PENSIONS COMMITTEE

16 September 2020

Title: Administration and Governance Report	
Report of the Chief Operating Officer	
Public Report	**For Information**
Wards Affected: None	**Key Decision:** No
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Accountable Director: Philip Gregory, Finance Director	
Accountable Strategic Leadership Director: Claire Symonds, Acting Chief Executive	
Recommendations The Committee is recommended to note: i. The Independent Advisors update on Government Consultation to address Age Discrimination relating to 'transitional protection' in the LGPS (commonly referred to as "McCloud"), ii. that the Fund is cash flow negative, iii. the Fund's three-year budget for the period 1 April 2020 to 31 March 2023, and iv. the London CIV's Update	

1. Introduction

1.1 It is best practice for Members to receive regular administration data and governance updates. This report covers three main areas including:

i. Independent Advisors update on Government Consultation to address Age Discrimination relating to 'transitional protection' in the LGPS (commonly referred to as "McCloud")
ii. Pension Fund Budget 1 April 2020 to 31 March 2023;
iii. Cash flow to 30 June 2020;

2. Update on Government Consultation to address Age Discrimination relating to 'transitional protection' in the LGPS (commonly referred to as "McCloud")

2.1 Introduction

The purpose of this paper is to inform the Pensions Committee of the Government Consultation issued on 16 July 2020 to address age discrimination relating to transitional protection arrangements introduced as part of the 2014 reforms of the LGPS.

2.2 On 16 July 2020 the Ministry of Housing Communities and Local Government (MHCLG) issued a consultation called “Amendments to the statutory underpin.” This consultation proposes amendments to the LGPS Regulations to remove age discrimination in relation to ‘transitional protection’ arrangements introduced when the LGPS was reformed in 2014. This whole issue is now commonly referred to as “McCloud” which refers to one of the court cases that highlighted the age discrimination present in all the public service pension schemes (which include the Judicial, Firefighters’, Civil Service, NHS, Police, Teachers and Local Government schemes) covered by the Public Service Pensions Act 2013.

2.3 When the LGPS was reformed in 2014 a number of changes were made including changing the scheme going forward from a final salary to a career average scheme. However, the new scheme included transitional protection arrangements for members nearing retirement designed to ensure older workers would not be worse off as a result of the introduction of the new scheme. This protection meant that members who met certain criteria, including that they were within ten years of their final salary scheme normal pension age on 1 April 2012, received ‘underpin protection.’ This meant that a member’s pension entitlement under the new career average scheme could not be lower than it would have been under the previous final salary scheme. An underpin test was required to be carried out comparing career average benefits the member accrued against the ‘underpin amount’ which is the final salary benefits that would have accrued if the LGPS had not been reformed.

2.4 Transitional protection arrangements for older workers were also introduced into the other major public sector pension schemes which were reformed in 2015 (a year later than the LGPS). These protections were challenged in the cases of both the Judicial and the Firefighters’ schemes in what are known as the “McCloud” and “Sergeant” cases respectively where it was argued that younger members received less favourable treatment than those older members who were given transitional protection. In December 2018, the Court of Appeal ruled that the transitional protection in the Judicial and Firefighters pension schemes constituted unlawful age discrimination. Consequently in 2019 the Government stated that it would take action to address this issue across all the public sector pension schemes covered by the Public Service Pensions Act 2013.

2.5 On 16 July 2020 the Ministry of Housing Communities and Local Government (MHCLG) issued a consultation called “Amendments to the statutory underpin” to address the age discrimination identified in the LGPS. A separate consultation to address the age discrimination in the other (unfunded) pension schemes covered by the Public Service Pensions Act 2013 was issued at the same time by HM Treasury.

2.6 The Consultation issued by the MHCLG is very long (69 pages), detailed and technical in nature. It includes draft Regulations to remedy the present defects in the LGPS Regulations. The Consultation also includes 29 questions which respondents may wish to address. The Consultation appears to have been very carefully prepared by MHCLG who have also held technical discussions with the LGPS Scheme Advisory Board for England and Wales prior to formally issuing the Consultation. The Consultation runs from 16 July to 8 October 2020. The final proposals as put into place through revisions to the LGPS Regulations will be back dated to 1 April 2014 when the new LGPS arrangements came into effect.

2.7 As the LGPS Regulations are currently constituted they treat members of the Scheme differently depending on their age as follows:

- Those who were active members of the Scheme on 31 March 2012 and were within ten yours of their normal pension age (NPA) on 1 April 2012 are entitled to underpin protection and are therefore "better off" than the group below
- Those who were active members of the Scheme on 31 March 2012 and were more than ten years from their NPA were not eligible for underpin protection and were therefore potentially "worse off" than the above group as they were not guaranteed a pension of at least the level they would have received in the final salary scheme. However, in reality most younger members will not benefit from any change to the underpin protection

2.8 The exact details and the mechanism for calculating whether a member is better off under the non-discriminatory underpin proposed in the Consultation are complex and lengthy. However, the proposals may be briefly summarised as described in the following paragraph:

2.9 In essence the Consultation proposes a solution and amendments to the LGPS Regulations which extend the underpin to the second group above (those described in the second bullet point) – that is it is proposed to extend the underpin protections to those who were not old enough to receive underpin protection when it was originally introduced. This should ensure equality between the two groups for benefits accrued from 1 April 2014 onwards. Vital general features of the proposed solution are briefly described at 1 to 4 below but these are only extremely brief summaries of a technically complex solution which is described and explained in the actual Consultation. Therefore, the summaries below should not be relied upon as describing the situation as it would apply to any particular individual

- Eligibility is restricted to those who were active members of the LGPS on 31 March 2012 and who went on to accrue benefits since 1 April 2014
- The underpin applies between 1 April 2014 and 31 March 2022 only. It will cease earlier than 31 March 2022 if the member ceases to be an active member or dies in service. Crucially it is only service between 1 April 2014 and 31 March 2022 that will be assessed under both "final salary" and "career average" calculations. Service before 1 April 2014 will be assessed only under the final salary arrangements of the previous LGPS. Service from 1 April 2022 will only be assessed using a "career average" basis.
- The final salary for comparison purposes is the salary when the member ceases to be an active member or reaches age 65. Therefore, some underpin calculations will still need to be undertaken in the 2050s!
- As paragraph 136 of the Consultation makes clear "A major challenge of implementing the changes proposed would apply in respect of obtaining additional data from employers for members who are newly benefitting from underpin protection – estimated to be around 1.2 million individuals. Under the 2014 Scheme, certain member data which was required for administering the 2008 Scheme… are not required for calculating member benefits. To administer the revised underpin, administrators would need to obtain this data for qualifying members for the period back to April 2014… Particular challenges are likely to

arise where employers have changed their payroll provider, and the data isn't stored in current systems."

2.10 Assuming the Consultation proposals are implemented then this will result in a huge task for Pension Administration Teams such as that which services the London Borough of Barking and Dagenham. This challenge goes way beyond the major Data collection/analysis implications of the proposed solution and will also require significant Governance, Communication and Training challenges. Careful planning and appropriate resourcing will be required to ensure that implementation of the remedy within the London Borough of Barking and Dagenham is as smooth and effective as possible. Barnett Waddingham, who are now the Actuary to the London Borough of Barking and Dagenham Pension Fund have, in a Briefing Note of 5 August 2020, described as "onerous" the task facing individual LGPS Funds to implement the amendments to the underpin.

2.11 The London Borough of Barking and Dagenham will need to develop and implement a project plan and commence the necessary steps to implement the "McCloud" remedy. This should include consideration of the extensive governance, data, communication, training and education activities that will require to be undertaken. Consideration should also be given to additional resourcing to implement the "McCloud" remedy. The Barnett Waddingham Briefing Note of 5 August 2020 includes the following comments in relation to the impact on Pensions Administration "It's important, given the scale of the task, that funds start to plan ahead and think what they can be doing now to get ready for implementation…It is clear that project planning and additional resources will be required."

2.12 The increase in liabilities resulting from the proposed "McCloud" remedy is uncertain and dependent on a number of variables. It is however not expected to be material in relation to the total liabilities of the LGPS. Paragraph 142 of the Consultation provides an estimate based on work by the Government Actuary Department (GAD) which states "…Assuming future member experience replicates the 2016 scheme valuation assumptions the future cost to LGPS employers could be around £2.5bn in the coming decades..." The Value of LGPS liabilities at 31 March 2019 was (according to the Scheme Advisory Board Annual Report) £296 billion and therefore the GAD estimate suggests an increase in liabilities of less than 1%.

2.13 This estimate by GAD may however be a significant overestimate. Hymans Robertson, one of the four actuarial firms who provide services to the LGPS (and who were Actuary to the Barking and Dagenham Fund at the 2019 Actuarial Valuation), have suggested in a Briefing Note of July 2017 that liabilities may increase by less than £1 billion "across the whole of the English & Welsh LGPS." Barnett Waddingham the present Actuary to the Barking and Dagenham Pension Fund has stated in their Briefing Note issued on 5 August 2020 that across the LGPS in England and Wales "…we estimate that the impact of the remedy might be to increase the liabilities by around 0.3% or around £0.9bn. This will depend on several factors; in particular, assumed salary growth relative to CPI and the level of withdrawals. This is significantly less that the £2.5bn estimated by GAD. This is largely because the salary growth assumption made by GAD is CPI plus 2.2% which is materially higher than our assumption for the 2019 E&W valuations which was typically CPI plus 1% p.a."

2.14 While the impact of the "McCloud" remedy on liabilities is likely to be very small at the level of a whole LGPS Fund, for example the London Borough of Barking and Dagenham Fund, it could possibly be significant for some employers. The Barnett Waddingham Briefing Note of 5 August 2020 includes the following comments on this issue "Although the impact is likely to be small at whole fund level it could be significant at individual employer level…For many employers in the LGPS with a mature workforce, like the councils, there is likely to be minimal impact…For employers with a young workforce… there could be a material impact on costs…Smaller employers may also be more affected. The change in an individual member's benefits may make up a significant proportion of their current liabilities and therefore the impact on smaller employers is likely to be more volatile." The issue of the effects of the proposed "McCloud" remedy on individual employers is therefore a matter the Barking and Dagenham Fund may wish to raise with its Actuary Barnett Waddingham.

3. Pension Fund Budget 1 April 2020 to 31 March 2023

3.1 Table 1 provides Members with the Fund's three-year budget to 31 March 2023.

Table 1: Pension Fund Budget 1 April 2020 to 31 March 2023

Contributions	**2020/21 Budget**	**2021/22 Budget**	**2022/23 Budget**
Opening Market Value	**974,493**	**1,012,293**	**1,050,243**
Employee Contributions			
Council	6,800	6,600	6,400
Admitted bodies	1,000	900	800
Scheduled bodies	1,950	2,000	2,050
Employer Contributions			
Council	21,000	22,000	23,000
Admitted bodies	4,000	3,750	3,500
Scheduled bodies	7,250	7,400	7,500
Pension Strain	1,000	1,000	1,000
Transfers In	2,500	2,500	2,500
Total Member Income	**45,500**	**46,150**	**46,750**
Expenditure			
Pensions	-36,500	-37,500	-38,500
Lump Sums and Death Grants	-7,000	-6,500	-6,500
Transfers Out	-2,500	-2,500	-2,500
Administrative expenses	-700	-700	-700
Total Expenditure on members	**-46,700**	**-47,200**	**-48,200**
Net dealings with members	**-1,200**	**-1,050**	**-1,450**
Returns on Investments			
Investment Income	7,500	7,500	7,500
Profit (losses)	35,000	35,000	35,000
Investment management expenses	-3,500	-3,500	-3,500
Net returns on investments	**39,000**	**39,000**	**39,000**
Net increase (decrease) in assets	**37,800**	**37,950**	**37,550**
Closing Market Value	**1,012,293**	**1,050,243**	**1,087,793**

3.2 The three-year budget shows a movement from members being employed by the Council to being funded by admitted bodies as staff move across to the various companies set up by the Council. The forecast is for the Council contribution to increase as the rate increases from 21.0% in 2020/21, 22.0% in 2021/22 and 23.0% in 2022/23. Admitted body contribution will initially increase, but as the admitted bodies are closed to new entries, their contributions will decrease over time. Due to these changes, the overall member income will decrease in 2021/22 and 2022/23.

3.3 An increase in death grant payments is projected in 2020/21. Pension payments are forecast to increase due to an increase in the number of pensioners as well as to reflect a pension increase of 1.7% for 2020/21.

3.4 Overall the Fund is expected to be cashflow negative for net dealings with members but cashflow positive if investment income and management expenses are included. Officers will be working with the fund managers over the coming year to establish a process to utilise the income from property and infrastructure to fund any cash flow shortfalls.

4. Cash flow to 30 June 2020

4.1 Table 2 below provides Members with the Fund's Cash flow to 30 June 2020.

Table 2: Actual Pension Fund Cash Flow to 30 June 2020

	2020/21 Budget £000's	2020/21 Actual £000's	Over / Under £000's
Contributions			
Employee Contributions			
Council	6,800	7,160	360
Admitted bodies	1,000	750	-250
Scheduled bodies	1,950	1,960	10
Employer Contributions			
Council	21,000	22,500	1,500
Admitted bodies	4,000	3,000	-1,000
Scheduled bodies	7,250	7,700	450
Pension Strain	1,000	1,000	0
Transfers In	2,500	2,300	-200
Total Member Income	**45,500**	**46,370**	**870**
Expenditure			
Pensions	-36,500	-35,700	800
Lump Sums and Death Grants	-7,000	-5,800	1,200
Payments to and on account of leavers	-2,500	-5,400	-2,900
Administrative expenses	-700	-700	-
Total Expenditure on members	**-46,700**	**-47,600**	**-900**
Net additions for dealings with members	**-1,200**	**-1,230**	**-30**
Returns on Investments			
Investment Income	7,500	7,500	-
Profit (losses)	35,000	35,000	-
Investment management expenses	-3,500	-3,500	-
Net returns on investments	**39,000**	**39,000**	**-**
Net increase (decrease) in the net assets	**37,800**	**37,770**	**-30**
Asset Values	**1,012,293**	**1,097,840**	
Liabilities	**-1,189,704**	**-1,285,865**	
Funding Level	**85.09%**	**85.38%**	

5. London CIV Update

5.1 The London Collective Investment Vehicle is the first fully authorised investment management company set up by Local Government. It aims to be the LGPS pool for London to enable Local Authorities to achieve their pooling requirements.

5.2 Having set up in 2015, CIV launched a number of funds which were seeded by London Borough Pension Funds. At 30 June 2020, London CIV assets under management was £8.9 billion which is a rise of more than 17% compared to the previous quarter.

5.3 The table below provides members with a breakdown of the LBBD Pension Funds holdings in LCIV as at 30 June 2020.

Fund	**Manager**	**Value of Holdings (£)**	**% of Pension Fund**
Global Alpha Growth Fund	Baillie Gifford	255,773,164	23.3%
Real Return Fund	Newton	73,146,995	6.7%
Global Total Real Fund	Pyrford	107,054,528	9.8%
Total		**435,974,687**	**39.8%**

5.4 Following a high staff turnover and interim appointments, LCIV have permanently appointed to three key posts over the last few months- the Client Relations Director (current post holder is retiring), the Chief Investment Officer (current postholder is an interim) and Head of Responsible Investment (new post).

6. Consultation

6.1 Council's Pension Fund governance arrangements involve continuous dialogue and consultation between finance staff and external advisers. The Finance Director and the Fund's Chair have been informed of the commentary in this report.

7. Financial Implications

Implications completed by: Philip Gregory, Finance Director

7.1 The Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. The management of the administration of benefits the Fund is supported and monitored by the Pension Board.

8. Legal Implications

Implications completed by: Dr. Paul Feild Senior Governance Solicitor

8.1 The Council operates the Local Government Pension Scheme which provides death and retirement benefits for all eligible employees of the Council and organisations which have admitted body status. There is a legal duty fiduciary to administer such funds soundly according to best principles balancing return on investment against risk and creating risk to call on the general fund in the event of deficits. With the returns of investments in Government Stock (Gilts) being very low they cannot be the primary investment. Therefore, to ensure an ability to meet the liability to pay beneficiaries the pension fund is actively managed to seek out the best investments. These investments are carried out by fund managers as set out in the report working with the Council's Officers and Members.

8.2 This report refers to the recent Supreme Court decision in R (on the application of Palestine Solidarity Campaign Ltd and another) (Appellants) v Secretary of State for Housing, Communities and Local Government (Respondent). Its implications are considered.

8.3 It related to a judicial review of Guidance issued by the Secretary of State on preparing and maintaining an Investment Strategy Statement. The Guidance was issued was issued pursuant to regulation 7(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (SI 2016/946) ("the 2016 Regulations"), and to take effect when the regulations did so, on 1 November 2016. The Guidance was entitled: "Local Government Pension Scheme: Guidance on Preparing and Maintaining an Investment Strategy Statement".

8.4 The guidance contained new stipulations designed to prohibit LGPS funds from pursuing boycotts, divestment and sanctions against foreign nations and UK defence industries. This guidance was challenged on the basis that the Secretary of State had exceed his authority in that the power to issue guidance was limited to the purpose of the legislation creating the power. The challenge was successful in the High Court and so the Secretary of State appealed to the Court of Appeal where he won as the Court reversed the High Courts decision. A further appeal was then entered to the Supreme Court (the replacement to the House of Lords and the highest court in the land). Here the objectors to the Guidance were successful by a majority 3 to 2 judges who held that the guidance extended to matters outside the Secretary of States authority to give guidance. It was determined that the position was that the Secretary of State sought to promote the government's own wider political approach, by insisting that, in two particular contexts related to foreign affairs and to defence, administering authorities could not refrain from making particular investments on non-financial grounds, regardless of the views held by the scheme members. The flaw according to the majority was that the position was that judgements about non-financial considerations in investment decisions were for administering authorities not the Secretary of State to take. Administering authorities may take non-financial considerations into account provided that in doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision.

8.5 In terms of direct implications, the guidance will need to be changed or at least amended. However, for practical purposes it has no specific impact for Barking and Dagenham as the administering authority has no stated intentions with regards to foreign policy or UK defence and within its investment strategy.

9. Other Implications

9.1 There are no other immediate implications arising from this report though the Public Service Pensions Act changes will have an impact on the short and long-term workload of the Pension Fund. This will continue to be monitored.

Background Papers Used in the Preparation of the Report:

The full (69 page) Consultation issued by the MHCLG to address the unlawful age discrimination in the present LGPS Regulations entitled "Amendments to the statutory underpin may be accessed at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/901173/Condoc_-_amendments_to_LGPS_underpin_-_FOR_PUBLICATION.pdf