Agenda Item 10

LOCAL PENSION BOARD

16 SEPTEMBER 2019

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

CONSULTATION – LOCAL VALUATION CYCLE AND MANAGEMENT OF EMPLOYER RISK

Purpose of the Report

1. The purpose of this report is to inform the Local Pension Board on the potential implications of the Ministry of Housing, Communities and Local Government (MHCLG) consultation "LGPS: Changes to the local valuation cycle and the management of employer risk policy".

Background

2. In May 2019 MHCLG started a 12 week consultation, which closed on 31 July 2019. The consultation covers the following areas:
   - Extension from the current three years to a four year valuation cycle
   - Mitigation to the risks of lengthening the valuation cycle
   - Flexibility on exit payments to reduce risk of employer default
   - Proposals for further policy changes to exit credits
   - Proposals for changes to the employers required to offer local government pension scheme membership.

   Officers in conjunction with the Chair of the Local Pension Board replied to the consultation on the 19 June 2019. The reply is attached as Appendix A.

3. Changes to the LGPS Valuation Cycle

   Every three years the triennial pension scheme valuation takes place. The Fund's assets and liabilities are assessed on the 31 March 2019 and the overall funding position is calculated. Each of the Fund's employer contributions rates are calculated and the rates set for three years, 1 April 2020 to 31 March 2023.

   There is a proposal that the LGPS scheme valuation should be moved from the current triennial to a quadrennial cycle in line with other public service scheme valuations. This could also influence the timing of local fund valuations. Discussions with MHCLG and actuarial advisers will take place shortly to consider the implications of this change.

4. Management of Employer Risk

The consultation proposes some changes to manging employer risk to reduce the risk of employers becoming insolvent when they leave the scheme.

The consultation questions whether Funds should have the flexibility to spread deficit payments, which are made on a full buy-out basis, that currently become due when the last active member leaves the scheme.

The Fund supports the proposal for regulation changes to allow flexibility on spreading repayments from exiting employers. Practically this already exists so the regulations changes are welcome.

The implications in not allowing this could be very significant for exiting employers. If an exiting employer was financially unstable, being forced to make payment of the exit termination valuation could bankrupt the employer. This debt would then fall on the remaining scheme employers. Therefore, spreading payment over a period of months or years to avoid bankruptcy seems eminently sensible.

5. Exit Credits

The consultation questions if the administering authority should take into account a scheme employers exposure to risk in calculating the value of an exit credit. This follows the Amendment Regulation changes introduced in May 2018 that have had some unintended consequences.

In response to the consultation the Fund propose the original employer (the letting employer) and the contractor, at the point of transfer, agree what will happen to any exit payment when the contract ends. If this takes place, the level of concern reduces but the Fund is in agreement that the administering authority should take into account of the employers' exposure to risk when calculating the exit credit.

The Fund fully supports not making payment of surpluses back to the contractor as standard and believes all payments should be calculated on a full buy out basis.

The implications of not making changes to the scheme rules means currently exiting contractors in surplus may receive payment back of the amount.

6. Employers Required to offer LGPS Membership

The consultation questions if Further Education corporations, sixth form college corporations and higher education corporations should be able to close the LGPS to new employees.

The Fund recognises the cost of the LGPS for some employers is becoming an increasing concern and why the chance for some employers not to offer the scheme to new members is attractive.

However, the implications of allowing this would be to create a more mature fund with less active members replacing the leavers. This will make employer contributions more sensitive to shortfalls. Without new member contributions the mature fund will have a negative cash flow meaning that investment returns play a diminishing role in reducing any shortfall.

This element of the consultation has arisen due to changes that have taken place in the further education sectors, in recent years. In the consultation the Government stresses the financial independence of these bodies:

“Reflecting the independent, non-public sector status, of further education, sixth form colleges, and the autonomous, non-public sector status of higher education corporations, these bodies are responsible for determining their own business models and for ensuring that their financial positions are sound”.

The consultation goes further reinforcing the risk to other scheme employers:

“The costs associated with meeting the liabilities of a failed organisation could therefore fall back on local authorities and other scheme employers, meaning there may be a direct impact on the finances of public bodies in a particular area if an organisation fails.”

Government is clearly indicating that they will not rescue these bodies if they were to become financially distressed. This risk is being taken into account in the actuarial valuation that is currently being undertaken.

Recommendation

It is recommended that Board notes the consultation response in the appendix.

Appendix

Response to MHCLG consultation

Equality and Human Rights Implications

None specific

Officers to Contact

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