LGPS update

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This briefing will cover

- The post election landscape - has structural reform gone away?
- The Scheme Advisory Board work-plan inc
    - Separation
    - Cost management 2016
- What to do about Deficits?
- An update on the issues for 2016 end of contracting out

Post election landscape

Secretary of State for Communities and Local Government
The Rt Hon Greg Clark MP

Parliamentary Under Secretary of State (Minister for Local Government)
Marcus Jones MP

Structural reform – stalled or dead?

- May 2013 DCLG/LGA roundtable
- June 2013 Call for evidence
- Dec 2013 Hymans report
- May 2014 government response to call for evidence
- May 2014 open consultation – CIVs and passive investment
- July 2014 consultation closes
- April 2015 pre election period and conspicuous silence
- June 2015 rumbles from within government

Structural reform – stalled or dead?

- Total expenses £644m (£504m investment, £140m administration) [1]
- Disclosed investment costs were 0.26% but these ranged from 1.13% to 0.02%[1]
- Hymans estimated actual investment costs (including transaction fees) at £800m but some estimates put costs nearer double at over £1b
- Using £1b for investments then total costs 0.63%[2] in 2014
- Consultation highlighted potential savings of £230m by moving to passive and £240m by moving away from fund of funds for alternatives
- Question of mandatory CIVs still firmly on the table within government (for both passive and alternatives)
- Announcement in Summer Budget......

[1]LGPS Annual report 2014

[2]using a total asset value of £190b

Structural reform – back on the table

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‘**2.19 Local Government Pension Scheme pooled investments** – The government will work with Local Government Pension Scheme administering authorities to ensure that they pool investments to significantly reduce costs, while maintaining overall investment performance. The government will invite local authorities to come forward with their own proposals to meet common criteria for delivering savings. A consultation to be published later this year will set out those detailed criteria as well as backstop legislation which will ensure that those administering authorities that do not come forward with sufficiently ambitious proposals are required to pool investments.’

The Scheme Advisory board.........

- Established 1st April as a statutory Board with interim membership
- Transition from existing shadow board
- Process for formal appointment of chair by Secretary of State
- Process for appointment of members by Secretary of State
- 2-12 members (having regard to equal numbers of employers and members)
- Plus up to three others
- Committees and working groups to be reviewed

The work-plan

- Putting the case for sector led CIVs with active mandates
- Deficits management report and recommendations
- Review of Ill Health benefits structure
- Engagement best practice guide
- Options for separation
- Cost management for 2016

.....and anything else the new minister wants

The work-plan - separation

Three options being investigated

- Soft split inside the host authority – higher walls around the fund
- One step removed – use of joint committees or combined authorities
- Complete disengagement – new bodies to run the funds

The work-plan – cost management

Which way will future costs go?

- HMT imposed items up to 0.7%
- 50/50 up to 0.5%
- Commutation, increases in longevity up to ??%

Options could include stripping away some elements and/or changing accrual rate

What to do about deficits – the financial background

- 40% cut in government funding since 2010[1]
- £10 billion of gross savings found in the three years from 2011/12[1]
- Council tax now funds around half of local government spending* (up from 40% in 2010)[2]
- Net service spend down from £115b in 2009-10 to £95b in 2014-15 [2]
- Spending per person down by 23.4% on average [2]
- Cuts in spend have varied across the country from 46.3% to 6.2% per person [2]
- Largest cuts in spend have fallen on London, North West and North East [2]
- 53% (and rising) of net service spend goes on adult social care [2]
- A further £13b is to be found from government departments from 2015 to 2019/20 when expenditure will rise in line with growth
- However local authority reserves rose to approximately £24b only £4b of which is neither ring-fenced nor earmarked [4]

Source [1]LGA [2] IFS * excluding directly funded activities [4] DCLG

What to do about deficits – LGPS funding

- LGPS common contribution rates at 2013 valuation ranged from 13.5% to 39% of payroll[1]
- Funding ratios ranged from 56% to 101% with the average at 79%[1]
- Average deficit contribution is 36% of total[1]
- Total local authority employer contributions in 2014 just under £5b[2] so about 5.25% of net spend (or 10.5% of council tax*)
- Of which around £1.8b goes toward paying off the deficit
- Total deficit is £48b (or £27b using HMT discount rates) [1]
- Scheme is cash-flow neutral at contributions and benefits level but £3b in the black when investment income is included
- Without the deficit the new scheme would cost local authorities about £2.9b[3] per annum or about 3% of net spend (or 6% of council tax*)

[1]SAB 2013 valuation report, [2]based on 75% LA membership of LGPS, [3]assumes a total £30b payroll and 75% LA membership
*excluding directly funded activities

Affordability and sustainability – the options - deficits

- Over a third of cost relates to past service deficit. Deficits can be better managed but can only be reduced by extra contributions, lower liabilities or better investment returns
- Benefits (liabilities) already accrued are protected by primary legislation (Pensions Act and European property rights) Any real impact on liabilities would therefore require primary legislation and a radical shift in government policy
- How should deficits be measured? Standard discount rates, best estimate?
- Is cash-flow management a more appropriate target than deficit reduction?
- Could deficit reduction plans take into account forecast spending levels and target extra contributions when they can be best afforded?
- Could a look at LA financing, for example, rules around the use of reserves and treatment of contributions in spending totals lessen the strain without losing sight of the objective?
- Are current levels of prudence still appropriate?

2016 - End of contracting out

- £796m per annum extra costs for employers
- £11b over 10 years across employers and employees
- Future replacement rates (SP and LGPS) of up to 140%
- GMP reconciliation exercise estimated to cost up to £100m
- Potential extra 0.2% of payroll for PI on GMPs?
- GMP equalisation – annual calculations?

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