McCloud will be taken into account for the ongoing valuations. Further considerations relate to the treatment for accounting (FRS/IAS) figures and any employer exits that arise in the interim until the remedy is confirmed.

3.29 Audit firms have required an appropriate allowance for the potential impact of McCloud for all but the minority of cases (where the impact can be argued to be immaterial). Funds could devise a tiered approach for undertaking the additional calculations for Employers, depending on the level of detail required. In the case of Enfield Council, between the GMP and McCloud cases, the pension liability increased by £37m.

3.30 For Employer exits, in determining their policy on the allowance for McCloud, Funds will need to consider wider issues including the covenant of the Employer in question and whether the termination involves a refund to the Employer or a payment to the Fund.

3.31 The overarching view is that the impact of the potential McCloud liabilities should be allowed for in some way that is appropriate.

SAB Publishes Good Governance Report

3.32 The SAB commissioned the governance report to examine the effectiveness of current LGPS governance models and alternatives or enhancements to existing models to strengthen LGPS governance.

3.33 The key proposals from the report were for an approach which specifies minimum standards including robust conflict management, assurances on administration/other resources, explanation of policy on employer/scheme member engagement and regular independent review of governance. Enhanced training requirements for Officers, S151s and S101 committee members, updated guidance and better signposting to requirements were also proposed.

3.34 The project team are now working on a plan to implement the proposals which will be presented to the SAB in November. Scheme stakeholders will be given the opportunity to comment on the Board's recommended implementation plan before any formal approach is made to MHCLG Ministers for changes to the Schemes' regulations or guidance.

GAD Section 13 review and data collection

3.35 GAD have now finalised their data collection requirements that they request in order to carry out their section 13 review of the LGPS Funds. This has been through several iterations and discussion with representatives of the firms of fund actuaries. Administering Authorities should expect to receive confirmation shortly of the spreadsheet that needs to be filled in and will be asked to request this information from their actuary. The deadline for provision of this information (including the funding position on the standardised basis) is 30 April 2020, which is welcome as it gives more time to carry out the necessary calculations than at the 2016 valuation. GAD will also be requesting membership data directly from all funds, and this is likely to be required in September 2019.

3.36 In addition, and in response to one of the recommendations in the section 13 report following the 2016 valuation, there will be a "dashboard" included in

the formal valuation reports, probably in the form of an additional appendix. This will include key information from the valuation and the results on the standardised basis and is intended to help lay readers compare funds and funding strategies. The information to be included in the dashboard was proposed by SAB and has been refined following discussions between GAD, SAB and the firms of fund actuaries.

Survivor Benefits

3.37 In July Guy Opperman, Minister for Pensions and Financial Inclusion issued a ministerial written statement. It confirms that, following a review of survivor benefits required under the Marriage (Same Sex Couples) Act 2013, no changes are to be made to legislative provisions. It notes that, following the decision in the case of Walker v Innospec, it is now clear that same-sex civil partners or spouses are entitled to survivor benefits in the same way as opposite sex spouses, and outlines the steps being taken to reflect the judgment for public sector schemes.

3.38 Also, in July the LGPC Secretariat issued a new LGPS Survivor Membership Technical Guide. It incorporates recent changes to the provision for survivor benefits including the LGPS (Miscellaneous Amendment) Regulations 2018 [SI2018/1366] which addresses the Walker v Innospec case. The guide is available on www.lgpsregs.org

TPR proposes a single combined code of practice

3.39 TPR released a statement indicating that it intends to make changes to its existing Codes of Practice (COP). Over the next year it will review the codes to reflect the IORP II Governance amendments – and states that this is expected to involve combining the content of the 15 current codes into a single, shorter code. That will include COP No. 14 for Public Service Pension Schemes. TPR is planning to launch a formal consultation later in the year, but before that, it will seek feedback on the proposed design and content. Trustees will need to be able to demonstrate that they have an effective system of governance within 12 months of publication of the updated code.

Consultation on Future of Trusteeship

3.40 TPR issued a consultation on 2 July entitled "Future of Trusteeship and Governance" with responses required by 24 September. It includes proposals around how to reduce the number of poorly governed pension schemes, including by promoting consolidation. The consultation, which also refers to Public Sector Schemes also considers how the trustee model can be made more effective, asking about how to improve and evidence trustee knowledge and understanding, how to improve diversity on boards, the role of accreditation and whether sole trustees can govern effectively.

Update on MHCLG Consultations

3.41 It has been a busy spring and summer so far with consultations on exit payments, New Fair Deal and valuation cycles. A brief recap of the proposals is set out below:

3.42 **£95K cap on exit payments**: the proposed limit to the value of settlement payments that are made to employees when they leave an employer. Payments are normally a lump sum cash payment or shares/share options, but for employers participating in the LGPS, settlement payments will also include the value or "strain" of taking an unreduced pension for members over age 55.

3.43 **New Fair Deal:** Employees whose employment is outsourced from a "Fair Deal employer" will be guaranteed to be able to access the LGPS. The 0option of the new employer establishing a "broadly comparable" scheme as an alternative will, in effect, become redundant.

3.44 **Four-year valuation cycle**: not just as it says on this tin, this consultation also includes proposals for interim valuations, more flexibility for dealing with termination payments, modifications to exit credits and removing the requirement for further education corporations, sixth form college corporations and higher education corporations in England to offer membership of the LGPS to their non-teaching staff for new entrants.

PASA Launches DB Transfer Guidance

3.45 On 8 July 2019 the Pensions Administration Standards Agency (PASA) launched DB transfer guidance. The guidance includes templates for documents to use at different stages of the transfer process and aims to:

i) improve member experience through quicker, safer transfers;

ii) improve efficiency for administrators; and

iii) improve communications and transparency in processing transfers.

3.46 Although compliance is voluntary, it is anticipated that the pensions ombudsman will reference it when reviewing complaint cases as a source of what 'good practice' looks like.

AVC (Additional Voluntary Contribution) Updates

Equitable Life

3.47 As part of their Spring Announcement in 2018, Equitable Life announced their intention to transfer all policies to Reliance Life, with the transfers taking place during the latter part of 2019. Reliance Life has since been rebranded as Utmost Life and Pensions Limited.

3.48 As part of the transfer deal, the Equitable Life With-Profits Fund will close and will be disinvested, initially into a deposit fund, but then into unit linked funds.

3.49 Equitable Life has recently stated that (for most investors in a policy with a 3.5% guaranteed interest rate) the Capital Distribution is now expected to increase further than the 60-70% previously expected, although full details have yet to be confirmed.

3.50 Equitable Life are contacting LGPS Funds with further details of the proposed transfers and over the next few months Funds will need to make a number of decisions. It is recommended that Funds consider obtaining regulated investment advice to make these decisions appropriately.

Prudential

3.51 Following an internal review of lifestyle options available to members, Prudential has decided to fully close their "Optimiser" lifestyle plans later this year. Their review took into account the impact of pension freedom changes in 2015 and also experience of how the AVC Funds were being used by all members (across all Schemes).

3.52 Once the "Optimiser" plans have been fully closed, any funds invested in these plans need to be moved to new arrangements. Members will therefore be invited by Prudential to make a decision as to which lifestyle arrangement.

4. ALTERNATIVE OPTIONS CONSIDERED

i) There is no alternative.

5. REASONS FOR RECOMMENDATIONS

i) For effective and efficient management of the Fund.

ii) There is a requirement for Members of the Pension Board to be kept up to date with current issues and legislative developments as part of their scrutinising role.

6. COMMENTS FROM OTHER DEPARTMENTS

6.1 Financial Implications

i) Achieving good governance is a fundamental part of ensuring the effective and economic running of Enfield Pension Fund.

ii) The financial implications of poor quality data for the Pension Fund are considerable; not only does it raise the risk that member benefits will not be calculated in accordance with scheme regulations, but could also reduce the accuracy of the Fund's actuarial valuation and lead to inefficient management of investment risks. This could result in employers, including the Council, paying insufficient or excessive contributions with a material impact on their

own finances. The involvement of the Pension Regulator (TPR) in this area also raises the risk of financial penalties and reputational damage.

iii) Rectification of the issues outlined in this report will necessarily lead to some increase in administration and governance costs to the Fund. Where additional administration work results directly from the actions (or inaction) of an employer, it is the Fund's policy to recharge these costs to the employer in question.

6.2 **Legal Implications**

i) This

ii) The Pension Fund is required, under Section 4 of the Public Service Pensions

iii) (Record Keeping and Miscellaneous Amendments) Regulations 2014 to hold certain

iv) information about its members. Failure to maintain complete and accurate records

v) could result in the Fund failing to pay benefits in accordance with scheme regulations,

vi) inefficient management of investment risk and potentially excessive or insufficient

vii) contribution rates for employers.

viii) 5.2 The Fund has a legal requirement to report breaches of the law under section 70 of

ix) the Pensions Act 2004. As per its Reporting Breaches Policy, the Fund has deemed

x) 4 breaches experienced with respect to annual benefit statements during the period

xi) 2015-2018 to be reportable and has reported these to the Pensions Regulator

xii) accordingly.

xiii) 5.3 Under the Pensions Committee's terms of reference, it is responsible for 'act[ing] as

xiv) Trustee of the Council's Pension Fund, consider[ing] pension matters and meet[ing]

xv) the obligations and duties of the Council under the Superannuation Act 1972, and the

xvi) various pension legislation'. As such, review of both the Fund's compliance with

xvii) relevant legislation and actions taken to address instances of non-compliance falls

xviii) within the Pensions Committee's remit.

7. KEY RISKS

i) It is important to keep abreast on current issues to facilitate the rigorous and robust management of the Pension Fund for a better, quicker and more effective decision-making process which can lead to better Fund performance and reduction in the contribution required from the Council towards the Fund.

ii) The monitoring arrangement for the Pension Fund and the work of the Pension Board should ensure that the Fund optimises the use of its resources in achieving the best returns for the Council and members of the Fund.

iii) Appropriate scrutiny through the relatively new and growing relationship with the Pensions Regulator (TPR) is helping drive forward improvements.

Background Papers – None

Appendices
Appendix 1 - The Scheme Advisory Board's briefing note
Appendix 2 - TPR Draft Guide on Setting Objectives for Investment Consultancy
Appendix 3 – Draft Enfield Pension Fund Investment Consultant Objectives