Cost Management, Benefit Design and Administration Committee (CMBDA)

MEETING OF 30TH OCTOBER 2023

ITEM 6 – PAPER C

SURPLUSES WORKING GROUP UPDATE

Current position:

1. The Surpluses Working Group was set up to explore the issues that may arise with more funds being in surplus.
2. The Group comprises: Euan Miller (West Yorkshire Pension Fund), Peter Wallach (Merseyside Pension Fund), Elizabeth Vollans (South Tyneside Pension Fund), Sara Maxey (Essex Pension Fund), Jonathan Teasdale (Aon), Robert Bilton (Hymans Robertson), Michelle Doman (Mercer), Clive Lewis (Mercer), David Goldsmith (Osborne Clarke), Roisin McGuire (ICAEW), John Neal (Unite), Charity Main (Anglian Learning), Jennie Mulrooney (DfE), Emelda Nicholroy (UCEA), Aidan Smith (GAD), Teresa Clay (DLUHC), Joanne Donnelly (LGA) Jeremy Hughes (LGA), Becky Clough (LGA) and Ona Ehimuan (LGA).
3. The Terms of Reference (ToR) for the group is at Annex A.

Impact on Contributions

4. The Group agreed that a key objective of the LGPS is to maintain stable contribution rates. Primary contribution rates had been rising but now seemed flat, or even falling. As employers had made extra payments when funds were in deficit, they might reasonably expect negative secondary contribution rates in a surplus situation. It was commented that most employers were not demanding reductions and understood the surplus position was only notional and potentially temporary in duration. There were however some funds where the surplus could reasonably be described as “structural”, and it was appropriate for employers in those funds to see reductions in contributions.
5. Employers’ understanding of what being in surplus meant varied, especially as there were differences between the calculation of valuation surplus and accounting surplus. It was discussed whether funds had an educational role to better explain the position to them. What mattered most to employers was feeling that there was parity of treatment and fairness across employers.

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6. Member representatives were keen to emphasise that while a surplus situation made it more attractive for employers to leave the scheme, this should be discouraged, and the benefits of continuing membership emphasised.

7. The group considered whether Regulation 64A was engaged by the drop in estimated liabilities due to market movements, and whether funds should consider reducing contributions for an employer who was financially stretched (especially local authorities at risk of a s114 notice) on that basis. It was also thought that well-funded employers may see this as an avenue to reduce the risk of future changes in contribution level and 'lock-in' higher funding levels. The preferred view was that there needed to be consistency across funds and employers, taking into account the need for stability and wider covenant considerations. It was noted that the Universities Superannuation Scheme (USS) was looking at mid-cycle valuations due to a changed funding position and if this was taken forward, it could create additional pressure from LGPS employers to be treated similarly.

8. Some felt that there were differences in how the DFE guarantee for academies was treated between LGPS funds. The group were informed that the Education and Skills Funding Agency (ESFA) had established a working group to look at the LGPS responsibilities from an academy school perspective and SAB had been invited to join the discussion.

Impact on Investment Strategies

9. The Group noted that more employers were now taking an interest in their fund's investment strategy and were looking to have a strategy that was tailored to meet the particular needs. Often this was around de-risking and stabilising future contributions. It was observed that with current market conditions it was unclear how achievable de-risking actually was, and the Liability Driven Investments (LDI) crisis of 2022 showed that risks can sometimes be unforeseen or unexpected.

10. On the issue of employing different strategies for different employers, a number of funds urged caution. It could add considerable complexity, could lead to cross-subsidy between employers and could have unintended consequences if it needed to be unwound for any reason.

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Communications

11. The group felt that there was a need for better communications. It was noted that sometimes there was a low level of feedback from employers when funds consulted on their funding strategies – possibly as few employers understood the changes. The SAB's Funding Strategy Statement working group was looking at revising the current CIPFA guidance on this to make it easier for employers to access and understand, as well as providing more practical advice on consulting. Any findings or recommendations of this group would be fed back to the working group.

12. DLUHC expressed interest in understanding more about the current situation and asked if there is data supporting some of points made in the meeting.

Next steps

13. The group agreed that the SAB Secretariat would collate the issues discussed and at the next meeting agree how the specific actions can be taken forward. The immediate actions the Secretariat will be taking forward, and members of the CMBDA are asked to approve, are:

    1. To produce a statement from the Board offering our view of the main issues exposed in the Group's discussion.
    2. Liaise with DLUHC to see if there is an appetite to provide further guidance on employer flexibilities in the LGPS Regulations.
    3. Consider addressing these issues in one of our LGPS Live events.

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