Complete Agenda

Democratic Service
Swyddfa'r Cyngor
CAERNARFON
Gwynedd
LL55 1SH

Meeting

PENSIONS COMMITTEE

Date and Time

2.00 pm, MONDAY, 21ST JANUARY, 2019

Location

Ystafell Gwyrfai, Council Offices, Caernarfon, Gwynedd. LL55 1SH

Contact Point

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(DISTRIBUTED 14/01/19)

PENSIONS COMMITTEE

MEMBERSHIP (7)

Plaid Cymru (4)

Councillors

Aled Wyn Jones
Peter Read
Simon Glyn
Peredur Jenkins

Independent (2)

Councillors

John Brynmor Hughes
John Pughe Roberts

Individual Member (1)

Councillor
Stephen W. Churchman

Co-opted Members

Councillor David Cowans Conwy Borough Council
Councillor Robin Wyn Williams Ynys Mon Council

Ex-officio Members

Chair and Vice-Chair of the Council

A G E N D A

1. APOLOGIES

To receive any apologies for absence

2. DECLARATION OF PERSONAL INTEREST

To receive any declaration of personal interest

3. URGENT ITEMS

To note any items which are urgent business in the opinion of the Chairman so that they may be considered

4. MINUTES 5 - 7

The Chairman shall propose that the minutes of the meeting of this committee held on 08.11.2018 to be signed as a true record

5. FIXED INCOME SUB-FUNDS 8

To ask the Pensions Committee to consider and decide whether to agree to the fixed income options for Gwynedd Pension Fund in the Wales Pool

Appendix A separate for Committee Members only

The document is exempt under Paragraph 14 of Schedule 12A of the Local Government Act 1972. Information relating to the financial or business affairs of any particular person (including the authority holding that information).

There is acknowledged public interest in openness in relation to the use of public resources and related financial issues. It is also acknowledged that there are occasions, in order to protect the financial interests of the public authorities that matters related to commercial information need to be discussed without being publicised. The appendix deals with investment arrangements which are commercially sensitive and confidential to the company. Publication of such commercially sensitive information could undermine confidence of providers to engage with Council and therefore the Councils ability to invest effectively. This would be contrary to the wider public interest of securing value for money and the best overall outcome. For those reason, the matter is exempt from public interest.

6. SECURITY LENDING 9 - 13

To ask the Pensions Committee to consider and decide whether to agree to security lending in the Wales Pool

Appendix B separate for Committee Members only

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Government Act 1972. Information relating to the financial or business affairs of any particular person (including the authority holding that information).

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7. SCHEME ADVISORY BOARD COST MANAGEMENT 14 - 22

To consider the Head of Finance's report

8. PENSION ADMINISTRATION UNIT STAFFING 23 - 28

To approve additional resources to enable the Finance Department to establish a more resilient staff structure for the Pensions Unit

PENSIONS COMMITTEE 08.11.2018

Present: Councillors: Stephen Churchman, David Cowans (Conwy Borough Council), Simon Glyn, Peredur Jenkins, Aled Wyn Jones, John Brynmor Hughes, Peter Read, John Pughe Roberts (Chair), Robin Williams (Anglesey Council) and Sharon Warnes (Pensions Board - Observing)

Officers:- Dafydd Edwards (Head of Finance Department), Nicholas Hopkins (Pensions Manager), Delyth Wyn Jones-Thomas (Pensions and Treasury Management Accountant), Meirion Jones (Communication Officer - Pensions) and Lowri Haf Evans (Member Support Officer).

1. APOLOGIES

None to note

2. DECLARATION OF PERSONAL INTEREST

None to note.

3. URGENT ITEMS

None to note.

4. MINUTES

The Chair signed the minutes of the meeting of this committee, held on 19 June 2018, as a true record.

5. INVESTMENT STRATEGY STATEMENT

Submitted – a report requesting the Committee to approve the Amended Investment Strategy Statement. It was noted that the Pensions Committee had adopted the Statement in March 2017 accordance with the new legislation. It was highlighted that the statement now included the investment principles that the Committee and the Pensions Board had discussed and agreed in previous meetings, as a result of the developmental session with Hymans Robertson consultants. It was reiterated that the principles highlighted the Fund's aspirations clearly, which in turn would give guidance to the Fund's Assets Managers, as well as set the direction for discussions with the Wales Pensions Partnership joint practitioner.

In response to a question, it was confirmed that, in accordance with the second principle in the paper, the Fund would seek to invest within the Wales area when non-financial investments could derive from this, on condition that they satisfy the requirements of the fiduciary duty.

RESOLVED to approve the Investment Strategy Statement.

6. TREASURY MANAGEMENT – MID YEAR REVIEW 2018-2019

Submitted, for information, a report highlighting the Council's actual Treasury Management activity during the current financial year. It was highlighted that, during the six months between 1 April and 30 September 2018, the Council’s borrowing activity had

remained within the restrictions originally placed and there were no banks where the Council had deposited money that had failed to repay.

RESOLVED to accept the information.

7. RECONCILING GUARANTEED MINIMUM PENSIONS (GMP)

Submitted, for information, an update for the Committee regarding the work that had been undertaken to reconcile the Guaranteed Minimum Pension. Members were reminded that a team of three had been set up in January 2016 under the leadership of the former Pensions Manager, Mr Gareth Jones. With the process drawing to an end in December 2018, the Committee was notified that the Gwynedd position was comparatively good and the team was praised for its good work. It was noted that the former Manager's expertise had secured a substantial saving for the Council and it had been given to understand that other pension funds were employing expensive consultants specialising in the field, or had not taken any action and were therefore open to financial risk.

The current situation was envied that the Gwynedd Pension Fund had 119 cases designated as stalemate where the Council and Her Majesty's Revenue and Customs (HMRC) disagreed with the information submitted. The Pensions Manager confirmed that HMRC had no grounds to challenge the Council's information and that the Council was certain that its information was accurate and had evidence to prove it. The officers confirmed that the Gwynedd stalemates would be resolved in 2019 - 2020, but that the general situation with the Guaranteed Minimum Pension and stalemates was currently the subject of a Westminster Government investigation.

With the formal process drawing to an end on 31 December 2018, it was noted that any unresolved work would be transferred to the day-to-day work of the Pensions Department.

RESOLVED to accept the information and it was suggested that a letter be sent on behalf of the Committee to thank Mr Gareth Jones for the heroic work of the Reconciliation Team.

8. EXCLUSION OF PRESS AND PUBLIC

It was resolved that there is an acknowledged public interest in openness in relation to the use of public resources and related financial issues. It is also acknowledged that there are occasions, in order to protect the financial interests of public authorities that matters related to commercial information need to be discussed without being publicised. The report is specifically regarding receiving a specific offer for a software licence cost which is commercially sensitive information. Publishing commercially sensitive information of this type could undermine the provider's confidence in submitting prices to the Council and, therefore, the Council's ability to procure successfully. This would be contrary to the wider public interest of securing value for money and the best overall outcome. For these reasons, the matter was considered closed for the public interest.

9. SELF-SERVICE SYSTEM FOR PENSION SCHEME MEMBERS

Submitted – a report requesting the Committee to approve additional funding to implement and run the new Members' Self-Service system. The main reasons for the need to update the system were highlighted, and a short presentation was given comparing the old and new, and it was noted that Gwynedd would choose to host the new software on hardware within the Council. It was reiterated that negotiations with the provider were continuing in order to lower the price.

During the ensuing discussion, it was agreed that a new system would offer value for money and addressed the Council's Language Policy requirements. The officers were encouraged to continue to negotiate the price and put pressure to be able to run the system on the Council's server.

RESOLVED to approve the funding up to the total noted in the report

The meeting commenced at 2:00pm and concluded at 2:45pm

MEETING:	**PENSIONS COMMITTEE**
DATE:	**21 JANUARY 2019**
TITLE:	**Fixed Income Sub-Funds**
PURPOSE:	**To ask the pensions committee to consider and decide whether to agree to the fixed income options for Gwynedd Pension Fund in the Wales Pool**
AUTHOR:	**DAFYDD L EDWARDS, HEAD OF FINANCE**

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1. Introduction

At the Investment Panel in November 2018 the Wales Pensions Pool (WPP) Fixed Income Sub-Funds Report was one of the papers presented to the members of the Pensions Committee. A summary of the options is attached at Appendix A.

2. Fixed Income Options

As a “back-stop”, the Gwynedd Pension Fund has access to BlackRock passive fixed income, through the Wales Pension Partnership’s passive investment contract, which includes fixed income as well as equities.

However, we should first consider transferring assets to the Wales Pension Partnership’s active fixed income portfolios in early summer 2019. There are likely to be four fixed income funds, as follows:

- Global Credit Fund
- Global Government Bond fund
- Absolute Return fund
- Multi Asset Credit fund

Members at the Investment Panel agreed that the Absolute Return fund and Multi Asset Credit fund will be of most interest to the Gwynedd Fund, with Insight’s holdings likely to transfer to the Absolute Return fund, and the ‘de-risking’ portion from Fidelity likely to transfer to Multi Asset Credit.

3. Conclusion

Members are asked to make a decision for the fixed income investments for Gwynedd Pension Fund in the pool. The final selection of investment managers for each fund has not been confirmed but will be in the near future. The Committee is asked to give the Head of Finance in consult with the Chair of the Pension Committee to agree the final selection.

MEETING:	**PENSIONS COMMITTEE**
DATE:	**21 JANUARY 2019**
TITLE:	**SECURITY LENDING**
PURPOSE:	**To ask the pensions committee to consider and decide whether to agree to security lending in the Wales Pool**
AUTHOR:	**DAFYDD L EDWARDS, HEAD OF FINANCE**

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1. Introduction

At the Wales Pension Partnership Officer Working Group Meeting on 30 November 2018 there was a presentation on Security Lending as an opportunity to increase income from the equities in the funds.

2. Presentation

Russell made the proposal, explained how it works and the type of collateral that would be held.

A paper from Hymans Robertson is attached as **Appendix A**. This explains the process and why investors would lend or borrow stocks and the risks involved. The fees would help to defray some of the additional costs of operating the pool.

The slide presentation 'Introduction to Securities Lending' from Mercer Sentinel is an exempt item relating to the company's financial or business affairs which has been distributed separately as **Appendix B**.

3. Conclusion

Each fund in the Wales Pool must either allow or disallow stock-lending. If the Wales Pension Partnership wants to lend stock then all of the participating authorities must agree to that policy. Each partner fund should consider their needs to reach a decision on whether to permit stock-lending in the sub-funds.

ATODIAD A

Stock-lending: overview

Introduction

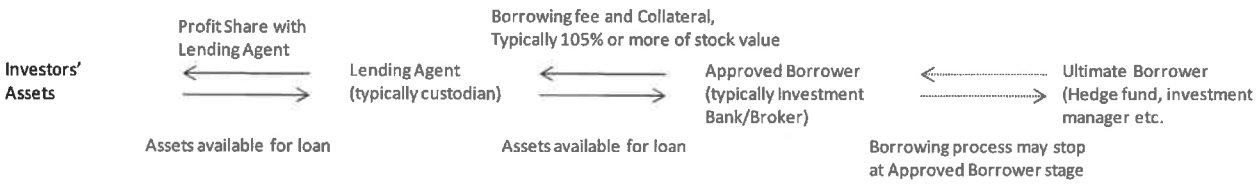
This paper has been prepared for the Officer Working Group ("OWG") of the Wales Pension Partnership ("WPP"). It provides an overview of stock-lending. Attached to this paper is a presentation that the OWG received from Mercer Sentinel on this subject. The aim of the paper, and the attached presentation, is to help WPP funds come to a view as to whether stock-lending should be permitted in one of more of the WPP's underlying sub funds. This paper should not be released or otherwise disclosed to any third party except with our prior written consent, in which case it should be released in its entirety. We accept no liability to any other party unless we have accepted such liability in writing.

What is stock lending?

Stock lending is an opportunity for investors, such as pension funds - as traditionally long-term investors, to extract a premium from their assets by providing liquidity to the market. Securities are lent to approved borrowers (typically investment banks/brokers) who pay a borrowing fee and who also transfer some form of collateral (typically cash or gilts) to mitigate the lender's credit exposure to the borrower.

An overview of the lending process is shown below (chart1).

Chart 1: Overview of lending process



The lending process is typically sub-contracted to an agent who has responsibility for recording details of stocks that have been lent and ensuring that risks are managed through the posting of collateral. Whilst the lending agent is commonly the investors' custodian, there are a small number of specialist lending agents who can provide stock lending services.

Why do people borrow stock?

Stock lending initially came about as a method to cover settlement failures, i.e. brokers would borrow stock to avoid incurring the costs and penalties associated with failed settlements. However, stock borrowing has become more widely used in the investment industry, with investors borrowing stocks to meet an array of short-term needs, including (but not limited to):

- Avoiding settlement failures;
- Facilitating tax arbitrage opportunities (i.e. where investors domiciled in different countries make mutually beneficial arrangements to take advantage of differences in tax laws). Such opportunities typically occur at the time of dividend payments;
- Supporting short-selling and hedge fund strategies;
- Upgrading asset quality to help collateralise over the counter derivatives; and
- To improve the credit quality of a borrower's balance sheet for regulatory purposes (e.g. banks)

Generally it serves a useful economic purpose in supporting liquidity in markets.

Why would pension funds lend stock?

Pension funds lend stock because:

- They receive a fee for doing so and this will help defray the additional costs of operating the pool (see comment below); and
- It supports market efficiency.

Fees are earned based on the value of the loans and the desirability of the assets (see table 1 below - the lender also receives payments from the borrower equivalent to any dividend payments made during the lending period.) Over time, stock lending programmes can be expected to generate an additional return of a few basis points on an investor's assets, with the amount of income generated from stock lending varying over time depending upon the level of borrower demand - driven by a number of factors, including portfolio composition, trading volume/patterns, lending restrictions, market activity and seasonality around dividend payments.

As well as the fees earned, another important consideration is the agreement with the lending agent on how the borrowing fees are split (also shown in table 1 below – shaded column). As well as scale of assets being lent, revenue splits can also often depend upon the level of protection the lending agent provides the lenders e.g. more protection offered the agent typically seeks a larger proportion of the revenue.

Table 1: Example fees and revenue split

Annualised Fee Rates	Revenue splits
• 5 basis points (bps) on general collateral trades • 20 bps on term lending of fixed income • 50 bps on certain emerging markets equities • 100+ bps on "specials" that are in demand and hard to find	• The agent bank generally takes a gross fee from the borrower, then splits the fee with the lender by an agreed percentage (larger % to the lender): • 60%-40%: historically typically seen in many pooled funds • 70%-30%: more usual for segregated lenders and some pooled funds • 80%-20%: for larger segregated accounts of $1+ billion of lendable assets • 90%-10%: for the very largest accounts with $25+ billion • 100%: very rarely, for the largest sovereign wealth funds, on a tiered basis

Source: Mercer Sentinel

On the face of it, for the WPP, a fee split of 80:20 or more would be a positive outcome (most sub-fund mandate sizes are sub-£1bn) - subject to the Funds being satisfied with the indemnity agreements that are being offered by the provider.

What are the risks involved?

The risks below are managed by the lending agent operating the stock lending facility.

Risks	Mitigating the risk
Borrower risk - the risk of the borrower defaulting on a loan	The lender should only enter into stock-lending agreements with borrowers they are comfortable lending to. Ultimately this is controlled by the lending agent's approach to assessing and managing counterparty credit risk.
Intraday settlement risk – the risk of the securities which are lent being delivered to the borrower before collateral is received.	The lender can specify that collateral is received a day before the loan settles. On maturity of the loan, the lender should ensure that their shares are returned prior to or in conjunction with the collateral being released back to the borrower.
Legal risk – the risk that the contract in place does not provide sufficient protection to the lender in the event of the borrower defaulting.	In most cases, it is recommended that lenders seek professional advice when reviewing contracts. Any agreements signed with the borrower should adhere to commonly used market standard documentation.
Collateral risk – the risk that the value of the collateral the loan requires is below the replacement cost of the stocks on loan.	We would expect and require collateral to be greater than the value of the stocks on loan (typically 105% or more in the current market). Collateral positions can be reviewed daily. The lender should ensure their collateral policy specifies the types of assets which can be used as collateral.
Cash collateral risk – the risk that on re-investment of the cash collateral, the lender suffers a loss.	The lender should be aware of the level of credit and liquidity risk involved in the investment of cash collateral in the event of these investments needing to be sold at short notice. The lending agent's s investment guidelines should provide an appropriate level of risk and return and be consistent with the investment guidelines agreed with the lender. t.
Operational risk – the risk of operational matters involved in the day-to-day running of the lending.	Agreements between the lender and borrower should clearly state which party takes responsibility for which operational risk and in what circumstances. All parties should ensure that robust procedures are developed in order to protect against such risks.
Loss of voting rights	Securities out on loan cannot be voted by lenders. However lenders can, if they wish, recall the securities by the record date in order to exercise their votes. The right to recall securities on loan is enshrined in the legal agreement underpinning securities lending activity, Beneficial owners can adopt one of several positions with regard to votes and recalls: • voting and recalling all or some securities at every opportunity • voting and recalling securities only on certain votes • not voting (i.e. not recalling positions) • maintain a "buffer" position in each holding to ensure an efficient flow of information from the issuer and vote every security.
Other risks – any non-financial risks, such as reputational risks.	The lender should ensure stock lending conforms to their policies and investment objectives.

Summary and next steps

Summary

Stock lending is carried out widely by local authority pension funds e.g. stock lending occurs in a number of the leading passive managers' pooled funds (including BlackRock). However, within the WPP, only one of the eight partner funds currently stock lends in their actively managed funds.

We are seeing a number of LGPS funds revisit their policy on stock lending, as part of the move to pooling. This is in part due to the need for collective agreement and a common policy within their pools, but also due to the collective scale offering much more competitive terms, in terms of revenue split, than was typically available previously at an individual Fund level.

Whilst there are risks associated with stock lending, there is no such thing as a 'free lunch', overall we are broadly comfortable with funds stock-lending, subject to the agent having suitable risk management arrangements in place and offering appropriate indemnities.

Next steps

Each sub-fund in WPP's ACS must either allow or disallow stock-lending. If some investing authorities wish to stock-lend and others do not, then it would be necessary to have two sub-funds – one which stock-lends and one which does not. In order to avoid "doubling" the number of sub-funds and avoid any associated increase in costs, the WPP would prefer to have a single, common policy on stock-lending.

It follows that if the WPP wants to lend stock then all of the participating authorities must agree to that policy. If any authority decides it does not wish to stock-lend, then that policy will be built into the prospectus for the given sub-fund and no investing authorities will be able to access the additional revenues from stock-lending. It is therefore important that each partner fund considers their needs, alongside the points raised in this paper and the appendix, to reach a decision as to whether they are willing to permit stock-lending in the sub-funds that they will invest in.

In the event that the administering authorities agree in principle to have stock-lending on the ACS sub-funds for the WPP pool, we would recommend WPP takes advice from specialists in stock-lending (e.g. Mercer Sentinel) on the stock-lending agent (eg Northern Trust has been proposed as agent by Link) and reviews the competitiveness of the fee split proposed, the quality of the indemnities offered and the proposed Stock Lending Agreement.

We look forward to discussing this paper with you in the near future.

Prepared for, and on behalf of, Hymans Robertson LLP

William Marshall and John Wright

December 2018

General risk warning

Please note the value of investments, and income from them, may fall as well as rise. This includes but is not limited to equities, government or corporate bonds, derivatives, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of investments. As a result, an investor may not get back the full amount of the original investment. Past performance is not necessarily a guide to future performance

Meeting:	Pension Committee
Date:	21/01/2019
Title:	Scheme Advisory Board Cost Management
Author:	Dafydd L Edwards, Head of Finance and Meirion Jones, Senior Communication Officer
Purpose:	For information only

1. Introduction

On 21/12/2018 the Scheme Advisory Board (SAB) issued an update on the cost management process. The full update can be seen in Appendix 1, however a summary can be seen below as well as the view of our Actuary, Hymans Robertson.

2. Scheme Advisory Board (SAB) Cost Management

Cost management for the Local Government Pension Scheme (LGPS) in England and Wales is taking place in the contex of a public service pension scheme wide cost cap review under HM Treasuary directions.

As the LGPS is a funded scheme, it has a separate cost management process to all other public service pension schemes.

Based on work undertaken by the Board's actuarial adviser, the total cost of the scheme (employer and employee) under the Board's process is 19% against a target total scheme cost of 19.5%.

The Board agreed to delegate to the Chair and a representative from both the employers and employees' sides, assisted by a small technical group, responsibility for agreeing a package of benefit changes to return the scheme to its total target cost of 19.5% while also looking at employee contributions at the lower end.

In order to achieve this, changes to benefits must be made. Section 3 below gives a summary of the proposed changes.

3. Proposed changes/recommendations

The following package of benefit improvements and employee contribution reductions were submitted to the Secretary of State on 16th November 2018. Since then discussions have taken place with the minister and his team and further legal and equality impact advice has been obtained.

Ill health:

- Removal of the third tier of ill health retirement (amendment required to Regulation 35)

Death in service:

- Introduction of a minimum lump sum death in service benefit of £75,000 per member (amendments required to Regulation 40)

Early retirement:

- Enhanced early retirement factors for all members who are active on 1st April 2019 in respect of their final salary linked membership only. Following further legal advice obtained by Government an amendment to this recommendation was agreed and submitted on 12th December. The recommendation now is that, within the same cost envelope, enhanced early retirement factors should be applied to all service of all members active on 1st April 2019 (new actuarial guidance required).

Employee contributions:

- A new 2.75% band at pay of £0 to £12,850. This new band reflects the lack of any pension tax relief for levels of pay below the new personal allowance.

- An expansion in size but reduction in rate of the current band 2 (5.8%). This would now go from £12,501 to £22,500 and be at a rate of 4.4% benefitting lower paid members.

- An expansion of the top of current 6.8% band from £45,200 to £53,500 to reflect the increases in the higher rate tax allowance since the bands were introduced in 2014.

4. Estimated financial impact of the package

The revision back to revaluation of pension accrued to the start of the scheme year is estimated to be a **reduction** in the future scheme cost of 0.4% of payroll.

This package of recommended benefit improvements is estimated to **increase** the total future service cost of the scheme by 0.5% of payroll.

Within that total it is estimated that the reduction in the employee contribution yield as a result of the new bands will be 0.8% of payroll in 2019-20 with a potentially equivalent **increase** in employer contributions.

All other things being equal the above package would see net increases in average employer future service rates of 0.9% of payroll.

However all other things are not equal and few employers pay the average rate therefore the actual impact for each scheme employer will depend on the outcome of the 2019 valuation process and in particular;

- The view taken by the fund actuaries of the costs of each element of the package
- The membership profile of each employer; with those with higher paid full time staff possibly seeing a smaller upward pressure on contributions and conversely those with a very large proportion of staff earning less than £12,000 potentially seeing a much higher upward pressure possibly in excess of 2%.
- The extent to which the costs are mitigated by other factors such as the falling away of future longevity increases

5. The next step

The SAB is advisory only. The ultimate decision on the final package of amendments rests with MHCLG. It is likely that a consultation is due to be launched in late January/early February, and by necessity will have to be short as the amendments are effective from 1 April 2019 (this date is being driven by HM Treasury and will apply to all public sector pension schemes).

SAB say in their note that they would like MHCLG to issue a letter of comfort to give funds and software providers as much notice as possible of the changes ahead of the effective date.

6. View of the Actuary

The initial thoughts of our Actuary on the announcement are:

- The validity and effectiveness of the whole cost management approach can be discussed at great length. It does seem odd to be awarding benefit improvements at a time when public sector pension costs are the highest they have been for a long time. This has been recognised by HMT who have committed to reviewing, at some point in the future, the cost management approach to see if it meets the current policy intent.

- The presence of the SAB cost management valuation is good news for the LGPS. No other public sector pension scheme has a SAB mechanism in place and as such those schemes are fully exposed to the results of the HMT cost management valuation which has seen cost savings between 3-5% of pay (compared with SAB's saving of 0.5% of pay) and significant proposed improvements to accrual rates. Hopefully, the proposed package of benefit and contribution changes will be sufficient to ensure that the results of the HMT cost management valuation on the LGPS are such that no further and significant benefit improvements are not triggered.

- The estimated cost of the impact of the proposed changes are at scheme level. However, the LGPS is funded at employer level and this is where the changes will be realised. Due to some of the more significant changes (employee contribution rates and death in service) being focussed at the lowest paid members, it follows that those employers with more lower paid staff than the national average will see higher increases. For example, if all of an employer's staff earn less than £12,850 p.a. then the employer contribution rate will increase by 2.75% of pay due to this change alone. It would have been preferable, and more equitable, from an employer's point of view if the proposed changes were consistent across the whole membership.

- The compressed timescale is disappointing and we would question if it allows any real consultation to take place. Given that these changes will have a direct and, in some cases, significant impact on actual benefits, administration and funding, we would have hoped for a longer period to consider the proposals, discuss alternatives and allow time to communicate them to members and employers. Funds will also be under real pressure in an already busy period to update administration systems and routines to cope with the changes to benefits.

Hyman Robertson are currently considering the proposals in more depth and will be providing a more detailed note in the forthcoming weeks.

Appendix A

THIS DOCUMENT DOES NOT IN ANY WAY CONSTITUTE CONFIRMED POLICY NOR DOES IT IN ANY WAY PREJUDGE THE OUTCOME OF ANY FORTHCOMING CONSULTATION PROCESS. IT IS DESIGNED TO GIVE ADMINISTERING AUTHORITIES AND SCHEME EMPLOYERS INFORMATION REGARDING THE PROPOSALS SUBMITTED BY THE LGPS ADVISORY BOARD IN RESPECT OF THE COST MANAGEMENT PROCESS. NO LIABILITY IN ANY FORM CAN BE ACCEPTED BY THE LGPS ADVISORY BOARD OR ANY OF ITS MEMBERS IN RESPECT OF ANY ACTION TAKEN BASED ON THE CONTENTS OF THIS DOCUMENT.

Local Government Pension Scheme Advisory Board
SAB Cost Management

Context

1. Cost management for the LGPS in England and Wales is taking place in the context of a public service pension scheme wide cost cap review under HM Treasury directions. In the other schemes indicative outcomes have seen breaches of the cost cap floor requiring benefit improvements in excess of 3% of payroll.

2. The closest comparable public service scheme undergoing the cost cap process this year is LGPS in Northern Ireland which has recently commenced a consulation on a benefit improvment package costing 3.2% of payroll.

3. LGPS in England and Wales has a separate cost management process which is completed prior to finalisation of the HMT cost cap calculations.

Board cost management outcome

4. At the Board meeting of the 10th October it was noted that, subject to agreement by government to return the scheme design to that agreed in 2013 by the employers and scheme members in relation to the annual revaluation of CARE benefits, the outcome of the Board's cost management process was a total scheme future service cost of 19%. As the target for the process is 19.5% the Board agreed to consider recommendations to return the total cost back to the target.

5. It was further agreed that a Board sub group consisting of the Chair, Vice Chair and an employer representative would consider a package of benefit improvements sufficient to return the total cost back to 19.5% and such further changes to employee contributions within that total cost necessary to obtain the support of both employer and employee representatives of the Board.

6. The Board agreed that options for changes to benefits should be limited to Third Tier Ill Health, Lump sum death grants, Early Retirement and Commutation. These being elements which were both of interest to scheme members and affordable within the 0.5% target cost increase. Any changes to employee contribution rates were to be targeted principally at the lowest bands but also seeking to address existing anomalies with regard to pension tax relief at both the personal and higher rate allowance points.

Consideration of options

7. In order to provide the Board sub group with the information necessary to come to a view a small technical group consisting of representatives of both scheme member and employers as well as the secretariat was formed. This group received actuarial input (in the form of technical advice from MHCLG's GAD adviser and independent actuarial advice from

the Board's actuarial adviser) and legal views from Eversheds (in particular with regard to potential discrimination issues) and considered a number of options around the elements agreed by Board.

8. The secretariat also held discussions with LGPS actuarial firms in order to get a very broad feel of the potential actual impact at fund and employer level of the various options.

9. The following proposals were put to the Board for agreement.

Ill health

10. That the removal of the third tier of ill health (costed on the assumption that tier 2 would be awarded in these cases) should be recommended.

Death in service

11. That due to the high cost and low perceived benefit a small improvement to the existing lump sum death in service benefit (3 x pay) for all members was not appropriate for recommendation. However a targeted improvement via the introduction of a minimum payment of £75,000 (per member) was.

Early Retirement

12. A number of options on enhanced early retirement factors were considered including limiting the enhancements to various groups of members or sections of the scheme. Following legal opinion on the potential for challenge to a number of options on the grounds of age discrimination two options were put forward to the Board; application of equal enhancement to all members in all sections of the scheme and targeted enhancements to final salary section benefits.

Commutation

13. Given the potential cost of a membership wide increase together with the potential for confusion and administrative overhead of limiting commutation improvements to a particular group of members or section of the scheme this option was not considered to be a priority and therefore no recommendations were made to the Board in this area.

Employee contributions

14. Based on costing information provided, six options for changes to employee contribution rates were considered. The objective for the options was to find one that most closely met the dual ambition of removing tax relief anomalies (where net contributions are lower after an increase in pay because of the effect of pension tax relief) and providing a real reduction for the lowest paid members.

15. The option that most closely met these ambitions was agreed to be;

- A new 2.75% band at pay of £0 to £12,850. This new band reflects the lack of any pension tax relief for levels of pay below the new personal allowance.
- An expansion in size but reduction in rate of the current band 2 (5.8%). This would now go from £12,501 to £22,500 and be at a rate of 4.4% benefitting lower paid members.

- An expansion of the top of current 6.8% band from £45,200 to £53,500 to reflect the increases in the higher rate tax allowance since the bands were introduced in 2014.

16. It was also proposed to the Board that moving the bands out of regulation and into guidance would in future years enable a more effective tracking of changes to pension tax relief as well as providing a more effective and speedier means to meet the target yield.

17. The Board sub group considered these options and obtained agreement by the employee and employer representatives on the Board.

Recommendations of the Board

18. The following package of benefit improvements and employee contribution reductions were submitted to the Secretary of State on 16th November. Since then discussions of taken place with the minister and his team and further legal and equality impact advice has been obtained.

a) Removal of Tier 3 of Ill Health (amendments required to Regulation 35)

b) A minimum lump sum death in service benefit of £75,000 per member (amendments required to Regulation 40)

c) Enhanced early retirement factors for all members who are active on 1st April 2019 in respect of their final salary linked membership only. Following further legal advice obtained by Government an amendment to this recommendation was agreed and submitted on 12th December. The recommendation now is that, within the same cost envelope, enhanced early retirement factors should be applied to all service of all members active on 1st April 2019 (new actuarial guidance required).

d) Removal of contribution bands from regulations replaced by reference to guidance (amendments required to Regulation 9)

e) Introduction of the bands shown below for 2019-20 (new guidance required)

Band	Pensionable Pay from £	Pensionable Pay to £	Contribution rate
1	0	12,850	2.75%
2	12,851	22,500	4.4%
3	22,501	36,500	6.5%
4	36,501	53,500	6.8%
5	53,501	64,600	8.5%
6	64,601	91,500	9.9%
7	91,501	107,700	10.5%
8	107,701	161,500	11.4%
9	161,501		12.5%

Estimated financial impact of the package

19. The revision back to revaluation of pension accrued to the start of the scheme year is estimated to be a **reduction** in the future scheme cost of 0.4% of payroll.

20. This package of recommended benefit improvements is estimated to **increase** the total future service cost of the scheme by 0.5% of payroll.

21. Within that total it is estimated that the reduction in the employee contribution yield as a result of the new bands will be 0.8% of payroll in 2019-20 with a potentially equivalent **increase** in employer contributions.

22. All other things being equal the above package would see net increases in average employer future service rates of 0.9% of payroll.

23. However all other things are not equal and few employers pay the average rate therefore the actual impact for each scheme employer will depend on the outcome of the 2019 valuation process and in particular;

- The view taken by the fund actuaries of the costs of each element of the package
- The membership profile of each employer; with those with higher paid full time staff possibly seeing a smaller upward pressure on contributions and conversely those with a very large proportion of staff earning less than £12,000 potentially seeing a much higher upward pressure possibly in excess of 2%.
- The extent to which the costs are mitigated by other factors such as the falling away of future longevity increases
- The extent to which the costs are amplified by other factors such as reductions to future service discount rates
- The upward or downward pressure of changes to employer deficits on the total employer rate

Next steps on Board cost management

24. It was hoped that agreement could have been reached with MHCLG on these recommendations and a consultation launched before Christmas. For a number of reasons this has not proved possible, however, it is anticipated that such a consultation will be published in late January/early February for regulations to take effect from 1st April.

25. The Board has made representations to MHCLG and HM Treasury that meeting the implementation date of 1st April 2019, will be significantly challenging for administering authorities and have proposed putting back the implementation date if possible. However, indications are that due to the requirements placed on all public service pension schemes the 1st April implementation date will not be changed

26. The Board has strongly suggested to MHCLG that -

(a) the consultation be as short as is possible and

(b) a letter of comfort is issued as soon as is legally possible to allow administering authorities and software providers to anticipate the changes to regulations and employers to implement new contribution rates.

27. In the meantime, the Board advise that authorities begin preparations for the above changes including taking a view on advising their employers of the proposed contributions rates. Without preempting regulatory changes it may be prudent to put in place the necessary preparations to avoid changing bands on 1st April under current regulations then retrospectively making further changes to bands and rates resulting in contribution overpayments. Doing so could enable employers to take immediate and full advantage of any letter of comfort issued prior to regulations in this area.

28. You may also wish to make employers and members aware of the proposed changes to ill health and early retirement with effect from 1st April so that decisions can be made in light of the proposals.

29. The Board secretariat will contact software suppliers and major payroll providers to assess the changes required to systems to implement these proposals. In particular to determine the most effective way to introduce enhanced early retirement factors with the absolute minimum impact on administrative processes.

30. The secretariat will review the NI database to ensure it can provide the necessary membership information to ensure that minimum death in service lump sums are appropriately limited where multiple active membership records exist across funds.

31. The secretariat will also work with fund actuaries to ensure the proposed changes are able to be appropriately accounted for in the coming valuation.

32. At its last meeting the LGPS Technical Group, consisting of representatives from the regional Pension Officer Groups (POGs), agreed to form a working group early in the New Year to further assess the administrative implications of the proposals and provide information and advice to administering authorities.

Next steps on MHT cost cap

33. The HMT cost cap process will be completed once the outcome of the above proposals and subsequent consultation is known.

34. If the proposals are not accepted by government either prior to or following a consultation then the HMT process will complete without having to take account of any changes to scheme design when determining if the cost floor has been breached.

35. If the proposals are accepted and submitted for legislation, the HMT process will take the changes into account when determining if the cost floor has been breached.

36. In either case if the cost floor is breached changes to benefits will be required under the terms of the Public Service Pension Schemes Act 2013.

Jeff Houston
Secretary to the Local Government Pension Scheme Advisory Board (England and Wales)

If you have any questions please contact the Board Secretariat on any of the following email addresses. Please note you will get an out of office from the team over the Christmas period but your email will be picked up and will be responded to as quickly as possible.

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21st December 2018

Meeting:	**Pensions Committee**
Date:	**21/01/2019**
Title:	**Pension Administration Unit Staffing**
Author:	**Nicholas Hopkins – Pensions Manager**
Recommendation:	**Approve additional resources to enable the Finance Department to establish a more resilient staff structure for the Pensions Unit**

Background

1 As reported to previous Pensions Committee meetings, due to the increasing complexity of administering the Local Government Pension Scheme, there is increasing pressure on the staffing resources. This report seeks the Pensions Committee's approval of additional resources to enable the Pensions Administration Unit to efficiently cope with the level of work that is now required.

2 Pressure of work has increased continuously, due to –

- the ever increasing complexity of introducing the CARE scheme from 1/4/2014,
- the problems of Assumed Pensionable Pay and the final salary link retaining the old meaning of pensionable pay under the regulations prior to April 2014,
- the increasing pressure from various departments, such as MHCLG, the Pensions Regulator, Government Actuaries Department, LGA, and all the Actuarial consultants for accurate data,
- the challenge of obtaining accurate, timely data from employers.

3 Meanwhile, the resources of the Pensions Administration Unit has been largely unchanged for several years, other than the temporary 'GMP' staff.

Review of Staffing of the Pensions Unit

4 To improve the efficiency of the Pensions Administration Unit, a structural adjustment to the section's staff structure is proposed.

5 Also, to deal with the additional work pressure, it is proposed to increase the section's staff resources, by establishing 4 permanent new posts.

6 The new posts include a Systems Assistant (presumed at the S1 grade, salary £23,013 pa, subject to pending job evaluation) to assist the Systems Officer with all data input queries from employers, and 3 new Pension Assistant posts (presumed at the GS5 grade, £18,592 pa, again subject to job evaluation).

7 Further, it is proposed to permanently retain the temporary grades of the 3 staff that were previously seconded to higher salaries whilst the GMP reconciliation process was in place. These postholders will all continue to do higher tariff work within the section. Two posts that were previously both GS5 (£18,592 pa) would be regraded upwards to S1 (£23,013 pa), while one post that was previously S1 (£23,013 pa) would be regraded upwards to S2 £25,355 pa.

8 Following the recent resignation of the current Systems Officer, it is also proposed to down grade that post from S4 (£30,624 pa) to S3 (£28,101 pa), in line with the current Senior Pensions Officer's post, saving £2,523. That requires a Senior Communications Officer post to be regraded to grade PS1 from S3 at a cost of £6,665, to reflect the additional overall systems management responsibility taken from the Systems Officer post.

9 The proposed structure is shown in Appendix 2 (for information the current structure is shown in Appendix 1).

10 It should be noted that within the revised total cost of £121,120, an ongoing amount of £65,628 is included for temporary staff since the 1st January 2016.

11 The revised total costs also includes the £15,231 that the Fund has been paying to the seconded staff since the 1st January 2016.

Resources Required

12 The proposed costings are as follows and includes the employer's on-costs (NI and pension contributions).

13 Create 4 new posts as follows:-

Details of post	Proposed scale	Full time annual pay	On cost
1 Systems Technician	S1	£23,013	£7,168
3 Pension Assistants (£18,592)	GS5	£55,776	£16,704
		Annual total	£102,661

14 Keep seconded staff on permanent grade as follows:-

Details of post	Proposed scale	Full time annual pay	On cost
2 GS5 to S1 Pens technician	S1	£8,842	£3,200
1 S1 to S2 Pens Officer	S2	£2,342	£847
		Annual total	£15,231

15 Senior Communications Officer post to be regraded from S3 to grade PS1

Details of post	Proposed scale	Full time annual pay	On cost
S3 to PS1 Senior Comms Officer	PS1	£4,893	£1,772
		Annual total	£6,665

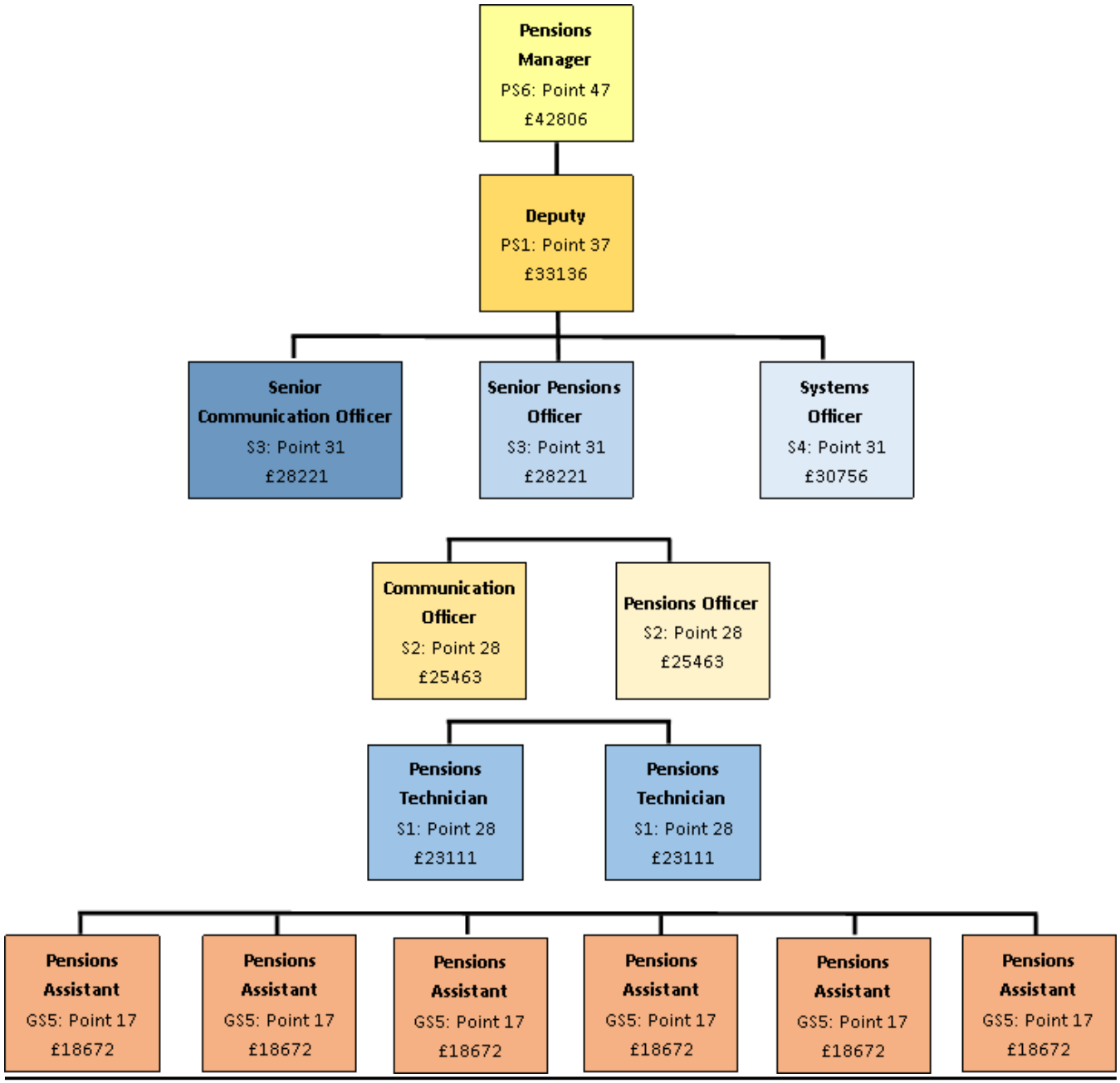
16 Downgrade Systems Officer post to S3 from S4

Details of post	Proposed scale	Full time annual pay	On cost
S4 to S3 Systems Officer	S3	(£2,523)	(£914)
		Annual total	(£3,437)

Recommendation

17 Members are requested to approve the increase in budgeted expenditure to enable the Finance Department to establish a more resilient staff structure for the Pensions Unit at a cost of £121,120 and ask the Head of Finance to implement an appropriate revised staffing structure for the Pensions Unit as soon as practically possible, in order to manage business risks and pressures.

Appendix 1 – Current Structure



Appendix 2 – New Structure