

Current issues in the LGPS

September 2020

McCloud support

There's been a flurry of activity from various sources since MHCLG issued its [consultation](#) on a proposed McCloud remedy for the LGPS. We recently shared our [response](#) to the consultation and a [Briefing Note](#), together with information on our project management 'starter pack', which is an ideal tool to ensure you set up your McCloud project in the most effective way. Some of you have already benefited from our initial data analysis, helping you understand the scale of the issue for your Fund together with possible resource implications. We're also able to provide analysis on employer funding costs as well as providing comms material for use with your Pension Committee or Board. Please get in touch if you wish to discuss any of the support we can give.

Management of employer risk regulations

On 26 August MHCLG published its latest [partial response](#) to the May 2019 consultation called "Changes to the local valuation cycle and management of employer risk". The accompanying [amendment regulations](#) have also been made and are due to come into force from 23 September 2020. The new regulations provide more flexibility to funds to manage employer risk in three key areas, via 1) inter-valuation reviews of employer contributions, 2) spreading of exit debts and 3) Deferred Debt Agreements. Our [60 Second Summary](#) provides further detail. The regulations require funds to have policies in place around these new powers and MHCLG intends to develop guidance in collaboration with SAB and CIPFA. The speed at which the regulation have been drafted and put into force reflects the concern around administering authorities and employers being able to manage and mitigate risks arising from the COVID-19 pandemic. As our recent [Briefing Note](#) outlines, please speak to your fund actuary about getting the required policy/processes in place.

Public Sector Exit Payments - £95k cap and *BREAKING NEWS* Statutory Redundancy Payments

The government first announced plans to cap exit payments in the public sector in 2015. On 10 April 2019 HM Treasury (HMT) launched a consultation on draft regulations to implement the cap. HMT published its [response to the consultation](#) on 21 July 2020. We understand that government intends to have the cap implemented before the end of the calendar year. The exit payment cap is set at a total of £95,000 and will apply to all public sector employers. Exit payments include redundancy payments, severance payments and pension strain costs – which arise when an LGPS pension is paid unreduced before a member's normal pension age. The legislation is devolved in Wales and Scotland, and it is possible (or likely?) that they will exclude strain costs from the cap.

Statutory Redundancy Payments

In breaking and unexpected news, it appears that SRP is affected under these proposals too - you may have heard this on our webinar on Thursday 10th where Jeff Houston of LGA explained this in more detail. In essence, under the proposed new rules, anyone taking early retirement will in essence have to choose between taking unreduced pension (and then losing their SRP), or else taking the SRP but having their pension either reduced or deferred: all this is regardless of the size of their exit package vs £95k. The MHCLG consultation was not clear on this, and the SRP aspect has only become apparent after various conversations subsequent to Monday's announcement. We will be passing you more details very shortly, but in the meantime do get in touch to find out more if you need to update your HR colleagues, finance team and/or Elected Members.

Pension strain cost

Currently the pension strain cost that an employer pays on the early retirement or redundancy of a member over the age of 55 is calculated at a local fund level using factors provided by your actuary which reflect your local funding assumptions. The local approach to calculating the strain could mean that members in different LGPS funds with the same accrued pension may have a different strain cost to take into account in the calculation of the exit payment limit. Therefore, MHCLG have asked the Government Actuary's Department (GAD) to produce standardised factors for use in these calculations. If a pension strain payment cannot be made in full because of the cap, then the member's pension would be reduced. This will result in equity between members in different funds but will lead to less accurate assessments of the strain costs for the employers and could result in employers paying less in strain costs at the time of exit. Any shortfalls will feed into an employer's position at the next triennial valuation and may result in contribution increases at that time.

Implementation Issues

Although this policy was first announced back in 2015, there is now a very short timeframe for implementation and for the required changes to Regulations to be made. Any member leaving from an employer subject to the cap, after the end of the year, will have to have the employer strain cost calculated using the new standardised strain factors when available and members' pensions reduced as appropriate. As a result, it will be difficult to provide redundancy cost estimates to employers over the next few months. There will also be two different processes for early retirements. Employers who are outside of the public sector exit cap have members who are still entitled to unreduced benefits on redundancy regardless of the strain cost, which the employer must meet in full.

TCFD reporting to become mandatory?

The DWP is [consulting](#) on the introduction of mandatory reporting and governance of climate risks for larger UK occupational pension schemes. Whilst not in scope, the consultation notes that MHCLG "will make provision for the Local Government Pension Scheme, in line with their responsibility for the investment and governance of the LGPS". Given the broadly consistent approach being taken by UK regulators, it would seem likely that similar obligations will fall on the LGPS in coming years and Pension Committees should therefore continue to take steps to embed climate risk considerations into their governance arrangements. Our [briefing note](#) provides further detail on the proposals.

Finding the right investment opportunity

2020 has been a period of extreme turbulence for us, both in our day-to-day lives but also in financial markets. The volatility we have experienced has presented challenges but can also provide opportunities. Over the last couple of months, we've been working with managers to understand which opportunities are most likely to provide genuine accessible investments for investors. As markets and economies tentatively recover, focus can now move to the implementation of these new investment opportunities. Our latest issue of [Investment Perspectives](#) and [webinar on 4 September](#) outline three of the opportunities that we consider most attractive.

Annual Allowance

So, you've issued your annual benefit statements, and it's straight into pension savings statements. All being well, this is the last year of the taper, but overall volumes increase year-on-year as more members are hit by the standard allowance. The impact of aggregation is resulting in more queries and concerns from members. Dealing with these demands takes time away from other priorities. We can help by undertaking your calculations, providing team training or member awareness sessions or even member 1-2-1s, if required. Our Governance, Administration and Projects team would be happy to discuss any support we can provide.

Good Governance update

The project team met with the SAB on 25 August and agreed to progress 3 key deliverables over the next month or so, namely 1) implementation advice around the [Phase 2 proposals](#), 2) a sample of a fund's new Governance

Compliance Statement (GCS), and 3) a sample independent governance review report (IGR). Please click [here](#) for fuller details.

NKA – and the results were....

We announced the [results](#) of the National Knowledge Assessment (NKA) at our [webinar](#) on 18 August. Among the headline results was a confirmed strong level of knowledge on the more traditional committee topics of financial markets and investments. We also confirmed that Chairs of Committees and Pension Boards scored higher in nearly all topics (7 out of 8) than the other NKA participants and we discussed how the NKA provided evidence to participant funds of the spread of knowledge held on both groups. The NKA remains open to funds that did not participate - please get in touch if your fund wishes to take part now and access this NKA benchmark information.

Educating employers

To help Academies with their August 2020 accounting exercise, we are running a webinar on 22 September. We'll be covering the process for producing reports, some of the differences between pensions funding and accounting, and will also have a discussion on the hot topics in the LGPS (of which there are many!). To register, click [here](#).

Many employers may also be thinking about what COVID-19 means for their own participation in the LGPS. Market volatility will affect different employers in different ways, depending on their time horizon in the Fund. However, it's not only assets that are impacted. The other side of the balance sheet may also see an impact, due to changes in market expectations of future investment returns which in turn influences the pensions liability. You can read our article [here](#). Please feel free to share the article and the webinar link with your Fund employers.

2020 valuations gathering steam

August was a not a month of rest for administration teams in Scotland as they prepared and submitted the 2020 valuation extracts. Work is now well underway ensuring the data is fit for purpose and the calculations can begin. Whilst those take place, funds will need to consider how (if?) they make any allowance for the potential benefit changes due to the 2017 Cost Cap valuation (which has been 'un-paused' following the release of the proposed McCloud remedy) and how they will virtually communicate results to Committee, Boards and employers as the current lockdown measures continue.

Ensuring the ongoing viability of the LGPS

The Pension Regulator's funding code consultation may have been lost in the recent flurry of LGPS regulatory activity, however nestled within it is a requirement that could have significant implications for the LGPS. The [LGPS SAB Chair wrote to TPR](#) to express his concern about the principle of de-risking in respect of open defined benefit pension schemes and how it may, over time, be forced to apply LGPS funds. The result would be sharp increases in contribution rates which would likely leave the scheme unaffordable to all employers. Hopefully a sufficient robust exemption status is placed on the LGPS in the new funding code.

Exit credits

LGPS regulations and guidance are littered with the words 'must', 'should' and 'may'. Must is the strongest of these, but can a 'must' not mean you must do something? In March, the English and Welsh regulations in respect of exit valuations were retrospectively changed in order to address the unintended consequences resulting from the introduction of exit credits. One of the new regulations says "*In exercising its discretion to determine the amount of an exit credit the administering authority must have regard to the following factors-*". The factors are the size of the surplus, the proportion of the surplus resulting from employer contributions, any representations from the employer, guarantor or connected employer and any other relevant factors. The key here is "*must have regard to*". It is open to interpretation as to whether administering authorities have to explicitly take these factors into account when making their determination, or whether just giving them some thought is sufficient. Given this ambiguity, we encourage administering authorities to thoroughly document how they have reached their determination when deciding on the level of exit credit to ensure they are not caught out if challenged through IDRPs.

Appendix

McCloud support

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/901173/Condoc_-_amendments_to_LGPS_underpin_-_FOR_PUBLICATION.pdf

<https://www.hymans.co.uk/insights/research-and-publications/publication/mhclg-mccloud-consultation-response/>

<https://www.hymans.co.uk/insights/research-and-publications/publication/mhclg-mccloud-consultation/>

Management of employer risk regulations

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/911792/Government_response_Exit_payments_and_review_employer_contributions.pdf

<https://www.legislation.gov.uk/ukxi/2020/893/made>

<https://www.hymans.co.uk/insights/research-and-publications/publication/management-of-employer-risk-regulations/>

<https://www.hymans.co.uk/insights/research-and-publications/publication/employer-management-in-the-lgps/>

Public Sector Exit Payments - £95k cap

<https://www.gov.uk/government/consultations/restricting-exit-payments-in-the-public-sector>

TCFD reporting to become mandatory?

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/911894/tcfd-taking-action-on-climate-risk.pdf

<https://www.hymans.co.uk/insights/research-and-publications/publication/climate-risk-taskforce-on-climate-related-financial-disclosures-reporting-to-become-mandatory-for-larger-schemes/>

Finding the right investment opportunity

<https://www.hymans.co.uk/insights/research-and-publications/publication/investment-perspectives-summer-2020/>

<https://www.hymans.co.uk/insights/events/seeking-investment-opportunities-in-the-wake-of-covid-19/>

Good Governance update

<https://www.hymans.co.uk/insights/research-and-publications/publication/good-governance-in-the-lgps-phase-2-report/>

<https://www.hymans.co.uk/insights/blogs/blog/update-good-governance-in-the-lgps/>

NKA – And the results were....

<https://www.hymans.co.uk/insights/research-and-publications/publication/webinar-replay-lgps-national-assessment-assessment-results/>

<https://www.hymans.co.uk/insights/research-and-publications/publication/lgps-national-knowledge-assessment-report/>

Educating employers

<https://www.hymans.co.uk/insights/events/accounting-webinar-for-academies/>

<https://www.hymans.co.uk/insights/research-and-publications/publication/covid-19-pandemic-lgps-employers/>

Ensuring the ongoing viability of the LGPS

<http://lgpsboard.org/images/PDF/letters/SABTPRFC.pdf>