

LOCAL PENSION BOARD**27 SEPTEMBER 2023**

REPORT TITLE:	LOCAL GOVERNMENT PENSION SCHEME (LGPS) UPDATE- ADMINISTRATION AND FUNDING
REPORT OF:	DIRECTOR OF PENSIONS

REPORT SUMMARY

This report provides an overview of the legislative changes affecting the administration of the Local Government Pension Scheme (LGPS) along with developments in relation to the Cost Control Mechanism under section 12 of the Public Service Pensions Act 2013.

The Cost Control Mechanism seeks to equitably share the cost of the scheme between members and local taxpayers.

RECOMMENDATION/S

That the Local Pension Board be recommended to note the legislative changes to ensure the Fund's continued compliance with statutory requirements.

SUPPORTING INFORMATION

1.0 REASON FOR RECOMMENDATION

- 1.1 There is a requirement for the Local Pension Board to be fully informed of national directives and legislative developments to ensure the appropriate governance and stewardship of the Fund in its role of assisting the Scheme Manager.

2.0 OTHER OPTIONS CONSIDERED

- 2.1 This is the most appropriate option for informing the Local Pension Board of regulatory, legislative and industry developments.

3.0 BACKGROUND INFORMATION

Consultation on the McCloud Remedy

- 3.1 On 30 May 2023 the Department for Levelling Up, Housing and Communities (DLUHC) published a further consultation and draft regulations covering supplementary issues not addressed in the initial consultation on the proposed McCloud Remedy.

The updated approach as to how the underpin protection will be applied in the following scenarios is summarised below:

- Protection is to be extended to pension accounts where prior periods of membership are not aggregated.
- Protection is to be granted where a member has previous membership prior to 31 March 2012 of other public service pension schemes which has not been transferred to the LGPS.
- Protection is to be granted to benefits built up in the period to 1 April 2022 after a member takes flexible retirement prior to 1 April 2022.

- 3.2 The consultation also sought views on the following matters:

- Policies for individuals with excess teacher service.
- Compensation for those members who have suffered a loss due to the McCloud case.
- Interest terms that will apply for any late payments arising due to McCloud.

- 3.3 The above measures serve to align the remedy within the LGPS to the other Public Service pension schemes.

- 3.4 The consultation closed on 30 June 2023 and a response is now awaited. The consultation is accessible here: <https://mpfund.uk/mcccloudconsult2>

- 3.5 Final regulations are expected shortly and will be effective from 1 October 2023 backdated to 1 April 2014.
- 3.6 Fund Officers are participating in regional task groups working with other LGPS Funds, the Local Government Association (LGA) and DLUHC, with the key focus on developing national guidance to assist with operational procedures to ensure the McCloud remedy is implemented on a consistent basis across the Scheme.

Draft Legislation Issued to Abolish the Lifetime Allowance (LTA)

- 3.7 Pensions Committee considered the announcements in respect of changes to the LTA at its previous meeting on 11 July 2023. His Majesty's Revenue & Customs (HMRC) issued a consultation and draft legislation on 18 July 2023 to remove the LTA from 6 April 2024, as promised in the Spring Budget earlier this year.
- 3.8 HMRC is inviting technical comments on the draft legislation until 12 September 2023 and the consultation document is accessible here:

<https://www.gov.uk/government/publications/abolishing-the-pensions-lifetime-allowance>
- 3.9 The legislation includes transitional provisions for individuals with existing LTA protection to ensure that they retain secured rights to a higher tax-free lump sum.
- 3.10 The draft legislation introduces a new structure for Pension Commencement Lump Sums (PCLS) based on a standard tax-free maximum of 25% of the value of benefits or £268,275. Individuals will be allowed to take lump sums of a greater value, but the excess will be subject to income tax at their marginal rate.
- 3.11 A deadline of 5 April 2025 will be introduced in regard applications for 'Fixed Protection 2016' and 'Individual Protection 2016'.

Cost Control Mechanism and the 2020 Scheme Valuation

- 3.12 The Cost Control Mechanism (CCM) is a process where the Treasury (HMT) commissions valuations to assess whether the costs of the public sector schemes have increased or decreased since the schemes were reformed - from a final salary basis to a career average revalued earnings structure.
- 3.13 Where the 'cost corridor' within the LGPS, originally moved by more than 2% of pay in either direction of the target cost of 19.5% of pensionable pay with a ratio of 2/3rd employer contribution to 1/3rd employee contribution, this would require a change to benefits or member contributions, in order to bring the cost back towards the target cost.
- 3.14 The LGPS Scheme Advisory Board (SAB) undertakes a parallel valuation; the Cost Management Process (CMP), with the intention that this would be carried out before the HMT valuation, and for SAB's recommendations on changes to benefits or contributions to then be considered within the HMT valuation.

- 3.15 The first assessment of scheme costs under the main HMT CCM was undertaken as of 31 March 2016, with the provisional results showing a breach of the cost cap floor for all public sector schemes.
- 3.16 The key drivers of the breach were reductions in the assumed level of future pay increases and reductions to assumed life expectancy.
- 3.17 HMT noted that these reasons did not fit the category of 'extraordinary, unpredictable events', intended to trigger benefit rectification under the CCM. This then raised the question of whether the mechanism as designed was too volatile and the government commissioned the Government Actuary to undertake a review of the CCM for future exercises.
- 3.18 In October 2021, the Government announced that the outcome of the review would result in three main changes to the HMT CCM in order to deliver the original policy objective; specifically, to protect taxpayers from unforeseen costs and to provide stability and certainty to benefit levels.
- 3.19 The three changes made to reduce the likelihood of future changes to benefits or contributions following future cost control valuations are:
- to value only the reformed scheme design excluding experience and costs relating to the legacy schemes.
 - to widen the cost corridor where no action would be taken from 2 to 3 percent of pay.
 - to introduce an economic check, which acts as a sense check in line with forecasts of economic growth.
- 3.20 Subsequently the SAB made recommendations to Government with the aim of ensuring that the SAB CMP and the HMT CCM remain aligned in preparation for the 2020 Scheme valuation.
- 3.21 In response DLUHC issued the Local Government Pension Scheme (Amendment) (No. 2) Regulations 2023, effective from 1 June 2023, which amend the following provisions:
- Regulation 14 - the timing of the LGPS cost management has moved from three years to a four-year cycle in-line with the other public service schemes.
 - Regulation 16 - provides SAB with greater flexibility in relation to making recommendations to the Secretary of State where the 3% cost corridor is breached.
- 3.22 HMT published a written ministerial statement on 15 May 2023, providing detailed information on one of the changes to the CCM - confirming that only the reformed scheme design will be included in the cost control mechanism.

- 3.23 In terms of the LGPS, this means that the Scheme valuation will only consider service post 1 April 2014, and will disregard any McCloud underpin for service between 1 April 2014 and 31 March 2022.

The statement is accessible here:

<https://questions-statements.parliament.uk/written-statements/detail/2023-05-15/hcws771>

- 3.24 The next cost management valuations will be carried out as at 1 April 2020, with the potential for amendments to benefits provisions or member contributions from April 2024.

4.0 FINANCIAL IMPLICATIONS

- 4.1 The Government Actuary's Department, responsible for undertaking the Scheme Valuation, has indicated to SAB that due to the existence of the economic check, it is very unlikely that there will be a floor breach resulting from the 2020 valuation. This is because there is likely to be an increase in Scheme costs due to the lower economic growth forecasts used to derive the reduction in the "SCAPE" (superannuation contributions adjusted for past experience) discount rate from 2.4% to 1.7% per annum. This will offset any reductions in costs that may be observed from a slowdown in the rate of longevity improvements.
- 4.2 The cumulative cost of McCloud across employers participating in the Fund has been assessed by the actuary to be in the region of £100 million, representing 1% of the total Fund liabilities of £10.3 billion, as calculated at the 31 March 2022 triennial valuation. The costs have been incorporated within the results of the employers' balance sheets and have been reflected in contribution schedules for the period 1 April 2023 to 31 March 2026.

5.0 LEGAL IMPLICATIONS

- 5.1 The administering authority solicitor, acting for the Fund, provides advice as to the implementation and interpretation of legislative and governance requirements.

6.0 RESOURCE IMPLICATIONS: STAFFING, ICT AND ASSETS

- 6.1 The administrative requirements of the McCloud remedy will be significant with the level of additional resources to ensure compliance dependent on the complexity of the final provisions and the timely development of systems to provide bulk calculations.
- 6.2 Given the final regulations are yet to be issued, the time available prior to 1 October 2023, along with the complexities inherent within implementation of the remedy, administration teams and system providers are facing significant challenges in validating remedy data and testing the software to revisit recalculations for post-2014 leavers.
- 6.3 The changes to the taxation of benefits will necessitate procedures to be reviewed relating to the new structure for Pension Commencement Lump Sums and reporting

the correct tax on any benefits in excess of the permitted allowance for any benefit crystallisation events after 6 April 2024.

7.0 RELEVANT RISKS

- 7.1 There is a risk of miscommunication and incorrect payment of pension benefits to members if the legislative changes are not implemented in accordance with the revised regulations with an associated impact on employer costs.
- 7.2 Failure to comply with regulations may lead to sanction by the Pensions Regulator, including the possibility of financial penalties and reputational damage.

8.0 ENGAGEMENT/CONSULTATION

- 8.1 The changes to administration and governance of the LGPS are consulted on at national level by the relevant government department.

9.0 EQUALITY IMPLICATIONS

- 9.1 Department for Levelling Up, Housing and Communities (DLUHC) and the Pensions Regulator undertake equality impact assessments regarding the provisions of the LGPS Regulations and the administration and governance of public service pension schemes.
- 9.2 The Equality Statement published on the introduction of the Local Government Pension Scheme 2014 can be viewed at: <https://mpfund.uk/lgpsequalitystatement>
- 9.3 DLUHC and HM Treasury undertake equality impact assessments with regard to the statutory reform of the public sector pension schemes and LGPS.

10.0 ENVIRONMENT AND CLIMATE IMPLICATIONS

- 10.1 The Fund continues with its digital strategy across all operational areas and communications with stakeholders, with the aim to improve service delivery and to reduce its internal carbon footprint.

11.0 COMMUNITY WEALTH IMPLICATIONS

- 11.1 There are none directly arising from this report.

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BACKGROUND PAPERS

HM TREASURY Policy Paper- 15 May 2023

Public Service Pensions - Cost Control Mechanism and Reformed Scheme Only Design

<https://www.gov.uk/government/publications/abolishing-the-pensions-lifetime-allowance>

CIPFA: the guide for local pension boards

TERMS OF REFERENCE

This report is being considered by the Local Pension Board in accordance with Section 13.2(b) of its Terms of Reference:

(d) Review management, administrative and governance processes and procedures in order to ensure they remain compliant with the Regulations, relevant legislation and in particular the Code.

SUBJECT HISTORY (last 3 years)

Council Meeting	Date
Standing Agenda Item	