Warwickshire Local Pension Board

Regulatory Update

20 October 2021

Recommendation(s)

1. That the Board notes and comments on the report.

1. Executive Summary

1.1 This report seeks to update the Board on relevant regulatory developments in the pension arena.

2. Financial Implications

None.

3. Environmental Implications

None.

4. Supporting Information

Consultation on Special Severance Payments

4.1 The Ministry for Housing, Communities, and Local Government (MHCLG) issued a consultation on draft statutory guidance on the making and disclosure of Special Severance Payments (SSP) by local authorities.

4.2 The purpose of the draft guidance is to limit the use of SSP, noting the government's view that these payments do not represent value for money and should be considered in truly exceptional circumstances.

4.3 Special Severance Payments are stated as being payments to employees, officeholders, workers, contractors, and others outside of normal statutory or contractual requirements when leaving employment in public service. Examples include payments reached under settlement agreement, paid special leave such as gardening leave and payments for retraining.

4.4 Statutory and contractual redundancy payments do not constitute SSP, nor payments made to compensate for ill-health, injury, or death. However, pay or compensation in lieu of notice and pension strain payments arising from employer discretions to enhance pension benefits may be a SSP.

4.5 This means there could be implications where employers exercise their discretion to waive early retirement reductions on voluntary retirement (e.g., compassionate grounds), flexible retirement etc.

4.6 The proposals state that if an SSP is made employers should consider lower cost alternatives, public perception of the payment and the setting of possible precedents. They should also consider the impact of SSP including legal advice on the prospect of defending a claim at tribunal, so that payments are justified..

4.7 The proposals also recommend that if an SSP is made it requires that the personal approval and sign off of the Chief Executive Officer is documented with a clear record of the Leader's approval, and the guidance makes it clear that the Section 151 Officer and Monitoring Officer must be able to justify such payments. This is an issue that has been picked up by the LGA in its response as staffing arrangements are a council side function under legislation and cannot be dealt with by a member of the Executive.

4.8 Warwickshire County Council contributed to the response on that consultation submitted by West Midlands Employers.

Public Sector Exit Payments

4.9 Members of the Board will recall that regulations capping the amount payable to members retiring early were revoked earlier in the year.

4.10 Officers are aware that the Government continue to review these payments and expect further information to be issued at some time.

Cost Management Mechanism

4.11 The Cost Management Mechanism (the mechanism) was introduced following the Hutton review with the aim of providing protection to taxpayers and employees against unexpected changes (expected to be increases) in pension costs.

4.12 This would ensure that the anticipated risks of the rising cost of pensions would be fairly shared between employers and employees. The mechanism not only introduced a ceiling but also a floor so that if costs reduced then changes would be required to increase costs back to a fixed cost.

4.13 So, in 2016 when the mechanism was first utilised contrary to what was expected it was the floor that was breached and not the ceiling, resulting in improved benefits.

4.14 The recommendations were:

- Removal of tier 3 ill-health benefits, with tier 2 the minimum,
- Introduction of a minimum death in service entitlement of £75,000

- Enhanced early retirement factors
- Recommendation around changes to employee contribution bands

4.15 These recommendations were placed on-hold pending an assessment of the cost of the McCloud settlement.

4.16 HM Treasury (HMT) asked the Government Actuary's Department (GAD) to review the mechanism to determine if it is working as intended.

4.17 GAD concluded the mechanism failed to meet several key objectives and that it can lead to "intergenerational unfairness and result in perverse outcomes such as an increase in benefits to members whilst at the same time having to increase employer contribution rates," and made several recommendations to HMT.

4.18 HMT has in turn released a consultation on changes to the mechanism in which they propose to take effect from the 2020 cost management valuations:

- To remove any allowance for the legacy schemes (i.e., final salary) in the mechanism (although it proposed to include past service of the 2014 / 2015 schemes in the mechanism).
- To widen the corridor beyond which a breach occurs from 2% of pay to 3% of pay.
- Add an economic check so that changes will only be implemented to the benefits if the breach of the corridor would still have occurred had the changes in economic assumptions been considered.

4.19 Officers will keep the Board appraised of any developments.

The Pension Regulator's new Code of Practice

4.20 Members of the Board will recall that the Pension Regulator (TPR) issued a consultation document about a new combined code of practice.

4.21 The period of consultation has now ended and TPR has received over 100 responses. TPR feels that it is essential they give themselves the necessary time to consider these responses. This means TPR do not expect their full response and laying the new Code before Parliament until 2022 and the new Code to become effective in Summer 2022.

4.22 Officers will keep the Board informed of developments.

Update on the Government Actuary's Department Section 13 report

4.23 As required under Section 13 of the Public Services Pensions Act 2013, The Government Actuary's Department (GAD) has now concluded its review of the 2019 LGPS valuations and circulated a draft version of their report to the Fund Actuaries for comment. Although Hymans are not able to issue the draft report, they have provided headlines for each of the four tests undertaken by GAD.

Compliance

- There are no issues around compliance of the valuation

Consistency

- There were no issues raised about any specific fund under this measure.

- General comments (Hymans):

  - GAD still believe there is room for improvement around consistency of assumptions in the LGPS. We are seeking to ascertain whether that means GAD think a common funding basis should be used for the LGPS (something we believe would be a backward step leaving us unable to reflect local circumstances, local investment strategies and your membership profile) or if there should be further consistency around how assumptions are set. Given the process that the fund undertook to discuss and agree the funding assumptions for the 2019 valuation, this ensured that local considerations were taken into account and reflected, along with the fund's membership profile.
  - GAD also believe that further investigations should be undertaken to see if there is merit in putting in place a consistent approach to allocating assets to Academy schools upon conversion. As was our position when this recommendation was made in 2019, we believe that this should remain a local fund decision (so it can align with the fund's approach to other new employers). Furthermore, it would now be difficult to mandate a potentially different approach on funds given the large number of Academy schools that have already converted.

Solvency

- GAD carry out a series of tests on each fund to check (in their view) whether the solvency criteria is met

  - The fund received a 'white flag' under the measure of asset shock. A white flag is one where the result of GAD's test triggered an amber warning, however, upon review of the flag, GAD have deemed that the measure is no cause for action (it would have remained amber if GAD had broader concerns). The asset shock tests the required change in the average employer contribution rate as a percentage of core spending power if return-seeking assets fell by 15%. This is a relatively blunt test as it assumes that any fall would be sustained (i.e., there would be no bounce back) and ignores that in such situation the fund could change in the investment strategy instead of having to increase contribution rates. GAD estimate the increase in rate for your fund would be 3.0%, equal to the amber threshold of 3.0%. For the avoidance of doubt, we do not believe this flag should require you to have any concern over the robustness of your funding and investment strategies.

Long -term cost efficiency

- GAD carry out a series of tests on each fund to check (in their view) whether the long-term cost efficiency criteria is met
- The fund received a green flag in every test.

5. Timescales associated with the decision and next steps

5.1 None

Appendices

None

Background Papers

None

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The report was circulated to the following members prior to publication:

Local Member(s): None
Other members: n/a