



Pensions Fund Sub-Committee
08 November 2016

**Report from the Chief Finance
Officer**

For Information Purposes

Wards affected:
ALL

New Regulatory Oversight for LGPS Pension Schemes

1.0 INTRODUCTION

1.1 Recent changes brought about by the Public Services Pension Act 2013 (“The Act”) have changed the regulatory framework of the LGPS Pensions Scheme. In particular, Section 13 of The Act introduces additional measures by which the activity of LGPS Schemes is overseen by Central Government, that has in turn appointed GAD (Government Actuary Department) to be the “appointed person” to deliver that function.

2.0 RECOMMENDATIONS

2.1 To note this report.

2.2 Note that the Pension Fund will need to comply with the section 13 process, responding to all queries and requirements of Government’s Actuary Department (GAD).

2.3 Note that results on the review by GAD will come back to this Committee when GAD has completed its report (early 2018)

3.0 DETAILS

3.1 Both the Chair of the Pensions Board and the Head of Finance went to a conference in September 2016 on the impact of Section 13. Due to the complexity of the subject

matter, this briefing note was produced. It is also important to understand Brent's Pension Fund specific position in this, especially as scrutiny of the LGPS is now built in to Central Government regulations.

- 3.2 The Section 13 process was set up following the introduction of the Public Service Pensions Act 2013 ("the Act"). Section 13 of the Act sets out a new review framework that sits over the LGPS pensions across England and Wales. The legislation requires the Government Actuary's Department (GAD), as the 'appointed person' to report on whether the LGPS funding valuations comply with four criteria: Compliance, Consistency, Solvency & Long-Term Cost Efficiency. Section 13 is a review mechanism to ensure that all the valuations use appropriate assumptions but the power will still sit locally to determine appropriate contribution rates that reflect local circumstances, as 'no one size fits all'.
- 3.3 Section 13 of the Act has been a long drawn-out process with negotiations between the various stakeholders (GAD, Treasury, the actuarial companies and CIPFA, and LGA have represented Councils to date). A dry-run process reviewing funding valuation methodologies and results took place using 2013 data to determine where problems actually lay as opposed to where Government thought they did. GAD has tried to use standardised calculations to see where there were outliers. It allowed them to pick out funds at greater risk.
- 3.4 It is important to note that the dry run was not statutory but the one reviewing the current 2016 Triennial Review process will be and the results should be made public in early 2018. The main purpose of the dry run is to highlight risks and get feedback so that the statutory one will be fit for purpose.
- 3.5 Gradually, it has become clear due to the better quality of data from the dry run that many of the earlier potential recommendations revolving around tougher oversight measures have become unnecessary because the LGPS has largely been well-managed.
- 3.6 The Act explicitly gives power to the Government to force changes if necessary and both GAD and the actuarial firms have found the concept of 'Actuarial Override' problematic, as it represents a challenge to an industry that places great weight upon profession opinion. Therefore, there is a clear incentive to ensure that all actuarial assumptions and methodologies occupy a shared space of reasonableness. As far as GAD were concerned, the Act's reference to remedial measures highlighted the importance of early informal discussions with Government. However, CLG may

require the authority to report on progress and/or direct scheme manager to take remedial steps. These remedial steps potentially could range from providing additional clarity on matters to an increase in contributions with immediate effect.

- 3.7 **Compliance:** Are the valuations carried out in-line with regulations? This has genuinely not turned out to be a problem, as local government tends to be thorough at ensuring that they are compliant with laws and regulations.
- 3.8 **Consistency:** Are the valuations carried out in a consistent manner with each other? This posed a problem as the dry run exposed that inconsistencies were not always justified by local differences. Also, there were significant presentational and evidential ones but this tended to be a comment on the various actuarial companies' approaches rather than between funds, in general. It was interesting to note that the actuarial firms had significantly different estimates of funding levels dependent on the firm. Brent's still remained the lowest funding level but because GAD does not try to take a very prudent perspective, the level as calculated by GAD was significantly higher.
- 3.9 The Common Contribution Rate (CCR) was calculated differently between the actuarial firms, as were many of the other Pension measures. Even though the CCR has now been replaced by clearer (albeit still not explicit) definitions of primary and second rates of contributions, GAD decided that it needed to produce its own standardised indicators so it could compare, contrast and undertake meaningful analyses.
- 3.10- GAD felt it important to state that their indicators are about transparency and not about minimum funding requirement or a race to the bottom. It is not clear that the actuarial firms fully agree with this statement. These indicators did not take into local circumstances, such as guarantees, and highlighted the differences in assumptions and approaches between the valuation firms.
- 3.11 **Solvency:** Are the contributions sufficient to ensure the funds remained solvent? There were 10 measures in GAD's assessment to assess solvency and the report made a clear decision to target 100% funding regardless. Overall, the outcomes were very positive for most LGPS funds. Brent did not throw up any red flags, bar the known funding level issue. GAD expected that contributions will vary over time, especially for closed funds. They were also looking for plans such as asset liability matching or guarantees.

- 3.12 **Long-Term Cost Efficiency:** Are the Contributions enough to meet future demands on the Pension Fund and close the existing deficit? The important aspect of this was there was clear evidence of not deferring cost, i.e. sufficient contribution rates. Brent's contribution levels were consistent with an approach that would on the balance of things be likely to close its deficit, as long as its assumptions were realistic. However, GAD could not take the position that Brent was fine because the future is unknowable and the funding level is so low. However, its analysis did not cause any specific worries around having 'heroic' assumptions, as a few funds did.

Other Issues

- 3.13 Despite it being a dry run, challenges around data quality did not prevent some useful analysis, such as identifying those funds that may need to do greater risk modelling, review assumptions and/or contribution strategies. GAD also pointed out that it was important to take into account a basket of measures. However, getting the correct data specifications and having the appropriate data indicators are exceedingly important. Some of the measures seemed redundant or duplicative. Furthermore, a general critique from local government was that using one year's worth of contributions rather than three was flawed because different years in the three year cycle might have very different contribution rates depending on the local strategy.
- 3.14 There was clear concern from many of the Pension Fund leads around the GAD's direction of travel into looking into investment decisions versus the original focus upon calculation of liabilities and funding strategies. It was not clear that GAD had the skills to undertake this and there were worries that the investigation into asset-liability matching was outside the remit of the regulations.

Conclusions

- 3.15 Overall, Section 13 was well received as a positive piece of analysis by the main stakeholders but there were still concerns as noted above about content and certainly around messaging.
- 3.16 Brent Pension Fund was clearly flagged up as having a low overall funding level, but it was not one of those that exercised GAD. The main worry expressed was regarding those Councils with apparently low contribution rates combined with low funding levels.

3.17 However, Brent Pension Fund should not view this analysis as a sign that everything is acceptable: the 2016 statutory review is still to take place and the need to be prudent and have an appropriate funding strategy with such a large deficit still remains a challenge.

4.0 Financial Implications

4.1 There are no direct financial implications from this report. However, it is important that results from the statutory report that should be finished by the end of 2017 has the potential to override the Pension Fund contribution rates if they are deemed too low. The Funding strategy in the original analysis conducted was consistent with an approach that should within an appropriate amount of time reduce the deficit to zero, according to GAD's analysis. However, any new analysis might potentially produce different results.

5.0 Legal Implications

5.1 Section 13 of the Act provides for the setting of the rate of employer contributions in defined benefits schemes with a pension fund, most notably the funded Local Government Pension Scheme (LGPS). This section requires an actuarial valuation of the pension fund to inform the setting of the employer contribution rate. The valuation of the pension fund is separate from and in addition to the valuation of the whole LGPS scheme under section 11 of the Act. Section 13 provides for an independent review of the valuation and employer contribution rates to check that they are appropriate and requires remedial action to be taken where that review identifies a problem.

6.0 Diversity Implications

6.1 Not Applicable

Contact Officers

Persons wishing to discuss the above should contact Gareth Robinson, Head of Finance, on 020 8937 6567, Gareth.Robinson at Brent Civic Centre