



## Committee report

Committee	<b>ISLE OF WIGHT PENSION FUND COMMITTEE</b>
Date	<b>2 SEPTEMBER 2020</b>
Title	<b>CHANGES TO THE LOCAL GOVERNMENT PENSION SCHEME</b>
Report of	<b>TECHNICAL FINANCE MANAGER</b>

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### EXECUTIVE SUMMARY

1. This report provides information to committee members on recent developments in the legislative requirements, statutory guidance and requirements of the Pensions Regulator in the management of the Local Government Pension Scheme (LGPS).
2. Specifically, it covers government consultations on updated regulations to implement the McCloud remedy, the results of the 2019 consultation on restricting exit payments, the reinstatement of the cost cap mechanism and an employment tribunal decision (Goodwin) in respect of sex discrimination
3. Members are asked to note the information provided.

### McCLOUD REMEDY

4. In June 2019, the Supreme Court rejected the Government's appeal against a ruling which found that the transitional protection introduced to the firefighters' and judges' pension schemes in 2015 amounted to age discrimination for younger workers. In July 2019, the Chief Secretary to the Treasury confirmed that the McCloud judgement would be applied to all public service pension schemes.
5. The committee received a short presentation on the background of this case and the decision at its meeting on 19 July 2019. Since then information on the development of the remedy has been circulated to members as it has been produced.
6. The Ministry of Housing, Communities and Local Government (MHCLG) issued a consultation document on 16 July 2020, which sets out proposals to remove the unlawful age discrimination identified in the McCloud judgment from the Local Government Pension Scheme.
7. Similar proposals have been set out by HM Treasury (HMT) for unfunded public service pension schemes (NHS in England and Wales, NHS Scotland, Teachers in England and Wales, Teachers in Scotland, Fire in England, Fire in Wales, Fire in Scotland, Police in England and Wales, Police in Scotland, Civil Service in Great Britain, UK Armed Forces, and the Civil Service (Others)). The consultation document

for the other public service pension scheme regulations was also issued on 16 July 2020.

8. Links to both consultation documents are included in the background papers to this report. This report focusses on the LGPS proposals.
9. The remedy for LGPS extends the ‘transitional protections’ underpin that was promised to active members in 2012 who were within 10 years of normal retirement age to all other active members, regardless of age. This underpin gives a member the better of Career Average Revalued Earnings (CARE) or final salary benefits for the eligible period of service.
  - Eligibility is restricted to members who were active in the LGPS on 31 March 2012 and who went on to have membership of the CARE scheme (from 1 April 2014), without a break in service of 5 years.
  - The underpin period applies between 1 April 2014 and 31 March 2022, but ceases when the member leaves active membership or dies in service.
  - The final salary for comparison purposes applies at the point that the member leaves active status or reaches age 65 therefore preserving the final salary link beyond 2022 as long as they are accruing benefits.
10. The changes will be retrospective and will apply to anyone who has left, retired or died and who did not meet the old underpin criteria but meets the new one. In some cases, this will mean retrospectively recalculating benefits for pensioners, and paying arrears and interest.
11. The changes present a significant challenge to administering authorities and to employers, not least of which will be a major data collection exercise to enable the final salary underpin to be calculated. While benefits accruing from 1 April 2022 will be career average for all members, the new underpin will require 2008 scheme pay to be recorded for some members for the next 40 years. As well as changes to ongoing administrative systems, processes and communications, the recalculation of leavers' benefits represents an enormous task, covering retirements, deferred leavers, deaths, transfers and trivial commutations.
12. In respect of contribution rates, the Scheme Advisory Board (England and Wales) (SAB) asked Funds and actuaries to allow for McCloud costs at the 2019 valuation in England and Wales when setting funding strategies. Within the Isle of Wight Council Pension Fund the Fund Actuary based contribution rates on slightly more prudent measures – rather than adding on an explicit ‘McCloud margin’ to the contributions themselves. At whole fund level, the Fund Actuary does not expect the McCloud remedy to have a significant impact on liabilities or contributions rates - based on typical LGPS funding assumptions, they estimated that total liabilities might increase by around 0.2 per cent (or by 0.6 per cent of active liabilities), equivalent to around £0.5 billion across the whole of the English and Welsh LGPS which will have a small impact on contributions.
13. This estimate is significantly less than the £2.5 billion quoted in the LGPS consultation. This will be due to a combination of factors, with the pay growth assumption being a crucial one (the Government estimate uses CPI +2.2 per cent per annum which is significantly higher than that used by a typical LGPS fund (which might only be around CPI + 0.7 per cent per annum)). The sensitivity to pay growth

assumptions is also reflected in the impact across employers: employers with younger members will be impacted more as their membership has a longer period of salary increases compared to older members (especially once promotional increases are considered, which tend to be higher at younger ages).

14. A very early estimate suggests that approximately 4,000 members of the Isle of Wight fund could fall in scope of this remedy. However, more detailed analysis is required to specifically identify impacted members.
15. The LGPS consultation closes on 8 October 2020, and that for the other public service schemes closes on 11 October 2020.

### COST CONTROL MECHANISM

16. The HMT Cost Control Mechanism is the process introduced across public sector schemes where the benefit structure (including member contributions) is revisited from time to time to ensure that the cost of benefits remains within a 'cost cap envelope'.
17. Alongside the consultation, the Government has confirmed that:
  - the pause of the cost control mechanism will be lifted and the cost control element of the 2016 valuations process will be completed; and
  - the costs of addressing the discrimination identified in the McCloud judgment will be fully reflected in this process
18. The inclusion of McCloud in the cost envelope will reduce, or possibly even wipe out completely, the proposed package of benefit improvements that had been due to take effect from 1 April 2019 in the LGPS in England and Wales.
19. The Scheme Advisory Board (England and Wales) will also reconsider its position on the SAB employer cost cap process (which feeds into the HMT Cost Control Mechanism).

### RESTRICTING EXIT PAYMENTS

20. The government published a consultation on 10 April 2019 seeking views on regulations implementing a £95,000 cap on exit payments in the public sector. The consultation closed on 3 July 2019.
21. The government has now published its response to the April 2019 consultation on restricting exit payments in the public sector introducing a £95,000 cap on public sector exit payments. Importantly early retirement strain costs are included within the £95,000 cap.
22. The SAB has published a summary of the implications of the proposals as they relate to the Local Government Pension Scheme (LGPS) in England and Wales. A link to this document is provided in the background information to this report.
23. MHCLG will be consulting on changes to LGPS regulations 'shortly' but HMT are aiming for Regulations to be in force by end of this calendar year.

## GOODWIN DETERMINATION

24. In June 2020, the Employment Tribunal determined that providing for a survivor's pension which is less favourable for a widower or surviving male civil partner than would be the case for a widow or surviving female civil partner is discriminatory.
25. Although the determination relates to the Teachers Scheme, it is expected that it could also impact the LGPS and potentially other public sector schemes (although this is to be confirmed). Similar to McCloud, the expected remedy will have a short term impact on administration to identify, correct the pensions of and compensate survivors.
26. Initial indications are that this will impact a relatively small proportion of scheme membership, specifically survivor pensions of female members with pre-1988 service who die after 2005. No work has yet been undertaken to identify specific numbers for the Isle of Wight fund.

## STRATEGIC CONTEXT

27. The primary objective of the fund is to provide pension and lump sum benefits for members on their retirement and/or benefits on death, before or after retirement, for their dependents, in accordance with the Local Government Pension Scheme (LGPS) regulations and statutory provisions. The committee aims to operate the fund in such a manner that, in normal market conditions, all accrued benefits are fully covered by the value of the fund's assets and that an appropriate level of contributions is agreed by the employer to meet the cost of future benefits accruing.
28. The fund has agreed the following administration and governance objectives (among others) to maintain the high standards of management of the fund:
  - (a) Ensure compliance with the LGPS Regulations, other relevant legislation and the Pensions Regulator's Codes of Practice.
  - (b) Provide pension and lump sum benefits for all members, in accordance with LGPS Regulations.

## FINANCIAL / BUDGET IMPLICATIONS

### McCloud remedy

29. While there will be some financial implications for the fund from implementing the McCloud remedy, in backdating any underpaid retirement or death and survivor benefits for impacted members, the most significant impact will be on the workload of the administration team.
30. A detailed project plan will be developed for the implementation of this remedy, which will include resourcing requirements and consideration of external support requirements.

### Cost control mechanism

31. The financial implications for this will likely be borne by scheme members (in terms of revised benefit structure) or scheme employers (in terms of contribution rates), rather than a direct impact on the fund. Further information will be provided as this develops.

### Restricting exit payments

32. This is likely to have an impact on scheme employers rather than directly on the fund, however further information will be provided as the regulations are finalised.

### Goodwin determination

33. Similar to the McCloud remedy, the most significant impact is likely to be on the workloads of the administration team.

## LEGAL IMPLICATIONS

34. The Isle of Wight Council Pension Fund is required to amend its operating procedures and governance processes to ensure full compliance with legislative requirements, statutory guidance and requirements of the Pensions Regulator.

## EQUALITY AND DIVERSITY

35. The council, as a public body, is required to meet its statutory obligations under the Equality Act 2010 to have due regard to eliminate unlawful discrimination, promote equal opportunities between people from different groups and to foster good relations between people who share a protected characteristic and people who do not share it. The protected characteristics are: age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation.
36. The McCloud remedy and the Goodwin employment tribunal determination are designed to eliminate the residual age and sex discrimination inherent within existing LGPS regulations.

### RECOMMENDATION

37. Members are asked to note the update, and that future information will be provided on all items as implementation actions are developed.

## BACKGROUND PAPERS

38. MHCLG consultation document, LGPS  
<https://www.gov.uk/government/consultations/local-government-pension-scheme-amendments-to-the-statutory-underpin>
39. HM Treasury consultation document, unfunded schemes  
<https://www.gov.uk/government/consultations/public-service-pension-schemes-consultation-changes-to-the-transitional-arrangements-to-the-2015-schemes>
40. Scheme Advisory Board, Public Sector Exit Payments cap – summary  
<https://lgpsboard.org/index.php/structure-reform/public-sector-exit-payments>

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