

**Report for: Pension Fund  
Committee**

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**Date of Meeting:** 25 November 2020

**Subject:** Update on Changes to Local  
Government Pension Scheme (LGPS)  
Regulations and Related matters

**Responsible Officer:** Dawn Calvert – Director of Finance  
and Assurance

**Exempt:** No

**Wards affected:** All

**Enclosures:** None

## **Section 1 – Summary and Recommendations**

This report describes several recent and proposed changes which will have a significant impact on the LGPS and on the workload of the Pensions Administration Team.

### **Recommendations:**

The Committee is requested to:

1. Agree that, until the LGPS Regulations 2013 ('the Regulations') are amended, where a member aged 55 or over is made redundant and the £95k exit payment cap would be breached by reason of the payment of pension strain, the following should be offered to the member:
  - a. An actuarially reduced pension under Regulation 30(5) of the Regulations; or
  - b. A deferred pension under Regulation 6 of the Regulations.
2. Agree that the draft actuarial factors issued by the Government Actuary Department be used in the calculation of pension strain unless and until different factors are issued.
3. Note the implications of the McCloud/Sargeant judgment
4. Note the implications of the Goodwin judgment
5. Note the new Employer Flexibilities

## **Section 2 – Report**

### **Background**

1. The administration of the pension fund is complex and requires the maintenance of proper records of all scheme members' service records and benefit entitlements. It is carried out in accordance with the LGPS Regulations, which are updated as necessary by the Government.
2. There have been several recent developments, linked to Government policy decisions or to judgements made in the UK courts which will require changes to be made to the Regulations. The Government (MCHLG) is currently making the various changes, but their complexity and potential impact on staff workloads mean that it is appropriate to bring these to the Committee's attention.
3. The four items, each of which is described below, are
  - The cap on "Exit Payments" for public sector staff
  - The McCloud / Sargeant Judgement
  - Employer Flexibilities

- The Goodwin Judgement.

### Cap on “exit payments”

4. The Restriction of Public Sector Exit Payments Regulations 2020 (SI No 1122) were signed in October and came into force on 4 November 2020. The Regulations are intended to implement what was a “manifesto pledge” by the current Government to limit public sector “exit payments” to £95,000.
5. For LGPS members, the term “exit payments” includes redundancy pay, other compensation, and any pension “strain costs” which are met by the employer to offset the cost to the pension fund of pensions being paid early.
6. This definition has significant implications for LGPS members, scheme employers and administering authorities, largely because of the impact of “strain costs” – which are not applied in the other (unfunded) public sector pension schemes. Strain costs arise because the current LGPS Regulations specify that if a scheme member who is aged 55 or more is made redundant, the member is entitled to receive immediate payment of pension based on the service they have accrued, without any reduction for early payment. Strain costs are paid by employers to the Pension Fund to compensate it for the impact of paying the pension early. They are calculated by reference to a series of factors set by the fund’s actuary. In the Harrow Pension Fund, we use factors which are common to all employers. Strain costs can be significant, depending on the scheme member’s age, gender, pensionable pay and length of service, particularly for a member who is at the lower end of the 55 to 65 age range. The costs decrease for scheme members who are closer to retirement, (e.g. they would be lower for someone who is 63 years old than for someone aged 57 with the same pensionable pay and length of service).
7. As indicated in paragraph 6 above, the existing strain cost factors are calculated on the basis that the employer will compensate the Pension Fund for the impact of paying the pension early. This approach is unsuitable for use under the new arrangements because in this context the factors may be used to reduce an individual’s pension. Therefore, the Government Actuary’s Department (GAD) is calculating common strain cost factors which will reflect the benefit to the individual of receiving their pension early. These factors will be applied across all LGPS funds and will be the same regardless of the gender of the redundant employee and hence will not be discriminatory.
8. GAD has consulted on the new factors, and the Fund’s Actuary, Hymans Robertson, has advised that they could be used in calculations from this point to deal with any redundancies already agreed before 4 November with a later implementation date.
9. The draft GAD strain cost factors will in general lead to a reduction in the amount of strain costs received by the Fund. This in turn will have some implications for funds and scheme employers as the current link

between the factors and funding levels will be lost. The reduction in strain costs will be addressed at the next subsequent triennial valuation, but Hymans Robertson advise that in most cases the impact is unlikely to be material, although this may not be the case for small employers.

10. The inclusion of strain costs within the cap means that as well as affecting “high earners”, it is likely to apply in cases which would not previously have been thought of as “excessive exit payments” – particularly for those on a mid-range salary with 30+ years’ service who have fairly recently passed the age of 55.
11. The Ministry of Communities, Housing and Local Government (MCHLG) have recently consulted on changes to the LGPS 2013 Regulations which included draft regulations. The consultation ended on 9 November. If the changes currently proposed are made, employees who are made redundant and who are caught by the exit cap will have the cap applied, and they will be able to choose between accepting a reduced pension or taking a deferred pension (at their normal retirement date). This presents a challenge for the pensions administration team, in that they may be asked to provide several calculations for a person.
12. The biggest immediate concern is that the Restriction of Public Sector Exit Payments Regulations 2020 and the current LGPS Regulations are in conflict with each other, as the LGPS Regulations specify that any scheme member who is made redundant at age 55+ has immediate unreduced access to accrued pension benefits, with no upper limit. The Local Government Association and the LGPS Scheme Advisory Board (SAB) have made representations to Government (MCHLG) on this matter, and it is anticipated that amended LGPS Regulations will be made before the end of 2020 or early in 2021.
13. In the interim, the Minister for Regional Growth and Local Government issued a letter to administering authorities on 28 October 2020. This stated that the Government intends to issue new Regulations, based upon the policy document and draft Regulations which were consulted upon earlier in the year. The new Regulations will remove the “ambiguity” between different the Regulations. The Minister’s letter states that until that happens, administering authorities should apply the Restriction on Exit Payments from 4 November 2020 by offering either a fully-reduced pension or a deferred pension plus a lump sum equivalent to the capped strain cost, the latter being payable under Regulation 8
14. However, the SAB and the London Boroughs’ Legal Alliance have sought legal advice, and both organisations’ QCs have separately advised that the Public Sector Exit Payments Regulations 2020 do not remove the requirements of the LGPS Regulations. Therefore, it is not possible to apply the “Exit Cap” without the risk of litigation being brought by the scheme member against the administering authority and/or the scheme employer for not having applied the LGPS regulations correctly.

15. In the interim, until changes are made to the LGPS Regulations, Hymans Robertson have advised that if the total of strain costs plus other “exit payments” would exceed the £95k cap, we should only pay either a reduced pension or agree to a deferred pension. In calculating this, we should apply the draft GAD factors. They do not advise making a payment under Regulation 8 as, if the non-payment of immediate unreduced pension is successfully challenged, the employee will end up benefitting from both the pension and the lump sum. This latter advice is directed at scheme employers as it would be they who have the power to make this payment.
16. Hymans Robertson have further advised that scheme employers should agree no further redundancies which would breach the cap until the new LGPS Regulations are available. However, this is an employer decision and not something that can be agreed by this Committee.
17. The Committee should also note that until the Regulations are finalised the providers of pensions administration software are unable to make changes to the systems which make the calculations. This means that in the short term, any calculations will have to be made manually. In Harrow, officers in Finance are working with HR colleagues to address the challenges. We have also communicated with scheme employers explaining the position to them and will include appropriate “qualifications” on any redundancy quotations issued during the period until the new LGPS Regulations are enacted.
18. The draft LGPS Regulations which have been consulted upon, will if implemented without further change, impact on scheme members who would otherwise have been unaffected by the £95,000 cap, as they propose that no individual would be entitled to receive both statutory redundancy pay and the “benefit” of a pension strain cost. This appears to go well beyond the intention of the original legislation, in that will impact differently on LGPS scheme members compared with those in other public sector schemes, and will affect even those scheme members for whom the total of these two elements would be well below £95,000.
19. The impact of this change means that various options will have to be prepared for any redundant individual – as they will in effect have to choose between a lump sum (redundancy payment) and immediate payment of unreduced pension.
20. The resource implications of this measure are not thought to be significant once the necessary changes in the LGPS Regulations have been incorporated into the software. It will however be necessary for all communications to warn that those receiving “quotation choices” should seek independent financial advice, and to clarify that the Pensions Team is not providing advice. Inevitably, the exact impact will depend upon the number of redundancy and other “exit” calculations required for the various scheme employers.

## **McCloud / Sargeant Judgement**

21. The “McCloud / Sargeant judgement” summarises two cases which relate to the transitional arrangements implemented in public sector pension schemes when the basis for calculating pension benefits was changed from using a final salary to a career average salary.
22. The judgement, made in the Court of Appeal, was in respect of claims brought against the Judges’ Pension Scheme (McCloud) and the Firefighters’ Pensions Scheme (Sargeant), in each case claiming that the transitional arrangements were discriminatory on the basis of age, sex and race. The claims were heard together. In the LGPS, they are normally referred to simply as the “McCloud judgement”.
23. The Court of Appeal determined, amongst other things, that transitional protection gave rise to unlawful age discrimination in both the judges’ and firefighters’ pension schemes. The Supreme Court refused the Government’s application for permission to appeal, meaning that the Court of Appeal decision stands.
24. The transitional arrangements were designed to protect people who were within 10 years of retirement at the point when the career average scheme was introduced (1 April 2014 for the LGPS) on the premise that younger members would have sufficient time to make adjustments to their retirement and pension arrangements. The protection operated by use of an “underpin” – a calculation applied to each individual on retirement to determine whether he/she would be worse off under the new (career average) scheme than under the old (final salary) scheme, and if so, offer the protection of the final salary arrangement. The impact would in each case depend on the individual’s salary, length of service, and any increase in their salary after 1 April 2014.
25. The protection was ruled discriminatory on the basis of age because it created a “cliff edge” which left many scheme members who were slightly more than 10 years from retirement worse off under the new arrangements than their peers who qualified for protection.
26. In July 2019, the Government announced that the judgement has implications for all public sector pension schemes and has set out proposals to remedy the discrimination. In the case of the LGPS, it has published and consulted on draft LGPS Regulations to enable the changes to be implemented – it is currently considering responses to the consultation.
27. The proposed Regulations will include a new underpin calculation, which works differently from the previous one. This means that in certain circumstances, it is possible for an individual who had received transitional protection under the old underpin to be worse off than if the new underpin arrangement had been applied. Therefore, in addition to applying the new arrangements to current active and deferred members, calculations in respect of people who have retired or died since 2014 will have to be re-visited to apply the new arrangements retrospectively so as to avoid a further discrimination.

28. The impact of these changes is significant, as it affects anyone who was a scheme member in 2012 and who accrued further pension benefits after the career average scheme was introduced in April 2014. The Regulations should include details of the date by which new calculations have to be completed (expected to be 31 March 2023) as well clarifying the treatment of members who have transferred from one LGPS fund to another, and whether there are to be any exceptions (for example it is possible that a minimum threshold for changes could be applied).
29. The software providers are again awaiting the final version of the Regulations to be issued, after which they will make the necessary changes to enable the calculations to be reviewed.
30. For Harrow, the Fund's actuary, Hymans Robertson, has carried out an initial analysis of the Fund's data, which indicates that approximately 4,200 members (roughly 20% of the total) could be affected by the changes. These include 500 pensioners who were covered by the original transitional arrangements, plus a further 225 pensioners who have subsequently retired, and approximately 50 deceased members. It is likely that in a proportion of these cases there will be no change to the pensions payable, but the calculations will have to be made before we can determine that.
31. Clearly, this change will have a significant impact on the workload of the pensions administration team. Officers have started to develop a project plan to complete the required work within the necessary timescale, to consider how this can best be resourced, and the most effective way in which additional capacity can be brought in (e.g. staff working overtime or additional hours, hiring of additional staff to carry out this work specifically, or secondment of existing team members and backfilling their existing roles with additional staff). In practice it is likely to be a mix of these approaches.
32. The judgement will also have a significant impact on the Fund's liabilities, although until the Regulations are published this cannot be assessed. The effects of the changes will be incorporated into the next triennial valuation of the Fund at 31 March 2022, and hence reflected in employer contributions set for the period from 1 April 2023 to 31 March 2026.

### **Employer Flexibilities**

33. The Government published the LGPS (Amendment) (No.2) Regulations 2020 on 23 September. These regulations introduce some flexibility for the Fund to assist it in managing scheme employers, and in doing so to balance the requirements of the Fund to collect contributions on time, but also to assist and support employers who may be experiencing temporary difficulties.

34. The Regulations were introduced partly to enable the Fund to act appropriately in respect of any employers for whom Covid-19 may have had a significant impact, by providing the Fund with the flexibility to
- Review employer contribution rates should a significant event make it necessary or appropriate to do so.
  - Spread “exit payments” (which may be due should an employer cease to be a scheme employer – for example at the end of a contract to deliver services to Harrow or an academy school in the borough) over an appropriate time frame
  - For employers which cease to have active members or are “exiting the scheme” to introduce deferred employer status and deferred debtor arrangements (again over a suitable time frame).
35. The nature of Harrow’s employer base is such that the Regulations will have less impact in Harrow than for some LGPS Funds. Of the 39 employers in the Fund, the Council plus the various schools and colleges amount to 31 of these. The remaining 8 employers are small in size (they had between 3 and 17 scheme members at 31 March 2020, in total less than 0.3% of the Fund’s membership) and provide services such as catering, IT or grounds maintenance for the Council or schools.
36. Whilst no immediate action is required in respect of these Regulations, it is necessary for the Fund to develop a policy for managing employers, utilising these regulations as necessary and reflecting this in the Funding Strategy Statement. Officers have commenced work with the Fund’s actuary, Hymans Robertson, to develop such a policy, and it is intended that this will be brought to the Committee’s next meeting for approval.

### **Goodwin Judgement**

37. This relates to a judgement made in the Supreme Court in the case of Mrs Linda Goodwin v the Secretary of State for Education. Whilst Mrs Goodwin’s claim was against the Teachers’ Pension Scheme, the judgement has implications for other public sector pension schemes, including the LGPS.
38. This case again relates to discrimination, this time in respect of “survivor benefits” (also referred to as “spouse’s pensions”). In the UK, same sex partnerships did not have legal status until 2005 – hence before that date, “survivors” of pensioners in same sex relationships did not receive the same benefits as those in heterosexual relationships.
39. For the LGPS, the position is complicated further by the fact that female scheme members did not accrue benefits for a surviving spouse or civil partner until 1988.
40. Whilst the Government has not yet issued draft regulations to address this issue (these would enable administering authorities to rectify the



position for those affected), Hymans Robertson have advised that in the case of the LGPS, the judgement will affect only the survivors of female scheme members with pre 1988 service who died after 2005. Hymans Robertson also advise that the numbers of people affected are likely to be small in number, and that across the LGPS the impact on liabilities is unlikely to exceed 0.1% of total scheme liabilities.

41. No action will be taken on this case until draft regulations are published. However, given the specific group of scheme members who will be affected, the administrative impact is expected to be small, and can be managed within current resource levels.

## **Legal Implications**

42. The legal implications of the new exit payment regulations are largely set out in the body of this report. The approach suggested is an attempt to mitigate risk as there is no approach which can be said to be totally legally sound. The recommended approach has a high risk of successful challenge from a scheme member. However, breaching the £95k cap as a result of pension strain risks challenge from government. The recommended approach reduces the risk of overpayment to the scheme member.

## **Financial Implications**

43. The correct implementation of these regulatory changes is of paramount importance in the performance of the Pension Fund, and the cost of additional staff and software changes will be met from the Pension Fund. The impact of the regulatory changes on the Fund's liabilities will be addressed at the next triennial valuation of the Fund.

## **Risk Management Implications**

44. The Pension Fund has a risk register which includes all the risks identified which could affect the management of the Fund. The register is reviewed elsewhere on this agenda.

## **Equalities implications / Public Sector Equality Duty**

45. Was an Equality Impact Assessment carried out? No
46. There are no direct equalities implications arising from this report, although some of the regulatory changes have been made in response to court judgements which found that the impacts of existing Regulations were in some cases discriminatory.

## **Council Priorities**

47. The performance of the Pension Fund directly affects the level of employer contribution which then, in turn, affects the resources available for the Council's priorities.

## **Section 3 - Statutory Officer Clearance**

**Statutory Officer: Dawn Calvert**

Signed by the Chief Financial Officer

**Date: 12 November 2020**

**Statutory Officer: Caroline Eccles**

Signed on behalf of the Monitoring Officer

**Date: 12 November 2020**

**Statutory Officer: Charlie Stewart**

Signed by the Corporate Director

**Date: 16 November 2020**

## **Mandatory Checks**

**Ward Councillors notified: NO**

## **Section 4 - Contact Details and Background Papers**

**Contact:** Jeremy Randall – Interim Pensions Consultant

Email: [Jeremy.randall@harrow.gov.uk](mailto:Jeremy.randall@harrow.gov.uk)

### **Background Papers:**

Local Government Pension Scheme Advisory Board advice

<https://www.lgpsboard.org/index.php/structure-reform/public-sector-exit-payments>