

# TEESSIDE PENSION FUND

Administered by Middlesbrough Council

AGENDA ITEM 11

## PENSION FUND COMMITTEE REPORT

13 MARCH 2019

STRATEGIC DIRECTOR FINANCE, GOVERNANCE & SUPPORT – JAMES BROMILEY

### Cost Management

#### 1. PURPOSE OF THE REPORT

- 1.1 To advise Members of the Teesside Pension Board (the Board) of changes proposed to the regulations governing the Local Government Pension Scheme (LGPS) as a consequence of the Scheme Advisory Board's cost management process, and the reason implementation of these proposed changes has been delayed.

#### 2. RECOMMENDATIONS

- 2.1 That Members note this report.

#### 3. FINANCIAL IMPLICATIONS

- 3.1 If introduced, these changes would result in an average increase to employer contributions in the LGPS of around 0.9% of pensionable pay. The exact amount will vary significantly by employer, with those who employ mainly lower paid staff seeing an increase in employer costs of around 2.75% of pensionable pay.

#### 4. BACKGROUND

- 4.1 When the LGPS regulations were changed to introduce career-average revalued earnings benefits for future service from 1 April 2014, this was done under a new legislative framework for public service pension schemes under the Public Service Pensions Act 2013.
- 4.2 One of the requirements of the new framework for public service pension schemes was that the cost to employers of providing those schemes should be assessed periodically, potentially leading to adjustments to scheme members' benefits or contributions in order to bring the cost back into line with original figures.
- 4.3 This is known as the cost control process and, in the LGPS in England & Wales, there are two mechanisms for assessing the cost of the Scheme:
- an Employer Cost Cap mechanism (ECC), operated by HM Treasury on advice from the Government Actuary's Department (GAD) which is the mechanism formally required by the Public Service Pensions Act 2013, and

- a Future Service Cost mechanism (FSC), operated by the LGPS Scheme Advisory Board, on advice from GAD and to the satisfaction of the Ministry for Housing, Communities and Local Government (MHCLG).

4.4 Both processes are undertaken in the LGPS every three years in line with the local triennial valuations that are undertaken by each pension fund to determine funding levels and the employer contributions payable in the coming period. The cost control mechanisms will first be used to assess the cost of the Scheme at the same time as the 2016 valuations, using data as at 31st March 2016. Any changes to the Scheme's benefits structure or its employee contribution rates which arise from the 2016 cost control process are meant to be effective from 1st April 2019.

## **5. COST MANAGEMENT OUTCOME**

5.1 The Future Service Cost mechanism operated by the Scheme Advisory Board has determined the future service cost for the LGPS is 19% as against the target of 19.5%. In order to bring the cost back in line with the target cost, the Scheme Advisory Board recommended the following changes to contributions and benefits:

- Removal of the third tier of ill-health (assume it will be replaced by second tier ill-health)
- A minimum death in service benefit of £75,000
- Enhanced early retirement reduction factors
- Employee contributions: A new 2.75% band at pay from £0 to £12,850, reduced rate of 4.4% (from 5.8%) for pay from £12,501 to £22,500, and an expansion of the top of the current 6.8% band from £45,200 to £53,500.

5.2 The Scheme Advisory Board produced a draft consultation document (see Appendix A) which sets out the expected content of a more formal consultation which it stated at the time was due "late January/ early February".

5.3 The impact on employers will vary, depending on the profile of their scheme members. AON, the Pension Fund actuary, estimated the cost to employers as being 0.9% of pensionable pay on average but ranging up to 3.0% of pensionable pay. The additional cost of these potential future scheme changes will need to be considered as part of the 31 March 2019 valuation (results expected by the end of 2019).

## **6. ANNOUNCEMENT ON DELAY TO COST MANAGEMENT PROCESS**

6.1 The Scheme Advisory Board issued an email on 30 January 2019 advising that the Government had announced a pause in the cost management process for public service pension schemes (see Appendix B). This was because of an ongoing appeal about a court case (the McCloud case) the Government lost in December where it was found that the 'transitional protection' offered when scheme members moved into the 'new' public service pension schemes in 2014 and 2015 in some case amounted to unlawful discrimination. The potential cost of rectifying this (should the Government's appeal be unsuccessful) has been estimated as potentially £4 billion a

year. While this risk exists, and there is uncertainty about the value of all public service pension schemes' liabilities, the Government has decided not to progress with its cost management assessment.

- 6.2 The Scheme Advisory Board issued a further email on 8<sup>th</sup> February 2019 (see Appendix C) confirming that the cost management processes in the LGPS will be suspended pending the outcome of the McCloud case. It confirmed that "as a result there are currently no changes to benefits planned in respect of the cost cap. This situation will be reviewed once McCloud is resolved which is not expected for some months."

## **7. NEXT STEPS**

- 7.1 Further guidance is awaited on how Fund actuaries should take into account the expected increase in liabilities caused by either the implementation of the McCloud case outcome across the LGPS, or the introduction of benefit improvements and contribution reductions if the cost management process is implemented.
- 7.2 Information will be provided to scheme employers once the position is clearer.

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