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Dear Robert

Re: LGPS Governance Regulations 2014

Further to the issuance of the consultation documents in October seeking comments on the amended Draft Regulations of the future governance structure of Public Service Pension Schemes, please find our comments below. The response is on behalf of the West Midlands Pension Fund (WMPF) and the West Midlands Integrated Transport Authority (WMITA).

WMPF provides pension services to over 270,000 current and former members of the seven West Midlands district council and over 400 participating employers. It is one of the largest local government pension funds in England and Wales and as at 31 March 2014 had assets valued at over £10 billion.

WMITA is a closed fund with over 5000 members and had assets valued at over £400 million at 31 March 2014. Within this response where reference is made to 'WMPF' it is to be construed as to include WMITA also.

GOVERNANCE

Regulation 106 – Local Pension Boards: establishment

WMPF welcome the decision by Government to not restrict local pension boards by requiring their formation under S101 instead providing the flexibility of local choice.

We understand from the draft guidance issued by the Shadow Scheme Advisory Board, that the term "establish" means to amend the constitution of the Administering Authority and that the date the board could take effect could be "at a later date". WMPF welcome this in the guidance as it removes the potential for difficulty in having the board run on a different timetable to that of the Council's municipal year.

We understand the meaning in this Regulation to prevent elected Councillors from sitting on their own pension board and own pension committee. We do not interpret it to mean they are prevented from sitting on any pension board.

Regulation 107 – Local Pension Boards: membership

WMPF welcome the ability to have elected councillors sit as representatives on the local pension board and are grateful to government for acknowledging the potential difficulty of recruitment of officers and members.

What is unclear is the definition of "experience" and "capacity" of those appointed to the Board. WMPF would welcome further clarity to ensure consistency across all Funds.

Regulations 110/111 – Scheme Advisory Board: establishment/membership

WMPF welcome the opportunity for engagement in the recruitment of persons appointed to the Scheme Advisory Board and query whether the same recruiting requirements on local boards will be applied in the recruitment of persons to the Scheme Advisory Board.

The Regulation states that the Pension Board may appoint 3 persons to be non-voting advisory members. WMPF believe that these persons should be practitioners with voting powers. This is to ensure the expertise and understanding of scheme employers and administering authorities is balanced when considering policy.

Throughout the last year the Scheme Advisory Board has made use of a number of practitioners not limited to 3, WMPF believe that there has been benefit added in having these professionals sit alongside board members and would like to see this strengthened going forward.

Regulation 112 – Local Pension Boards: conflict of interest
WMPF agree that conflicts of persons appointed to the pension board should be managed the same way of those of elected councillors, however greater clarity as to the sanctions available where a person appointed fails to declare or leave a debate would be welcomed.

It is proposed that any breach of this Regulation will be managed by the pension board.

Regulation 113 – Scheme Advisory Board: funding
WMPF responded to the June consultation requesting that funding for the Scheme Advisory Board be applied on a banding basis with levels of funding determined by Fund size.

We maintain this position in the October draft.

We would further welcome guidance as to how and when that funding will be requested to ensure adequate budget setting, including opportunities for funds to influence to setting of the Scheme Advisory Board budget.

COST MANAGEMENT

General observations
New Regulations 115 and 116 introduce the cost control provisions into the LGPS, being the government's methodology for addressing recommendation 12 of the Hutton report: "The Government, on behalf of the taxpayer, should set out a fixed cost ceiling: the proportion of pensionable pay that they will contribute, on average, to employees' pensions over the long term. If this is exceeded then there should be a consultation process to bring costs back within the ceiling, with an automatic default change if agreement cannot be reached."

In essence, the proposed Regulations are enabling ones, and we do not see anything of substance here which was not already in the public domain. In particular, there are two cost control mechanisms which will run in parallel with one another:

- An HM Treasury (HMT) process, the details of which are covered under papers and draft valuation directions released previously by HM Treasury.
- An LGPS Advisory Board (LGPSAB) process.

Regulation 114 - Scheme actuary
New Regulation 114 confers power on the Secretary of State to appoint a Scheme actuary to carry out valuations of the Scheme in accordance with Treasury Directions. The Scheme actuary must be appropriately qualified to carry out a valuation of the LGPS and administering authorities must provide the Scheme actuary with any data that is reasonably required in accordance with Treasury directions. The proposal is for the Government Actuary's Department (GAD) to be appointed as the Scheme actuary.

The WMPF believes the appointment of GAD as the Scheme actuary to be a logical and sensible suggestion given the role of this organisation. The Fund would hope that this appointment would not serve to give rise to additional costs for LGPS Funds and consideration should be given to potential conflicts of interest in terms of GAD's role acting on behalf of the Treasury and also DCLG. The Fund would also appreciate clarity as to how GAD will reconcile the two cost control mechanisms, for instance in terms of precedence and how they differ.

Regulation 115 - Employer cost cap
Regulation 115(1) confirms that the employer cost cap is currently being calculated by GAD and will be available before the consultation period ends. We are aware the HMT cost cap of 19.5% has been divulged, although we await the LGPS equivalent. At the time of writing this response, the final details of the actual level of employer cost cap are yet to be released, which makes it difficult to provide a comprehensive response, however we anticipate the actual level will be higher than the equivalent figure under the LGPS process of 13% of pay for employer contributions. The WMPF also believes that full consideration should be given to the increasing maturity profiles of many LGPS Funds, combined with the redundancy and service cuts of many of the participating councils and employers.

Regulations 115(2) and (3) covers the margins of tolerance above and below the employer cost cap, set as +/-2% of pay and the process for dealing with that, specifically requiring agreement between the Secretary of State and all members of the LGPSAB for corrective action. The WMPF considers that agreement of all members of LGPSAB might be a little excessive and simply the approval of the Board as a whole might me more practical. The WMPF also notes that certain Funds, in particular Integrated Transport Funds, might already have a contribution level higher than that of the reference scheme, and this should be factored in.

Regulation 115(4) covers the circumstances where the HMT employer cost cap is breached, but where the LGPSAB cannot agree corrective action with the Secretary of State. The process appears to suggest the Secretary of State will amend the future accrual rate to achieve the desired target cost. The WMPF considers this to be a logical step, however it represents only one option for alternative scheme design, and it appears to limit flexibility over other methods, such as an adjustment to member contributions. The WMPF also observes that the employer cost cap will be set at a national level in totality and presumably compared to an average of all LGPS funds, therefore, whilst individual funds may well fall within the cost envelope at a local level, adjustments would still be imposed. It is with this in mind that details of the actual employer cost cap is awaited with interest, with further clarity on the implications for funds at a local level.

Regulation 116 - Scheme advisory board – additional functions
Regulations 116(1), (2) and (3) set out the requirement for the LGPSAB to obtain a scheme cost assessment from GAD and enables LGPSAB to make a recommendation to the Secretary of State to bring the overall cost of the scheme in line with the target cost and address the proportion whereby it falls above or below the target proportion. The target overall cost is defined in Regulation 116(7) as 19.5% of the pensionable earnings of members of the scheme and the target proportion as employers meetings two thirds and members meeting one third of the overall cost of the scheme

The WMPF understands that this is where the two processes (HMT and LGPS) will run in parallel, however with emphasis on the HMT process. As a result, and as outlined in Regulation 116(5) the primary driver will be the HMT employer cost cap, and if this is breached then there will be a requirement to bring this back into line. However, there is not any such requirement with the LGPS process as, rather than adjust the level of member contributions to meet the target proportion, it appears the target proportion would be achieved by amending the rate at which benefits accrue.

Having the two processes run alongside each other, although with one taking precedent over the other, will be a complex matter and it remains to be seen how this will work in practice, particularly as they target different parameters and ultimately potentially different timescales. The WMPF considers that greater flexibility could have been provided, whereby an adjustment to member contributions could be made, rather than the limitation of solely achieving this through amending the benefit accrual rate.

Regulations 116(8) to 116(11) set out the parameters for implementation, with the administering authority having to provide GAD with the appropriate data, LGPSAB having to produce a report within 23 months of obtaining the scheme cost assessment, and the Secretary of State providing a response to this report within six months.
The WMPF considers the content of regulations 116(8) to 116(11) to be reasonable, however we would welcome further clarity on how this will factor in triennial actuarial valuations on a local level. For instance, would the cost management in a valuation year seek to take effect in terms of adjusted employer contributions at the subsequent valuation three year's later?

We also feel that, whilst the cost control mechanisms are of significance, greater consideration should be given as to how deficits in the LGPS are to be addressed.

Finally, with regards to the construction of the Scheme Advisory Board, the WMPF firmly believes there should be a greater representation from practitioners than proposed. The WMPF feels this would enhance the understanding of the Scheme Advisory Board and consequently their ability to make sound judgement and decision making, taking into consideration the views of those who will be responsible for delivery and implementation.

Yours sincerely

Geik Drever
Director of Pensions