TEESSIDE PENSION FUND

Administered by Middlesbrough Council

AGENDA ITEM 10

TEESSIDE PENSION BOARD REPORT

4 NOVEMBER 2019

STRATEGIC DIRECTOR FINANCE, GOVERNANCE & SUPPORT – JAMES BROMILEY

Update on Current Issues

1. PURPOSE OF THE REPORT

1.1 To provide Members of the Teesside Pension Board (the Board) with an update on current issues affecting the Pension Fund locally or the Local Government Pension Scheme (LGPS) in general.

2. RECOMMENDATIONS

2.1 That Members note this report.

3. FINANCIAL IMPLICATIONS

3.1 There are no specific financial implications in respect of the information contained in this report.

4. ACTUARIAL VALUATION

4.1 Members will be aware that 2019 is a valuation year for the LGPS. The scheme actuary (AON) is carrying out a valuation of the assets and liabilities of the Fund as at 31 March 2019. The final report must be published by 31 March 2020 and the valuation outcome will set employer contribution rates for all the Fund's employers for the period from 1 April 2020 up until the day before the outcome of the next valuation applies (currently expected to be 31 March 2023).

4.2 AON had planned to start providing draft valuation outcomes (initially to the four large council employers) from mid-October onwards, with the intention that all employers would have their draft results by the end of December. However, owing to delays in data submission and resolution of data queries, the date for provision of initial data has slipped - at the time of writing this report the first employer results are expected at the end of October. A verbal update on progress on individual employer results, together with an indication of the 'whole of fund' valuation outcome will be provided to the Board at this meeting.

5. LGPS COST MANAGEMENT PROCESS AND CHANGES EXPECTED BECAUSE OF THE MCCLOUD CASE

5.1 The LGPS, in common with the other public service pension schemes, has a mechanism for periodically checking whether the cost of providing the scheme falls within acceptable parameters. If the cost of the scheme is assessed as too high this results in potential reductions to future scheme benefits and/or increases on employee contributions. Conversely, if the cost is assessed as too low this can result in improvements to future benefits and/or reductions in employee contributions.

5.2 This is known as the cost management process and the outcome of the latest process revealed that the average overall cost of the scheme was 19% of pensionable pay, which is 0.5% of pensionable pay lower than the target cost for the LGPS of 19.5% of pensionable pay. Consequently, the Scheme Advisory Board developed proposals to improve scheme benefits and reduce employee contributions to bring the cost of the scheme back up to the target level.

5.3 The proposals were not enacted and the cost management process was paused when the Government lost a high court case in December 2018 (the McCloud case) which had been brought by members of the Judges' pension scheme and the Firefighters' Pension Scheme, arguing that the protections put in place when changes were made to those schemes were age discriminatory, as they only protected older scheme members. This case has implications for all public service pension schemes, including the LGPS. The Government sought to appeal the case but the Supreme Court denied the Government leave to appeal in a decision on 27 June 2019. The Government subsequently issued a statement confirming that it will look at the issue of discriminatory treatment in the introduction of the new schemes across all public service pension schemes, including the LGPS.

5.4 It is likely to take many months before the employment tribunal concludes in relation to the discrimination in the Judges' and Firefighters' pension schemes. The Government has said that alongside this process it will engage with employer and member representatives in the other public service pension schemes to determine how those schemes will be changed to remove the discrimination introduced by transitional protection.

5.5 In the meantime, any cost management proposals remain on hold. Although it is very difficult to know what the eventual increase in pension liabilities will be as a result of this exercise, the Fund is working with the actuary to ensure an appropriate degree of prudence is built into the valuation outcome to take account of this. The current expectation is that the actuary will be setting out an explicit increase to employer contribution rates to take this into account. However, owing to the continuing uncertainty over what remedy the Government will apply to remove the discrimination, it is not possible to accurately forecast the exact impact either at a Fund or a scheme employer level.

6 THE PENSIONS REGULATOR'S ENGAGEMENT REPORT

6.1 In September 2019 The Pensions Regulator (TPR) produced the results of its in depth engagement with 10 LGPS Funds selected from across the UK to understand scheme managers' approaches to a number of key risks. The report is available on TPR's website at https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis and a print of the report is enclosed at Appendix A.

6.2 The report is not intended to be a full evaluation of how each LGPS Fund operates but it provides a useful indication of TPR's view of the LGPS. The report's summary identifies four key improvement areas:

"**Key person risk**: While most scheme managers demonstrated a good knowledge of what we expect, many funds have a lack of comprehensive documented policies and procedures. We also found an over-reliance on controls put in place by the Local Authority with little interaction between the scheme manager and Local Authority. This was particularly prevalent in relation to cyber security but this theme overlays several of the risk areas we explored.
Pension boards: Engagement levels varied, with concerns being raised about the frequency some pension boards meet and their appetite to build their knowledge and understanding. We saw evidence of some pension boards not wanting to review full documents, instead relying on much reduced summaries and leading us to question how they could fulfil their function. Others were well run and engaged.

Fraud / scams: We saw evidence of scheme managers learning from wider events and taking steps to secure scheme assets. However, not all were as vigilant when it came to protecting members from potential scams.

Employers: We saw considerable variance in the approaches taken to dealing with the risks surrounding employers, such as receiving contributions and employer insolvency. Generally this was connected to fund resourcing but also related to different philosophies related to taking security over assets."

6.3 The LGPS Scheme Advisory Board is currently reviewing governance issues in relation to the LGPS as a whole and is due to receive a paper on this subject at its November 2019 meeting. This is likely to include consideration of the findings of TPR's Engagement Report and recommendations on how they could best be applied across LGPS funds.

7. COMPETITION AND MARKETS AUTHORITY ORDER

7.1 On 10 June 2019 the Competition and Markets Authority (CMA) published the Investment Consultancy and Fiduciary Management Market Investigation Order 2019. The Order in had potential implications both for LGPS investment pools and for LGPS Funds.

7.2 Investment pools were potentially affected by the order if they are carrying out 'fiduciary management' for their underlying LGPS funds. 'Fiduciary management' typically involves a manager taking full responsibility for investment, including asset allocation decisions. One further possible impact of the order was that LGPS Funds could be required to carry out a competitive procurement process in order to appoint the LGPS investment pooling company to manage their assets – despite the fact most such pooling companies are owned by the LGPS Funds whose assets they manage. This potential anomaly has now been resolved through clarification of how the Order will be applied, and the Order now has no direct impact in this area.

7.3 However, LGPS Funds will still be affected by the Order as it sets out rules about how pension schemes should obtain investment consultancy. This requires investment consultants to be appointed through a suitable competitive tendering process, and for them to be set objectives. There is also a possibility that the Financial Conduct Authority will extend its definition of regulated activity to include asset allocation – meaning investment consultants working for LGPS Funds may need to be FCA authorised in future.

7.4 From our Fund's perspective, both our investment advisers were appointed as part of a competitive tendering process and both have been set objectives as part of their appointment. A paper will be presented to the December Pension Fund Committee confirming how the Fund is complying with the requirements of the Order.

8. NEXT STEPS

8.1 Further updates will be provided periodically.

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