Local Government Newsletter

July 2018

Welcome to the July 2018 edition of the newsletter.
I hope you enjoy reading this edition.

Becky

People News

This summer Scott has swapped his running shoes for some cycling shoes to cycle from Land's End to John O'Groats! Scott will be setting off on 11 August and will be cycling approx. 1000 miles across the country over 9 days. He is being joined by four friends; three of whom will be cycling and one carrying out the crucial role of driving the support vehicle. They are raising money for Hospice UK, a charity that has provided great support to various family members of the group – they have currently raised over £1,000. Scott is hoping for the good weather to continue although ideally the temperatures will drop a bit! Look out for a report of the ride in next month's Newsletter.

Talking points

Carillion and the impact on outsourcing

The Public Administration and Constitutional Affairs Committee has published its latest report, [After Carillion: Public Sector Outsourcing and Contracting].

The Committee found that the Government's overriding priority for outsourcing is spending as little money as possible while forcing contractors to take unacceptable levels of financial risk, and it recommends greater transparency, and calls on the Government to commit to underpinning contracts with realistic assessments of cost and risk transfer. The Committee calls on the Government to collect evidence about the benefits and disadvantages of outsourcing in general as well as for individual services, and use this evidence as the basis for transparent outsourcing decisions.

While this report is primarily looking at outsourcing from central government, any changes to outsourcing from central government is likely to have a knock on impact on local authority outsourcing decisions.

Aon webcast and SAB guidance on scheme specific data

Many thanks to those of you who joined us in our webcast at the end of June – we had representatives from nearly 50 different funds dial in which was a fantastic turnout!

During the webcast, Bob Holloway from SAB shared the news that the list of the scheme specific data that funds should measure <u>will not be completed</u> in time for the 2018 scheme return deadline. Based on feedback from software providers, it would have been a significant challenge to agree the required data items and get the changes to the existing data testing systems programmed in time for funds to test the data and submit by the scheme return deadline in October 2018.

An initial scheme specific list proposed by GAD and SAB has been sent to funds and the software providers to respond to LGA with any comments. This list will be refined and likely reduced to a set of absolutely essential items, in a project to be taken forward by the SAB over the next year. The full list of scheme specific data items and the guidance on what and how to test the existence and accuracy of those items should be available to all funds in advance of the 2019 scheme return.

In terms of what to do for the 2018 scheme return, the Regulator acknowledges that funds (or their software providers) will have different lists of scheme specific data and methods for testing the quality, so funds' scores won't be directly comparable. They also have accepted that while they would hope and expect to see data scores improving over time, the 2019 scores for funds could well deteriorate relative to 2018 simply due to the change in what is being tested (and how it's tested) when the new guidance is available. However they would still prefer to see funds testing their data and entering a score this year, as, apart from anything else, it can identify where there are issues in the data held and should be feeding in to funds' data improvement plans.

If you want to listen to the recording of the webcast please click on this link: Data Quality in the LGPS

If you would like to discuss this matter further or are interested in support on developing your data improvement plans please contact your usual Aon contact or email laura.caudwell@aon.com

Industry developments

Government to review pensions taxation

The Government has announced in the House of Lords that it intends to "examine the processes for payment of pensions tax relief for individuals to explore the current difference in treatment to ensure that we can make the most of any new opportunities that emerge, balancing simplicity, fairness and practicality". This is in the context of the significant difference in treatment between 'relief at source' and 'net pay' arrangements for non-tax payers. However, there has been press coverage suggesting that the reference to "any new opportunities" might signal wider future changes.

CIPFA Pension Board Guidance

CIPFA has just released a new guide for local pension boards, covering structure, roles and responsibilities, and other information.

DWP consults on trustee' investment duties

The Department for Work and Pensions has consulted on changes to the Occupational Pension Schemes (Investment) Regulations, including operation of the Statement of Investment Principles (SIP), the private sector equivalent of the Investment Strategy Statement (ISS). While this will not have a direct impact on LGPS funds, administering authorities may wish to note the new requirements, particularly those regarding environmental, social and governance (ESG).

The draft regulations are intended to reassure trustees that they can (and should):

- Take account of 'financially material risks', which include but are not limited to ESG considerations including climate change;
- Fulfil the responsibilities associated with holding the investments in members' best interests;
- Have an agreed approach on the extent, if at all, to which they will take account of members' concerns; and
- Use the SIP as a real, effective and regularly-reviewed guide to investment strategy.

In summary, under the proposed changes trustees of most DB schemes will have to:

- Include in their SIP how they take account of financially material risks including climate change, and their policies on stewardship, engagement and voting rights; and
- Prepare a statement setting out how the trustees account for members' views on investment strategy.

The SIP, statement of members' views and implementation report will have to be published on a publicly accessible website and signposted from benefit statements. None of the proposals seek to direct pension scheme trustees to invest in line with scheme members' wishes.

The DWP plans to lay final regulations around October 2018. The new requirements for SIPs, and for the statement on members' views, would then come into force a year later on 1 October 2019.

Scottish Consultation on overpayment of GMPs

A consultation is currently underway regarding the overpayment of GMPs discovered during GMP reconciliation exercises. The proposal in the *Draft Regulations - The Local Government Pension Scheme (Scotland) Pensions Amendment (Increased Pension Entitlement) Regulations 2018* is for pension in payment to remain unadjusted for affected pensioners in the Police, Firefighter and Local Government Pension schemes, and create a new scheme award known as an Increased Pension Entitlement (IPE) which reflects the GMP-related overpayment.

Exit credits (refund of surplus)

MHCLG have confirmed that there will be no tax charge on exit credit payments, and that there is no requirement for the scheme administrator of the pension scheme (or sub-scheme administrator of the sub-scheme) to report the payment to HMRC.

Insolvency of Housing Associations

A new special administration regime which allows the Regulator of Social Housing to deal with insolvent housing associations has now come into force, as part of the Housing and Planning Act 2016, meaning tenanted stock would be likely to be sold to another housing provider as opposed to being sold on the open market This may have implications when considering the covenant of such employers as part of the 2019 valuation.

What we've been talking to our clients about

A focus on risk

With the annual benefit statement exercise and data quality scores both demanding administering authority time and resource (not to mention pooling) it's important not to lose sight of other important elements of scheme management. The new governance arrangements introduced in 2015 led many administering authorities to review and enhance their approach to risk, developing fund-specific risk management strategies, policies and risk registers.

CIPFA's 2012 publication *Managing Risk in the Local Government Pension Scheme* (which Aon is currently helping to update) is clear that risk management is a continuous cycle. Risk registers should be a standing item at pension committee meetings, and funds should also periodically review their overall framework and policy documents to ensure they remain appropriate and reflect the administering authority's current appetite for, and attitude to, risk.

The CIPFA document also states that whilst investment risk is often a key focus, from a funding perspective there are other, equally fundamental risks, including liability risk and employer risk and we think this is as true now (if not more so) as it was in 2012. We would encourage an annual review of all fund policies and strategies, and with the valuations due next year, suggest a focus on how risks and counter-measures are articulated within the Funding Strategy Statement and how these fit within the fund's overall risk management framework.

Arguably the area where most has changed since 2012 is in relation to employer risk, and Aon has developed a model which helps identify which employers pose most risk to the fund and provides an audit trail for any decisions not to mitigate employer risk (since LGPS funds can and do absorb risk, not all risks need to be eliminated). If you think this could help your fund and would like to know more, please get in touch with Joel Duckham or Chris Darby.

A brighter outlook for contributions?

It would be very unwise to get carried away with 8 months to go until the next valuation date, but we should acknowledge that the outlook for next year's valuations (for the tax-raising employers at least) is currently quite rosy for many (but not all!) funds advised by Aon, despite falling discount rates leading to higher liabilities and future service rates.

Fund actuaries are more likely to advise increasing prudence than automatically reducing employer contributions, and will be extremely cautious about promising contribution reductions at all given the outcome is still very uncertain. Nevertheless, if market conditions remain as they are (and investment strategy isn't changing significantly), there could be an opportunity to provide the long-term secure employers with greater certainty of contributions much earlier than would usually be the case, perhaps even agreeing contributions for 2020/21 in advance of the valuation date if sufficient information on membership experience since the 2016 valuation is available.

With employer contributions having been on an upward trajectory for a number of years, employers are rightly demanding more and earlier information on funding and administering authorities should find greater transparency and earlier engagement make the valuation itself materially smoother. It is also arguable that managing expectations is just as important when the outlook looks good as when it is challenging – administering authorities and their actuaries may have always preached that smoothing of contribution changes works both ways, but may find employers have short memories when faced with the possibility of lower contributions.

We are starting to discuss with administering authorities the various options and messages to be given at any annual employer meetings later in the year. One challenge is that the message may vary by employer category with funding strategy increasingly differentiated according to the assessed level of risk posed by the employer as well as the funding target which would apply on exit. For some funds we have been discussing targeted meetings with small numbers of employers, or workshops in advance of the valuation date – both of these have been well received in the past.

How to protect your pension scheme from cyber risks through asset managers

Cyber risks are a hot topic in pension schemes at the moment. Aon have produced a paper which provides an overview of the cyber threats for asset managers and explores how these risks can be reduced.

Recent events

Aquila Heywood CLASS Group AGM 11 - 12 July (Manchester)

Chris Emmerson and Craig Payne attended the CLASS conference during the 11-12 July and had a great time catching up with many of you.

The theme of the conference centred on data quality, insights and innovation. Neil Wilson of the Pensions Regulator gave a timely reminder that Administering Authorities will be required to score their Common and Scheme Specific data for this year's scheme return and also formulate a Data Improvement Plan.

Aon Webinar – Data Quality in the LGPS – 28 June 2018

Aon was joined by representatives from the Pensions Regulator and the Local Government Pension Scheme Advisory Board (SAB) to discuss the new data quality measurement requirements in the annual scheme return, and how this measurement should lead to improvements in the quality of record keeping. Further details on the session are provided under "Talking points" above, and a recording of the webinar is available for those who were unable to dial in.

Upcoming Events

Aon Defined Benefit Investment Conference

We are delighted to invite you to our free half-day conference focused on the investment landscape for defined benefit pension schemes. Taking place in both London and Leeds, these conferences offer a unique opportunity to hear directly from our investment specialists and their latest views.

As well as hearing from Aon experts we are also pleased to be joined by several external speakers.

There will be plenty of opportunity for you to ask questions, share your views and continue the discussion over lunch following the conference.

Further details on speakers and content will be available shortly but don't miss out on reserving your place at this popular conference. We very much hope that you can join us and look forward to seeing you later in the year.

London
Thursday 27 September, 08:30—14:00
The Aon Centre, 122 Leadenhall Street, London

Leeds
Tuesday 2 October, 08:30—14:00
Park Plaza, Boar Lane, City Square, Leeds

Register for this event

Blog spot

The latest articles from the Aon Retirement and Investment Blog

- Weekly Update - 23 July 2018
- Aon's Investment Related White Papers
- Second Quarter 2018 Market Review and Outlook

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