LGPS CURRENT ISSUES

IN THIS ISSUE

NEWS IN BRIEF

2019 ACTUARIAL VALUATION (E&W)

As everyone will be aware, we have now passed the actuarial valuation date of 31 March 2019. The year ahead certainly promises to be an interesting (and busy!) one as there will be a number of challenges facing Funds and Employers, both locally and nationally, given the number of issues affecting the LGPS at the moment (e.g. McCloud, exit credits, interim valuations, etc.). All of these issues will need to be incorporated into Fund policies going forward.

Whilst membership data has not yet arrived (other than for the keenest Funds), there remains plenty for Funds to be considering at the moment in preparation for what lies ahead, namely:

- arranging preliminary results meetings to discuss snapshot funding positions at 31 March 2019 and in some cases to provide employers with provisional outcomes to assist with their budget planning.
- drafting updated Funding Strategy Statements (incorporating admission/termination policies, etc.) and beginning to plan for the forthcoming consultation exercise.
- continuing the work undertaken to date improving data quality in order to ensure the valuation data submissions are as clean and complete (and therefore as accurate) as possible.
- considering what will be required to implement/develop risk management frameworks as part of the valuation process, e.g. covenant assessments, asset/liability modelling, investment strategy reviews etc.

We are happy to assist Funds with all aspects of the valuation process (not just the boring number crunching!) and so please do discuss your requirements further with your Mercer consultant as required.

COST CAP AND MCCLOUD

On 14 May the LGPS Scheme Advisory Board (SAB) issued its guidance concerning dealing with the potential additional costs/liabilities arising from the Cost Cap process and the McCloud and Sargeant age discrimination case ("McCloud"). The full document can be found here. In practice the likely direction of the advice had been widely trailed, so it did not contain any surprises.

For the actuarial valuations, the SAB's view is that the current benefit design as set out under the existing LGPS Regulations should be used to set employer contribution rates, but that Funds and employers should be mindful of the potential extra liabilities when setting their contribution rates at the 2019 valuation. This is something that will be considered further as we go progress through the valuation process.

The McCloud position does have an impact on employer exits and the guidance suggests that it may be possible to take a more prudent approach when determining the exit position and so any payment or credit due. Funds should discuss the approach to be taken with their actuaries, and our overarching view is that the impact of the potential McCloud liabilities should be allowed for in some way that is appropriate.

CHANGES TO THE VALUATION CYCLE AND MANAGEMENT OF EMPLOYER RISK

On 8 May the MHCLG announced a consultation under the not-so-snappy title "Local Government Pension Scheme: Changes to the Local Valuation Cycle and the Management of Employer Risk". The deadline for responding to the consultation is 31 July 2019 and the full document can be found here.

The key proposals in the consultation are as follows:

- to amend the local fund valuation cycle of the LGPS from three years to four years from 2024 (with an out of cycle valuation taking place in 2022).
- to introduce powers for LGPS funds to undertake interim valuations (in full or in part) and to widen the power that allows LGPS administering authorities to amend an employer's contribution rate in between valuations.
- the introduction of a 'deferred employer' status that would allow funds to defer the triggering of an exit payment for certain employers who have a sufficiently strong covenant.
- allowing an exit payment calculated on a full buy-out basis to be recovered over a period of time for cases where 'deferred employer' status might not be appropriate.
- a review of the arrangements for paying exit credits in cases where risk sharing provisions exist within the contractual agreements with an employer.
- a removal of the requirement for further education corporations, sixth form college corporations and higher education corporations in England to offer membership of the LGPS to their non-teaching staff for new entrants.

We will shortly be submitting our own response to the consultation and will be discussing this with Funds in due course.

EXIT PAYMENT CAPS

For a number of years, the Government has been considering the introduction of a cap on the settlement payments that are made to employees when they leave an employer. These payments normally take the form of a lump sum cash payment, or in the form of shares/share options. For employers participating in the LGPS, settlement payments will also include the value or “strain” of taking an unreduced pension for members over age 55.

In April 2019, the Government issued a further consultation on the introduction of a £95,000 cap on exit payments, which confirms the overall intentions and also addresses some of the issues that need to be resolved prior to implementation. This consultation is across the whole of the public sector, not just the LGPS, and closes on 3 July.

The introduction of the cap will lead to a number of actions / complexities that administering authorities, and employers, will need to be aware of. A separate consultation specific to the LGPS is expected in due course and we will provide further comment on the implications of the exit cap to Funds at that time.

CODE OF TRANSPARENCY

The FCA established the Institutional Disclosure Working Group (“IDWG”) in 2017, with a remit to support consistent and standardised disclosure of costs and charges to institutional investors. The IDWG published a summary of their findings in July 2018, which included a recommendation to form a group to encourage and support the use of cost disclosure templates as well as monitor their use. In November 2018, this group was announced as the Cost Transparency Initiative (“CTI”).

The CTI launched its cost disclosure templates on 21 May 2019, having conducted a pilot involving asset managers and asset owners. The templates and user guides will be updated in response to feedback in 2020, but they will only be amended if essential so as not to lose asset manager support in their completion.

The objective of the CTI is for all UK asset managers to be able to publish templates in the next 6-12 months. They will be client specific, reflecting agreed terms with each investor. At this stage there is no regulation that obligates managers to complete templates, although this may change in the future. As a result, the process is reliant on pressure from the FCA, CTI, asset owners and advisors.

Of course this is alongside the work done by the LGPS Scheme Advisory Board since launching The LGPS Code of Transparency in May 2017. It was reported at the PLSA Local Authority conference in May by the SAB Chair Cllr Roger Phillips that 117 managers had signed up to the Code since the launch, and that almost 100% of listed assets were now covered. Work has been recently done on property and private equity templates, and it’s hoped that all remaining asset managers will sign up to the Code.

AVC UPDATES

Equitable Life

As part of their Spring Announcement in 2018, Equitable Life announced their intention to transfer all policies to Reliance Life, with the transfers taking place during the latter part of 2019. Reliance Life has since been rebranded as Utmost Life and Pensions Limited.

As part of the transfer deal, the Equitable Life With-Profits Fund will close and will be disinvested, initially into a deposit fund, but then into unit linked funds.

Equitable Life has recently stated that (for most investors in a policy with a 3.5% guaranteed interest rate) the Capital Distribution is now expected to increase further than the 60-70% previously expected, although full details have yet to be confirmed.

Equitable Life are now in the process of contacting LGPS Funds with further details of the proposed transfers and over the next few months Funds will need to make a number of decisions. We would recommend that Funds consider obtaining regulated investment advice to make these decisions and we will be happy to provide further assistance to Funds in this area as appropriate.

Prudential

Following an internal review of lifestyle options available to members, Prudential has decided to fully close their "Optimiser" lifestyle plans later this year. Their review took into account the impact of pension freedom changes in 2015 and also experience of how the AVC Funds were being used by all members (across all Schemes).

Once the "Optimiser" plans have been fully closed, any funds invested in these plans need to be moved to new arrangements. Members will therefore be invited by Prudential to make a decision as to which lifestyle arrangement they would like their funds to transfer.

However, in the absence of any decision made by members, Funds will need to make a decision (and notify Prudential) as to what the default lifestyle arrangement will be so the transfers can take place. We would be happy to assist Funds in making the necessary decisions and considering the wider Prudential AVC offering where necessary.

REGULATOR UPDATE – A NEW APPROACH TO GOVERNANCE

At the PLSA Local Authority conference in May, the Pensions Regulator announced its new approach to governance of LGPS Funds, under a Clearer, Quicker, Tougher mantra. Coupled with the ongoing SAB "Good Governance" review, governance is becoming an even more important subject for Funds to be focusing on, in particular now that the investment pools are all established. In anticipation of the Regulator's increased involvement in the governance of the LGPS going forwards, we will be continuing to build on the good work Funds have begun in recent years e.g. data quality, covenant, training, etc. such that Funds can ensure they are in a strong position going forwards for the benefit of all members and stakeholders.

ACTUARIAL FACTORS UPDATE

As a result of changes to the SCAPE discount rate in 2018, a number of actuarial factors (and in some cases the associated calculation guidance) have been updated and published by GAD recently, coming into effect from March/April 2019 in most cases. The factors updated include those associated with the Purchase of Additional Pension, Early Retirement, Lifetime Allowance, Pension Debits/Credits, Transfer Values and Trivial Commutation. The new factors should now be incorporated into calculation systems and routines.

Aside, a consultation on the implementation of new late retirement factors was issued in March 2019 and closed in April 2019. Alongside a change to the underlying late retirement factors, the consultation also proposed a change to the methodology for calculating late retirement pensions. A number of concerns were raised as part of our response, given the potential administrative/communication impact they would have on Funds (and also software providers) and also the monetary impact on members. From other consultation responses we have seen, these concerns have been echoed. The outcome of the consultation is now awaited.

FURTHER / HIGHER EDUCATION NEWS

Alongside potential changes to the way further/higher education employers offer membership of the LGPS to new entrants (included in the valuation cycle consultation referred to above), there remains significant pressure on employers in the sector from a funding perspective.

Indeed, it has also been announced recently that Hadlow College in Kent has become the first further education college to fall under the Government's new college insolvency scheme that was introduced earlier this year.

If Funds have not done so already, we would therefore recommend a review of the covenant of further/higher education employers participating in the Fund. For those Funds in England and Wales, the 2019 actuarial valuation exercise is an opportune time for such reviews to take place in order that the outcomes can be discussed as part of the Funding Strategy Consultation and reflected in any updated contribution outcomes from April 2020. We would be happy to assist Funds further with these reviews.

FAIR DEAL UPDATE

As mentioned in our previous Current Issues, the MHCLG had published its consultation on the "New" Fair Deal, concerning the introduction of greater pensions protection for employees of LGPS employers who are compulsorily transferred to service providers. The consultation closed on 4 April 2019 and the MHCLG is currently analysing the feedback.

We will provide you with more details on this as new information becomes available. In the meantime, if you have any queries in this area, please contact us.

UK STEWARDSHIP CODE

The Financial Reporting Council (FRC) published in January 2019 a proposed UK Stewardship Code (the Code) for wide public consultation. The consultation closed 29 March 2019 and drew in 170 companies and investors to comment on the proposed changes, including from the LGPS. The final version of the Code will be published in the summer of 2019.

"The proposed main changes to the Code include:

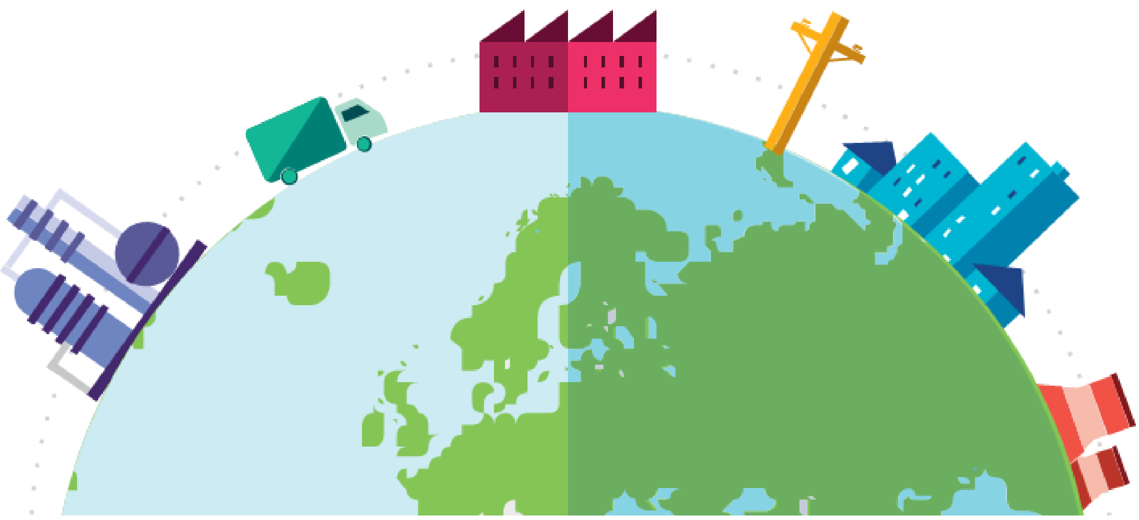
Purpose, values and culture. *Investors must report how their purpose, values and culture enable them to meet their obligations to clients and beneficiaries. This aligns the Code with the UK Corporate Governance Code and encourages embedding behaviour conducive to effective stewardship in the investor community.*

Recognising the importance of ESG factors. *The proposed Code now refers to environmental, social and governance (ESG) factors. Signatories are expected to take material ESG issues into account when fulfilling their stewardship responsibilities.*

Stewardship beyond listed equity. *The proposed Code now expects investors to exercise stewardship across a wider range of assets where they have influence and rights, in the UK and globally."*

From LGPS perspective, the Code further drives Funds to consider how stewardship delivers sustainable value - not only for beneficiaries, but the economy and society at large. Local Government Pension Schemes will need to form a view whether becoming a Code signatory is an action it wants to pursue to ultimately support the overall effectiveness of the proposed Code. Local Government Pension Schemes with their purpose, values and culture are potentially pivotal drivers of the Codes success by expressing their demand for better stewardship.

We would be happy to speak to Funds to discuss the potential impact of the new code and in particular, discuss their ESG investments given this is becoming an increasingly high profile area that Funds needs need to be addressing.



DATES TO REMEMBER

DATE	ISSUE	THE LATEST
31 July 2019	Valuation Cycle	Consultation closes
Summer 2019	UK Stewardship Code	Final version of the code expected to be published
31 August 2019	Benefit Statements	Deadline for Funds to issue annual benefits statements to members
6 October 2019	Pension Savings Statements	Deadline for issue to members
October 2019	Equitable Life	Voting on transfer decisions by eligible policyholders
2019	Pensions Dashboard	Expected to go live in 2019 (under review).
31 March 2020	2019 Actuarial Valuation	Deadline for formal reports and rates and adjustments certificate to be signed off by Fund Actuary
6 April 2020	Lifetime Allowance indexed in line with CPI	The LTA for 2020/21 to increase from £1,055,000 in line with CPI increases.
5 April 2021	Abolition of DB contracting out	End of the 5 year period during which an employer may use its overriding power to amend a scheme to reflect the abolition of contracting out.

MEET SOME OF THE TEAM

THINGS YOU MAYBE DIDN'T KNOW

Name: Michelle Doman
Role: Fund Actuary
Joined Mercer: 2001
Place of Birth: Liverpool
Favourite film: Difficult to narrow down, but a guilty pleasure would have to be the Harry Potter series.
What is your favourite animal and why?: Horses – so many reasons. Ranging from the fun of trying to race round a course of show jumps faster than fellow competitors, to what trusting creatures they are.
What did you do for the May bank holidays?: I went to visit the "World Horse Welfare" charity in Blackpool to donate some gear, eat cake and much to my other half's relief, not come back with another horse!

Name: Kieran Harkin
Role: Investment Consultant & Head of the LGPS Investment Team
Joined Mercer: April 2019 (previously joined JLT in March 2013)
Place of Birth: Stockport
Favourite film: Tough one, as I like so many films, but will go with Goodfellas
What is your favourite animal and why?: Any of the numerous birds that migrate between warmer climates in summer and winter. Why - travelling with friends and/or family to experience a change of environment twice a year and (in theory) enjoy decent weather all year round, sounds good to me!
What did you do for the May bank holidays?: We are having some house refurbishment over the summer so a lot of time was spent looking at (agreeing to!) various room designs my wife has planned.....

Name: Haris Ellahi
Role: Investment Analyst
Joined Mercer: 2017
Place of Birth: Liverpool
Favourite film: The Fast and Furious franchise (can't pick one film but the first 5 are the best)
What is your favourite animal and why?: Can't really think of one. I once had a Russian Dwarf hamster so I'll go with that.
What did you do for the May bank holidays?: Catch up on sleep – Fasting for Ramadan so need to conserve energy somehow!

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