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Please ask for: Yvonne Murphy

Date: 8 October 2020

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Dear Sirs

**LOCAL GOVERNMENT PENSION SCHEME:
AMENDMENTS TO THE STATUTORY UNDERPIN**

I refer to the above-mentioned consultation and I am responding to the invitation for comments on behalf of Wirral Council in its capacity as the Administering Authority for Merseyside Pension Fund.

The Fund is part of the Local Government Pension Scheme (LGPS) and the 4th largest of the 87 funds in England and Wales, with assets of £9bn. MPF undertakes the LGPS pension administration and investments on behalf of the five Merseyside district authorities, over 200 other employers on Merseyside and elsewhere throughout the UK. The Fund has over 139,000 active, deferred and pensioner members.

Please find attached as Annexe A, our detailed response to the 29 questions posed within the consultation.

The Fund has completed preliminary investigations on the membership and has concluded that 34 000 cases are likely to be in scope for this exercise, and this represents circa 24% of the entire Fund membership.

In finalising this response, Fund Officers have consulted with various parties connected with the Fund, including employee and employer representatives via the Local Pension Board and the Pension Fund Committee. The Fund officers have also consulted with its professional advisors

Our Response in Summary

In general, the Fund has responded positively to the questions, providing feedback on administration difficulties and challenges, whilst recognising the need to amend the statutory underpin in light of the Government requirement to remove age requirements from the current underpin qualification criteria.

However, as you will read within our detailed response, it is our Fund's view that the communication requirements to members are not only administratively burdensome but will also create considerable confusion amongst the membership of the LGPS. Indeed, the proposed requirement to publish a 'provisional underpin amount' on members' annual benefit statements is incongruous to the concept of providing 'guaranteed benefits' within the LGPS and will only generate confusion, administrative queries, and future complaints from members.

As a Fund we are adamant that the proposals for communication to members should be amended to require the provision of a narrative to members on their qualification of Statutory Underpin Protection that will be assessed at the crystallisation date, rather than a quantified amount of monies that may be subject to change in the future.

The Fund is cognisant of the significant administrative costs these proposals are putting on both the fund and employers, including the resource costs to implement the proposals, and strongly advocates the need for clear and regularly updated national guidance and template communications

Finally, I would like to offer the Fund's support to the extensive Scheme Advisory Board response to this consultation, particularly in regard to necessary amendments to the draft regulations.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Yvonne Murphy'. The signature is written in a cursive, flowing style with a large initial 'Y'.

Yvonne Murphy
Head of Pensions Administration

Enc: Annexe A – Merseyside Pension Fund Detailed Response

ANNEXE A

MERSEYSIDE PENSION FUND

AMENDMENTS TO THE STATUTORY UNDERPIN – DETAILED RESPONSE

Question		Response
1	Do you agree with our proposal to remove the discrimination found in the McCloud and Sargent case by extending the underpin to younger scheme members?	Merseyside Pension Fund (MPF) support the proposal to extend the underpin to younger scheme members who were active on 1 April 2012, which is consistent with the Court of Appeal's ruling and chimes with the Independent Public Service Pensions Commission assertion that "Age discrimination legislation means that it is not possible in practice to provide protection from change for members who are already above a certain age".
2	Do you agree that the underpin period should end in March 2022?	This is consistent with the original government commitment that members within 10 years of retirement from 1 April 2012 should be protected and to extend beyond this period would be counterproductive to the rationale for introducing the CARE benefit structure.
3	Do you agree that the regulations should apply retrospectively to 01/04/2014?	<p>As age discrimination began on 1 April 2014, in order to resolve the inequalities that exist between older and younger scheme members the regulations must be applied retrospectively. Clearly, doing so comes at a cost both in administration and the cost of the increase in benefits.</p> <p>With regard to interfund transfers, it appears that revisiting payments from ceding funds is unlikely to result in a material adjustment and could be operated on a 'knock-for-knock' basis, with the only requirement being to ensure the member record contains necessary data items for the underpin period. The administrative burden of revisiting settled cases is a complex and arduous task and as the position will not change for the vast majority of the membership, communicating this position may lead to confusion or challenge as to the value of any correspondence that does not change the status or value of the pension benefit.</p>

4	Do the draft regulations implement the revised underpin which we describe in this paper?	<p>The regulations appear to deliver the policy intent but they will cause a significant and complex administrative burden that administrators and employers will need to meet; this appears disproportionate due to the demographic profile of the LGPS and the low number of members who are likely to gain from the revised underpin protection.</p> <p>There are areas that require further clarification, such as the treatment of Pension Sharing Orders and Scheme Pays offsets. MPF supports the analysis undertaken by SAB which identify provisions that require further consideration or where the policy intent is not delivered.</p>
5	Do the draft regulations provide for a framework of protection which would work effectively for members, employers and administrators?	<p>The draft provisions are wide ranging and appear to eliminate any remaining element of potential age discrimination. However, the additional work required of employers, the onerous impact on LGPS administrators along with the associated costs should be considered regarding the context and timing of any communications.</p> <p>It is likely that a significant number of employers will not be able to provide every item of data required to calculate the underpin across all eligible members. We would therefore strongly suggest and request guidance from MHCLG/SAB be issued as soon as possible to clarify how funds should account for any missing data required to calculate the underpin and whether funds can take a proportionate approach when assessing data gaps and the demographic of the membership base, e.g. low paid part-time workers where the increased CARE accrual will likely outstrip any future earnings growth.</p>
6	Do you have other comments on technical matters related to the draft regulations?	We note that the consultation document assertion that an active member's date of death will be both their underpin date and underpin crystallisation date – this is not steadfast in circumstances where a member dies in service after their 2008 Scheme NPA.
7	Do you agree that members should not need to have an immediate entitlement to a pension at the date they leave the scheme for underpin protection to apply?	<p>Yes, we agree that the member should not have to be immediately entitled to benefits for underpin protection to apply, as the previous anomaly disadvantaged younger Scheme members and contravenes preservation requirements under the Pension Schemes Act 1993.</p> <p>As the revised underpin will now apply to qualifying members of all ages in more circumstances, with exponential administrative impact, it is crucial that SAB provide standardised wording for inclusion in the deferred benefit and CETV statements to members.</p>

		<p>However, the retrospective nature of the proposals will result in the requirement to revisit all deferred benefit and CETV calculations, which will be a mammoth exercise. Furthermore, considering the time period since 2014 it is unlikely for the majority of the membership that earnings growth will have outstripped CARE accrual and we would question the value of communicating the position at the leaving date, as this will result in confusion and queries from members. It may be more informative to use the Annual Benefit Statement to alert members that they have underpin protection which will be assessed when they access their pension benefits.</p>
8	<p>Are there any other comments regarding the proposed underpin qualifying criteria you would like to make?</p>	<p>We support the rationale that members who joined the scheme post 1 April 2012, are not defined as qualifying members. This is on the assertion that MHCLG have received a robust legal opinion that this cohort of membership cannot claim age discrimination at a future date.</p> <p>The consultation document states that those members who leave a fund without meeting the two-year vesting period would not have underpin protection. Consequently, it is assumed by this Fund that those members who aggregate membership without a disqualifying break in service <u>will</u> qualify for underpin protection, which may impact on any interfund payment made to a future fund. Clarity on this should certainly be included in the forthcoming statutory guidance.</p>
9	<p>Do you agree that members should meet the underpin qualifying criteria in a single scheme membership for underpin protections to apply?</p>	<p>We agree that the underpin qualifying criteria should have to apply in a single record along with the concept of 'relevant scheme membership'. This principle accords with other extant provisions with the requirement to aggregate membership to preserve the final salary link. It is important for administrators and scheme members that the solution adopted is both effective and straightforward, as added complexity generates confusion and additional cost.</p>
10	<p>Do you agree with our proposal that certain active and deferred members should have an additional 12-month period to decide to aggregate previous LGPS benefits as a consequence of the proposed changes?</p>	<p>As there are members with unaggregated periods of service, in the interest of fairness, these members should be given the opportunity to aggregate their records in order to preserve their underpin entitlement. We would welcome a discretion to permit administering authorities to extend the 12-month aggregation window, as there will be competing resource pressures in dealing with other overriding legislation and LGPS pension reform.</p> <p>It is also imperative that national communication materials are provided by SAB, to ensure a clear and consistent approach across the LGPS.</p>

		In addition, it should be noted that this proposal will be both onerous and problematic for funds to ensure that only qualifying members are included in the extended window to aggregate membership. Furthermore, an unintended consequence of extending the aggregation window may result in a significant change to the shape of a small employers' liabilities relative to the impact on the member's pension benefits.
11	Do you consider that the proposals outlined in paragraph 50 to 52 would have 'significant adverse effects' in relation to the pension payable to or in respect of affected members, as described in section 23 of the Public Service Pension Act 2103?	<p>There may be rare occasions where a member could argue that they have suffered an adverse effect from introducing the requirement to aggregate membership in order to retain status as a qualifying member. The provision of a 12 -month aggregation window prior to retirement may leave the member monetarily disadvantaged if the final pay increases are in excess of CARE accruals.</p> <p>Clarification is welcomed that the aggregation window should not be opened to members who opted out after 11 April 2015 and subsequently re-joined the Scheme.</p>
12	Do you have any comments on the proposed amendments described in paragraphs 56 to 59?	<p>The measures described appear to be consistent in ensuring a greater level of equality in application and appear consistent with the government's stated policy in providing protection for members and their survivors. The use of early /late retirement factors are a welcomed addition and reflect the value of the final salary and CARE benefits.</p> <p>The level of administrative activity and costs in resourcing the proposals should not be underestimated, along with the complexity of communicating the change in the underpin calculations where a protected member leaves active service, returns without a qualifying break and elects to aggregate the two membership periods.</p>
13	Do you agree with the two-stage underpin process proposed?	<p>We agree with the principle of the two stage process, acknowledging the necessity for the underpin comparison at the crystallisation date to reflect the different normal retirement ages in the two schemes with any underpin addition included in the final pension benefit.</p> <p>However, we strongly challenge the requirement to communicate a 'provisional guarantee amount', which does not change the pension entitlement at the underpin date. This will confuse members as the value will be subject to recalculation at the underpin crystallisation date and as such the proposed 'provisional guarantee amount' will not inform a member's financial planning.</p>

	<p>In addition, the inclusion of a provisional value on a deferred benefit award is counter to the premise that the LGPS provides guaranteed benefits. It will be of greater value to inform a qualifying member at their underpin date, or as part of the annual benefit statement exercise, that they qualify for statutory underpin protection and that the test will be undertaken at the benefit crystallisation date. This is preferable to communicating a quantified amount at the underpin date or on annual benefit statements.</p> <p>To manage member expectations, communications at the underpin date should highlight that the benefits payable from the CARE scheme are usually in excess of any underpin protection and typically will not result in an increase to their final pension entitlement.</p> <p>The following general points outline concerns in communicating a “provisional guarantee amount” to members:</p> <ul style="list-style-type: none"> • The requirement to revisit all past deferred benefit calculations and issue revised correspondence to members will be a huge undertaking and resource intensive. This is likely to cause confusion to members especially where the underpin does not bite at the underpin date. • Going forward the wording on deferred benefit statement would have to be clear to prevent confusion to members, as there is already a lot of information provided on both the deferred benefit statement and accompanying letter. • The inclusion in annual benefit statements of a “provisional guarantee amount” which is higher than the actual amount payable when benefits are actually taken, may result in complaints from members to the Administering Authority. Even though such complaints would in reality be unjustified, they will require staff resources to respond to individual members, in the context of their individual circumstances.
<p>14 Do you have any comments regarding the proposed approaches outlined above (point 64 to 102)?</p>	<p>The proposed process for Club Transfers places significant onus on the member as it requires them to make a decision as to how their benefits will be treated in the receiving Scheme. This will be a complex financial decision and one where the correct answer will not be known until retirement. This is likely to increase the anxiety of some members in considering whether they require financial advice, while at the same time creating an even greater requirement on administering authorities to ensure comprehensive member communications.</p>

		<p>The requirement to provide active members who remain in employment after the 2008 NPA with an underpin date calculation is questionable if they do not intend to retire. However, it is acknowledged that there would be a requirement to request the final pay calculation at the 2008 NPA to assess the underpin test when the member terminates employment and the benefits crystallise.</p> <p>It is also unclear whether it is the intent to award the 2008 Scheme NPA provisional guarantee amount to the benefit entitlement at the underpin date.</p> <p>In order to deal with the significant workloads created by the retrospective provisions, it is vital that the timeline to implement the regulations is practicable to enable system providers to deliver automated solutions to minimise manual calculations.</p>
15	Do you consider there to be any notable omissions in our proposals on the change to the underpin?	Pension Sharing Orders have been omitted and confirmation is requested that the revised underpin will not be considered for the Divorce CETV; on the basis that other financial elements of the matrimonial assets will have changed since the court made its original judgement.
16	Do you agree that annual benefit statements should include information about a qualifying member underpin protection?	<p>Yes as detailed in the response to Question 13 it would be more informative if annual benefit statements for active members include consistent narrative to inform members that they qualify for statutory underpin protection and that the test will be undertaken at the benefit crystallisation date, rather than communicating a quantified amount.</p> <p>As annual benefit statements provide illustrative values and do not incorporate any 'look back pay' provisions, the exclusion of a 'provisional underpin amount' should not devalue the use of the statement in a member's financial planning. Indeed, the inclusion of a "provisional underpin amount" could potentially mislead a member in their financial planning by indicating a higher pension than is their actual entitlement at the time they take their benefits.</p>
17	Do you have any comments regarding how the underpin should be presented on annual benefit statements?	<p>As already clearly stated and explained elsewhere in this response, we strongly believe that a provisional underpin value should not be included in annual benefit statements. If a provisional underpin value is included there may be years when the underpin applies and years when it does not which will introduce additional complexity and be challenging to explain to members resulting in disengagement and the potential for fewer members accessing or valuing the information.</p> <p>Confirmation that the member is a qualifying member and that the underpin test will apply at the benefit crystallisation date would assist member understanding that the values provided on the annual benefit statement are the minimum pension amounts payable.</p>

18	Do you have any comments or potential issues identified in paragraph 110?	We agree on balance that it is appropriate to apply the annual allowance test at the underpin crystallisation date. The alternative approach of taking a notional underpin amount into account year-on-year would add further complexity and may cause the member to breach the annual allowance in a tax year with the potential that the underpin would no longer apply at the underpin crystallisation date. It would be welcomed if a mitigation could be applied akin to that proposed in the unfunded schemes or an adjustment to reflect membership accruals backdated to 2014.
19	Do the proposals contained in this consultation adequately address the discrimination found in the 'McCloud' and 'Sargeant' cases?	Whilst the mechanics of the proposals do appear to address the McCloud and Sargeant cases, the potential for any future claims of discrimination from members who joined the Scheme after 31 March 2012 is of concern. We would seek clear assurance that Government has taken comprehensive legal advice. Any future challenge would mean Funds and employers would need to unravel the remedy which would be complex and costly.
20	Do you agree with our equalities impact assessment?	We appreciate that MHCLG and its advisors have carried out a lot of work on the equalities impact, likelihoods of outcomes and other related aspects. We are not in a position to comment any further in this area.
21	Are you aware of additional data sets that would help assess the potential impacts of the proposed changes on the LGPS membership, in particular for the protected characteristics not covered by the GAD analysis (age and sex)?	The Fund Actuary believes the cost in the GAD assessment is likely to overstate the overall cost of the remedy due to the salary increase assumption used which seems high in the current economic environment for LGPS members. It also may therefore overstate the impact on the different cohorts.
22	Are there other comments or observations on equalities impacts you would wish to make?	No further comment
23	What principles should be adopted to help members and employers understand the implications of the proposals outlined in this paper	<p>We think that standard and consistent communications across all LGPS funds will help employers and members understand the proposals.</p> <p>The Scheme Advisory Board should lead on the communication materials that should be used by LGPS funds. These should be kept up-to-date across various media and can be personalised and adapted for accessibility at a Fund level. It would be very helpful if an ongoing communications development plan was issued so it is known what is being 'worked on' and 'by when', so funds can focus their resources in the areas not being developed centrally.</p>

		<p>Our view is that the following approaches are most appropriate for the two groups:</p> <ul style="list-style-type: none"> • Members – we suggest that central example communications include, at a minimum, all scenarios that LGPS funds <u>should</u> be communicating with members. These should be straightforward and understandable. • Employers – the proposals will have a major impact on employers, so it would be helpful if appropriate materials for employer use are developed and shared nationally. <p>We would advocate for the continuation of the SAB’s McCloud implementation groups throughout the process as there will be emergent challenges, issues and clarifications sought by Funds and other stakeholders.</p>
24	<p>Do you have any comments to make on the administrative impacts of the proposals outlined in this paper?</p>	<p>While the underpin will not actually take effect for most members, the requirement to obtain the data items from employers will be resource intensive and problematic; particularly where employers cannot provide the required data.</p> <p>The requirement to retrospectively apply the underpin to members who have already retired, or left employment, is a significant challenge due to both the scale and complexity of the casework and the communication exercise.</p> <p>As such it would be helpful for MHCLG to provide direction, in the form of Statutory Guidance, in relation to reasonable timescales for the various stages of the project including:</p> <ul style="list-style-type: none"> • requiring employers to provide data as soon as is reasonably practical and no later than a defined date. It should be noted that a deadline of or around 31st March is not helpful due to year end pressures for both employers and pension funds. • provision of updated software from the software suppliers. • expected final dates for all funds to have reviewed and rectified benefits back to 2014 (deferred, pensioners, transfers out, deaths etc). <p>Clear national and formal direction will ensure funds, employers and software providers can ensure appropriate resources.</p>

25	What principles should be adopted in determining how to prioritise cases?	<p>Whilst we welcome general guidance on priorities, individual LGPS funds must be able to determine their own priorities based on the expertise, skills and capacity of each LGPS fund administration team, as progress is made throughout the implementation of the remedy.</p> <p>Our initial view of priority groups for the rectification of benefits are as below, but this should be kept under review by the administration team, whilst business-as-usual activity is maintained.</p> <ul style="list-style-type: none"> • Members closest to the underpin date to avoid recalculation of benefit • Pensioners in payment • Deaths and survivor cases • Transfers • Age 55s and over (especially in light of the recent reforms to exit pay)
26	Are there material ways in which the proposals could be simplified to ease the impacts on employers, software systems and scheme administrators?	<p>Statutory Guidance issued by MHCLG (rather than administrative guidance issues by SAB) clarifying how cases should be dealt with when member data is not available from employers would provide simplification if a practical and reasonable approach is adopted.</p> <p>Nationally defined tolerances that identify minimum thresholds before retrospective changes are made, balancing cost against impact on pension benefits could simplify the proposals and provide efficiencies for administrators.</p>
27	What issues should be covered in administrative guidance issued by the Scheme Advisory Board, in particular regarding the potential additional data requirements that would apply to employers?	<p>Clear guidance would be helpful to identify at what point the administrative costs outweigh the benefits of having 'perfect' member data records.</p> <p>This should extend to guidance for employers around their service level agreements with third party payroll providers; particularly following the end of contracts. For instance, employer guidance should prompt contract owners to give regard to data retention and accessibility to retained data by new providers.</p> <p>-A key area that would benefit from central guidance is the treatment of any back-payments made to various groups of members e.g. situations where a member and their surviving partner have both died, including clarification over interest payments/calculations.</p>

28	On what matters should there be a consistent approach to implementation of the changes proposed?	<p>Administrative guidance</p> <p>We strongly support centralised communications and a consistent administration approach achieved by the provision of national guidance, along with the continuation of the SAB working groups. This guidance and support would include communication templates and actions to take in certain circumstances (e.g. no replies, data absences, retrospective actions for pensioners, aggregation decisions).</p> <p>Auditor guidance</p> <p>It would be helpful for clear guidance to be available for auditors insofar as relates to pension fund accounting. This would be in order to pre-empt many queries and dialogue with auditors across the many thousands of employers within the scheme. This guidance should be created in partnership with CIPFA/SAB and any other interested parties and may need to be ongoing at the various stages of this process (e.g. response to consultation, potential further draft regulations, final regulations).</p>
29	Do you have any comments regarding the potential costs of McCloud remedy, and steps that should be taken to prevent increased costs being passed to local taxpayers?	<p>Funding the remedy via employer contributions</p> <p>For our Fund, the estimated impact of the remedy was calculated for all employers and was explicitly included in the 2019 actuarial valuation results for the vast majority of the employers. For those employers who did not make an allowance in their contributions plan, they should now be requested to do so. However, this requirement will be re-considered in light of any affordability constraints due to COVID-19.</p> <p>The allowances calculated at the 2019 valuation closely replicated the proposed remedy in the consultation (other than for some historical cases), so our intention is to only review costs at the next valuation. The impact did vary by employer from small-to-large, with a small number of employers not impacted at all (due to their membership profile). Equally, our Fund's FSS & Termination policies ensure that an estimate of any costs associated with the remedy are included in the exit assessment for an outgoing employer.</p> <p>This means that most funding costs have been incorporated into our funding strategy. However, this extends beyond local taxpayers as it applies to all employers, including universities who receive funding from other sources.</p>

Our view is that Statutory Guidance on McCloud should specifically require that full estimated McCloud costs are recovered through contribution requirements on both an ongoing basis for any employers who are not currently meeting the funding cost, but also in an employer exit scenario. Statutory Guidance should be clear and explicit to require fund policies and practices to be updated to ensure the final agreed remedy costs are attributed to the relevant employer and those costs are not borne by local taxpayers or any other groups. This may mean Funds may need to revisit policies prior to the next valuation.

Administering the remedy

The administrative burden is a significant one and therefore the costs relating to administration could be significant. These are split into two main areas: implementation and retrospective actions, and business-as-usual.

a) Implementation and retrospective actions

Short-term costs for Funds will be material and this includes system upgrades, additional resources, external advisor support and communication activities. The costs for employers may also be significant in terms of their own resources, including but not limited to their own system changes to extract the data from payroll/HR systems.

b) Business-as-usual

In the longer term, there is likely to be an additional cost although we would expect this to be de-minimis (largely arising out of additional system functionality) given the new processes will be fully embedded. We would not expect this to have a material effect on the employer rates in that case.

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