Lancashire Local Pension Board
Meeting to be held on Tuesday, 6 July 2021

Electoral Division affected:
(All Divisions);

Regulatory Update

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Executive Summary

This report sets out an update on various pension related regulatory issues to assist Board members to exercise their functions as a member of the Pension Board effectively.

Recommendation

The Board is asked to consider and note the contents of the report.

Background and Advice

1. Restricting exit payments in the public sector (95k Cap)

As highlighted at the last board meeting the Government has indicated that it still intends to reintroduce measures to limit public sector exit payments.

As part of those steps the Ministry of Housing, Communities and Local Government wrote to Chief Financial Officers of councils and combined authorities in England on 9 April 2021, letting them know about a new requirement to provide data on exit payments. Councils will be asked to provide data on all redundancy payments, pension strain payments and other special payments made in consequence of an exit for 2014/15 to 2020/21. The data will be used to inform development and delivery of the Government's policy commitment to end excessively high exit payments in the public sector.

2. 2020 LGPS Scheme Annual report

On 18 May 2021, the Scheme Advisory Board published the 2020 LGPS England and Wales Scheme Annual Report.

Highlights from the report include:
- Total membership up by 4.2% to 6.1 million members compared with 2019.
- Total assets decreased by 4.9% to £276 billion. These assets were invested in:
  1. 68% pooled investment vehicles
  2. 14% public equities
  3. 6% bonds

4. 3% direct property
5. 9% other asset classes.

- The Local Authority return on investment over 2019/20 was -4.8%. This was reflective of the market conditions during the year and set against the UK return of -28.3%.
- The Scheme maintained a positive cash-flow position overall, including investment income.
- Over 1.8 million pensioners paid in the year.
- LGPS liabilities estimated at £291 billion on 31 March 2019. This indicates an overall funding level of 98%.

Full details of the report can be found on the Scheme Advisory Board's website at the following link.
https://www.lgpsboard.org/index.php/schemedata/scheme-annual-report

3. McCloud

As part of the McCloud judgement, proposed changes would mean that a revised underpin protection will apply to all members, regardless of their age, who were active members of the LGPS on 31 March 2012, build up benefits in the 2014 Scheme and do not have a disqualifying break.

In the latest statement issued on 13 May 2021 by Luke Hall, Minister for Regional Growth and Local Government, confirmation was provided around the key changes that the Government will make to the LGPS regulations to remove the unlawful age discrimination. The statement confirms that:

- the age requirement for underpin protection will be removed

- a member will not need to leave with an immediate entitlement to benefits to qualify for underpin protection (i.e. members with a deferred entitlement to a pension will be in scope)

- the remedy period will end on 31 March 2022

- the underpin calculation will be based on final pay at the underpin date, even when this is after 31 March 2022

- there will be two stages to the underpin calculation (this will be undertaken to ensure that where there is a gap between a member's last day of active membership and the date they take their pension, members can be assured they are getting the higher benefit) :

  1. the first on the underpin date – the date of leaving or on the normal pension age in the 2008 Scheme, if earlier
  2. the second when the benefits are paid

  the regulations will be retrospective to 1 April 2014.

It is expected that the Ministry of Housing, Communities and Local Government will issue a full response to the consultation and publish draft regulations later this year.

4. Pension scams

Pension scams are a risk priority for the Fund particularly around pension transfers out of the scheme and there are already a number of checks and procedures that the pension service will complete before agreeing to the transfer out of a member's benefits.

A recent consultation launched by the Department of Work and Pensions proposes new requirements on trustees and scheme managers before a pension transfer can be completed. For the LGPS these transfers would include:

• If the transfer is to an occupational scheme (including a recognised overseas scheme) the member must demonstrate an employment link before the transfer can be completed.

• If the transfer is to a recognised overseas scheme and the member cannot demonstrate an employment link (where that scheme is an occupational scheme), they must prove residency in the same financial jurisdiction as the potential receiving scheme.

• Before any other transfer can be completed, the trustee or scheme manager must decide if there are any 'red flags' that would prevent a transfer. Red flags include:

1. the member was given financial advice by a firm or individual without regulatory permissions
2. the member was contacted out of the blue
3. the member was offered incentives to transfer, and/or
4. the member was pressured to complete the transfer quickly.

• If there are no 'red flags', the trustee or scheme manager must also establish whether there are any 'amber flags' which would include:

1. high risk or unregulated investments in the receiving scheme
2. high or unclear fees in the receiving scheme
3. complicated or unorthodox investment structures
4. overseas investments or advisers based overseas, and/or
5. a high volume of transfers to a single receiving scheme or involving a single adviser or firm.

• If the trustee or scheme manager identifies that 'amber flags' are present, the transfer can only proceed if the member takes scam advice from the Money and Pension Service.

• The member must provide the information needed for the trustees or scheme manager to assess the red and amber flags. If the member does not provide this information, the transfer cannot proceed.

The Department of Work and Pensions has produced a set of standard questions for trustees and scheme managers to use to gather information from the member that they will need to decide whether there are any ‘red flags’ or ‘amber flags’, and these will form part of any new agreed legislation.

5. High Court Judgement on exit credits

A recent claim by a scheme employer in another LGPS fund brought against the Ministry of Housing Communities and the Local Government in relation to the payment of Exit Credits, has now been ruled on by the High Court who have ruled in favour of the Ministry of Housing, Communities and Local Government and determined that an exit credit would not be payable in this case.

Exit credits were introduced into the Scheme rules in 2018 and allowed for a surplus position identified on the termination of an employer in the Fund, to be refunded to that employer in certain situations, generally where another scheme employer was not already picking up and guaranteeing the liability.

The main reason behind the ruling centered around the fixing of a “policy error” by the Ministry of Housing, Communities and Local Government when the regulations underlying the payment of Exit Credits were amended in 2020 to give LGPS Funds the discretion over whether such payments should be made. In cases where risk sharing arrangements existed between the exiting employer and the letting employer which would have protected the exiting employer, had a deficit, and not a surplus, existed on termination.

The amendments introduced in 2020 retrospectively applied to all outstanding cases from May 2018 and this formed the basis of the claim brought against the Ministry of Housing, Communities and Local Government given that the employer in question exited the LGPS prior to 2020. The ruling confirmed that all unsettled credits fall under the 2020 regulations.

In practice, the ruling does not change the position for LGPS Funds in that they will continue to have discretion over whether exit credit payments can be made to exiting employers, as introduced into Regulations last year.

The Lancashire Fund has recently updated their policies dealing with terminating employers and, having taken appropriate actuarial advice, are confident that a robust policy exists to deal with similar cases.

6. Cost control review report published

As reported at the last Board meeting the Government announced updates on the 2016 valuations and cost control mechanism and set out the following commitments:

• the cost control element of the 2016 valuations will now be completed including the cost of implementing the McCloud remedy

• there will be no reduction to member benefits as a result of completing the 2016 valuation if the cost ceiling is breached

• if the cost floor is breached, this will be honoured by implementing increases in benefit accrual and/or reductions in member contributions from 1 April 2019.

However separately the Government had committed to reviewing the cost control mechanism and a report setting out this review was published on 15 June 2021.

The cost control mechanism was introduced into the valuation process for public service pension schemes – not just LGPS - in the Public Service Pensions Act 2013 following consultation with member representatives. It was designed to ensure a fair balance of risk with regard to the cost of providing defined benefit (DB) public service pension schemes between members of those schemes and the taxpayer.

The Government Actuary undertook a review of the mechanism amidst concerns that it was not operating in line with its original objectives. These objectives are:

- To protect taxpayers from unforeseen costs
- To maintain the value of pension schemes to the members
- To provide stability and certainty to benefit levels – the mechanism should only be triggered by 'extraordinary, unpredictable events'

The Government Actuary's report sets out his findings and makes a number of recommendations on possible changes to the mechanism, primarily these are effectively designed to prevent the unexpected result of the 2016 valuation cost cap exercise. The report confirms that the review did not consider the separate cost control mechanism for the LGPS and acknowledges that the differences between the LGPS and the unfunded public service schemes mean that some of the recommendations, if adopted, may need revising to accommodate those differences.

The Government will respond to this report in due course.

Consultations
N/A

Implications:

This item has the following implications, as indicated:

Risk management

No significant risks have been identified

Local Government (Access to Information) Act 1985
List of Background Papers

Paper	Date	Contact/Tel
N/A		

Reason for inclusion in Part II, if appropriate
N/A