

JOHN RAISIN FINANCIAL SERVICES LIMITED

The Nottinghamshire Local Pension Board

LGPS Update

A paper by the Advisor to the Pension Board **September 2022**

Introduction

This paper informs and updates the Board in respect of a number of important issues relating to the ongoing development of the LGPS at a national level. This includes developments since the last Advisor's LGPS Update which was considered at the 17 March 2022 meeting of the Pension Board.

The issues covered in this paper will, in due course, inform the decision making of each of the 86 LGPS Funds in England and Wales including the Nottinghamshire County Council Fund. The paper informs the Pension Board of developments relating to the Department for Levelling Up Housing and Communities (DLUHC) which is the government department responsible for the LGPS in England and Wales. This includes an update on the Consultation which, in the Summer, had been expected to be issued by the DLUHC in Autumn 2022. The paper also provides the background to and an update on a number of important national issues which will be consulted upon by the DLUHC at some point. The issues covered in this paper are:

1. Developments relating to the DLUHC and issues upon which a Consultation had been anticipated in Autumn 2022.
2. Investment Pooling
3. Climate Reporting – Task Force on Climate Related Financial Disclosures (TCFD) Reporting
4. Good Governance in the LGPS
5. Age Discrimination in the LGPS (commonly referred to as “McCloud”)

It is hoped that this paper will be informative to all Members of the Pension Board and in particular to those who have joined the Board recently.

1.Developments relating to the DLUHC and issues upon which a Consultation had been anticipated in Autumn 2022

The Department for Levelling Up Housing and Communities (DLUHC) is the government department responsible for the LGPS in England and Wales. The DLUHC is responsible (after due Consultation) for issuing the Regulations and Statutory Guidance in accordance with which each of the 86 LGPS Funds in England and Wales (known as Administering Authorities in the LGPS Regulations) operate the LGPS locally.

The DLUHC is headed by the Secretary of State for Levelling Up Housing and Communities who is assisted by a number of Ministers including a Minister of State whose responsibilities include Local Government and therefore the LGPS. As reported in the March 2022 Update the Rt Hon Michael Gove MP was appointed Secretary of State in mid-September 2021 and in early October 2021 it was announced Kemi Badenoch MP had been appointed Minister of State whose responsibilities were to include Local Government and therefore the LGPS. As the LGPS Scheme Advisory Board for England and Wales (SAB) correctly stated on its website on 6 October 2021 “...*We would expect that the change of minister would lead to some delays in the current workstream...*”

On 19 April 2022, the SAB website reported that the Board Chair and Board Secretary had met with Kemi Badenoch MP. It was stated that “*Cllr Roger Phillips and Board Secretary Jo Donnelly had a useful meeting with the Minister after the Easter weekend. Topics discussed included climate risk and reporting regulations for the LGPS...; levelling up; pooling...*” By June 2022 it was anticipated that a Consultation covering a number of important outstanding issues would be published by the DLUHC in Autumn 2022. For example the Minutes of the SAB Investment, Governance and Engagement Committee of 6 June 2022 record that the representative from the DLUHC on the Committee “*reminded members that the forthcoming public consultation is now likely to be published in the Autumn and will cover a range of elements including TCFD reporting, levelling up,... and pooling guidance for administering authorities.*”

However, on 6 July 2022 Kemi Badenoch MP resigned as Minister of State at the DLUHC and on the same day Rt Hon Michael Gove MP was dismissed from his post as Secretary of State. On 7 July 2022 Rt Hon Greg Clark MP was appointed Secretary of State at the DLUHC and Paul Scully MP Minister of State whose responsibilities include Local Government and therefore the LGPS. When a new Minister of State responsible for Local Government is appointed, it is inevitable that there will likely be delays in further developing LGPS policy proposals particularly given that the LGPS is only a small part of the Minister’s overall responsibilities and inevitably a lower priority than overall Local Government policy and finance matters.

Therefore, it was no surprise that on 21 July 2022, in relation to the appointment of Paul Scully MP, a news update was posted on the SAB website which stated *“We expect that the change of minister, and the process of electing a new Conservative party leader / Prime Minister, may lead to some delays in current workstreams...”* The situation was further complicated by the fact that one issue (Investment Pooling guidance) that was expected to be included in the anticipated Autumn 2022 consultation is particularly complex and any Consultation on this matter will need to be/should be particularly carefully considered and approved at Ministerial level before it is issued.

Therefore, the issuing of the anticipated Autumn 2022 Consultation covering Climate (TCFD) reporting, Investment Pooling, and Levelling Up in the context of the LGPS was placed in clear doubt by the events (relating to changes in the Government) of July 2022. The SAB, however, actively, and positively sought to encourage the Government not to delay the issuing of the expected Autumn Consultation also stating on 21 July 2022 that the SAB *“will continue to work with the Department to minimise”* delays in the current workstream *“as much as possible.”* The SAB particularly sought to encourage the DLUHC to at least issue a Consultation covering Climate/ Task Force on Climate Related Financial Disclosures (TCFD) Reporting for the LGPS. On 15 July 2022 the Chair of SAB (Councillor Roger Phillips) wrote to the Secretary of State (Rt Hon Greg Clark MP) – this letter included the following *“The main purpose of this letter is to convey the Board’s hope that the timetable for public consultations on changes to the Scheme which, up to now, had been planned for the Autumn will not be delayed by the recent changes in the Ministerial team.*

Those consultations were likely to cover a number of different areas relevant to the scheme, however, our main concern centres on the introduction of a framework for LGPS administering authorities to report on climate change risks, as stipulated by the Taskforce on Climate Related Financial Disclosures (TCFD).

Corresponding regulations for private sector pension schemes came into force in October last year and reports for the 2021/22 period are now being published. The LGPS is therefore already a year behind the private sector and delaying the planned consultation beyond the Autumn risks even further delay and the resultant criticism that the scheme, and those responsible for making scheme regulations, are dragging their heels on this key issue.

I very much hope that you will feel able to give an early assurance to the Board that the anticipated public consultations, and in particular that the reporting of climate related risk, will proceed in time for the necessary regulations and associated guidance to be introduced by April next year. This is necessary to enable LGPS administering authorities to put in place arrangements to report on climate risks and progress against emissions targets... Any delay beyond then would put us a further year behind the private sector, which would be regrettable for a globally significant investor like the LGPS.”

A letter from the Chair of SAB to Paul Scully MP of 21 July 2022 referred to the fact that they had met on 19 July 2022 and included the following – *“Can I first of all reaffirm my request to you in Tuesday’s meeting for the Department to publish the TCFD consultation and regulations as soon as possible. We have been waiting to move forward with this since last October and there is growing concern about the delay in the LGPS when the DWP regulations and guidance are already out for private sector schemes... As a more public facing scheme it is important that we can demonstrate our commitment to climate risk reporting transparency, and other key issues.*

Similarly, I will support both the Board’s Secretariat and your officials working closely on getting the broader consultations due out after the recess...” Therefore, the SAB very clearly engaged with the DLUHC following the appointment of the new Ministers in July 2022 to seek to facilitate the issuing of the anticipated broad ranging LGPS Consultation in Autumn 2022. In particular the SAB sought to encourage DLUHC not to delay a Consultation covering Climate/TCFD reporting for the LGPS.

On 1 September 2022, the DLUHC issued a LGPS Consultation entitled **“Governance and reporting of climate change risks”** which seeks views on Government proposals to require LGPS administering authorities (LGPS Funds) *“in England and Wales to assess, manage and report on climate-related risks, in line with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).”* The Consultation closes on 24 November 2022.

The LGPS Consultation issued on 1 September 2022 is concerned solely with Climate related issues. There were no proposals relating to Investment Pooling (expected since 2019) or Levelling Up in relation to the LGPS. While it is not possible to state categorically that these issues will not be consulted on during 2022 it would now seem unlikely. This is because the Climate/TCFD reporting Consultation remains open until 24 November 2022, and then the DLUHC will have to consider all responses received, draft final Regulations and lay them before Parliament so as to enable the finalised LGPS Climate Change reporting Regulations to come into effect by 1 April 2023.

The changes in Ministerial appointments at the DLUHC in July 2022 were potentially temporary as they were made at the point when it was clear that there would be a change of Prime Minister in early September 2022. Following the appointment of Rt Hon Elizabeth Truss MP as Prime Minister on 6 September 2022 there was a change in the Secretary of State responsible for the DLUHC with the replacement of Rt Hon Greg Clark MP by Rt Hon Simon Clarke MP. It is however worth noting that the new Secretary of State has previously served as Minister of State with responsibility for the LGPS (February to September 2020).

Paul Scully MP who was appointed in July 2022 as the Minister of State whose responsibilities include the LGPS has been retained in this role by the new Prime Minister. This provides continuity and hopefully will avoid further delays to the policy development of the LGPS which would likely have resulted from the appointment of another (new) Minister of State.

2. Investment Pooling

A Consultation including proposals on further developing Investment (Asset) Pooling expected since 2019 had, as explained in Section 1 of this paper, been expected in the Autumn of 2022. This however now seems likely to be delayed until 2023.

In November 2015, the government issued guidance entitled “**Local Government Pension Scheme Investment Reform Criteria and Guidance.**” This set out criteria for the (then) 89 LGPS Funds in England and Wales to form Investment Pools whose fundamental role is to select asset managers to implement the Investment Strategy determined by each individual LGPS Fund. This resulted in the creation of 8 Investment Pools across the LGPS. These had a wide range of both regulatory and governance structures and have, individually, developed very differently since 2015. The Nottinghamshire County Council LGPS Fund is a member of the LGPS Central Pool.

Crucially, however, all Pools are creations of their constituent LGPS Funds, owned by them, and ultimately accountable to them. Furthermore, all assets continue to belong to the individual LGPS Funds not the Pools.

The sole fundamental role of Investment Pools, including LGPS Central, is to select and monitor investment managers to implement the Investment Strategy of their constituent (individual) LGPS Fund’s. The setting of Investment Strategy (including the types of Assets and their proportions) which academic studies clearly demonstrate is the primary driver of investment returns remains the responsibility of each individual LGPS Fund. To fulfil its role, it is crucial that an Investment Pool provides/procures investment products that meet the needs of its constituent LGPS Funds.

The (then) MHCLG issued a Consultation on a new framework for Pooling in January 2019 but subsequently withdrew this. In November 2020, the Government stated in writing (in “**The Balance Sheet Review Report**” issued by HM Treasury) that it would “consult” in 2021 “on next steps” to implement “a strengthened framework for LGPS investment and pooling” but this did not occur. Therefore, the mandate for Pooling within the actual LGPS Regulations remains limited to one statement in the LGPS (Management and Investment of Funds) Regulations 2016. This is, that the Investment Strategy of an LGPS Fund must include “*the authority’s approach to pooling investments, including the use of collective investment vehicles and shared services.*” In reality the present position with Investment Pooling is therefore that while LGPS Funds need to demonstrate commitment to the principle, the actual pooling of particular assets is in essence ultimately voluntary. The extent to which individual LGPS Funds across England and Wales have pooled their assets varies enormously. Some Funds have now placed the majority of their assets with their Pool while some have placed very little.

There can be no doubt, however, based on both written statements and speeches made by Civil Servants that Pooling is here to stay and that the DLUHC intend to develop it further. The question is how? The DLUHC will certainly need to think carefully given responses to the Consultation of 2019 and the 2020 Supreme Court case relating to another LGPS issue which resulted in a judgement which included reference to the (limited) extent to which the Secretary of State (DLUHC) can use Statutory Guidance (rather than Regulations) to mandate how LGPS Funds should act.

There have been various suggestions as to the nature of the Consultation that the DLUHC will issue. Particular important themes will be the extent of mandation which could cover a range of issues including the structures and governance of Investment Pools, and possible timescales. One suggestion is that the Consultation might include “comply or explain” provisions. Whatever the contents of the Consultation, however, given the broad range of views amongst the 86 LGPS Funds together with the diverse approach to Pooling that has developed since 2015 there will doubtlessly be a vigorous response from the LGPS community when the Consultation is (finally) issued.

3. Climate Reporting – Task Force on Climate Related Financial Disclosures (TCFD) Reporting

In 2015 the Financial Stability Board (established in 2009 by the G20 countries) created the Task Force on Climate Related Financial Disclosures (TCFD) to develop consistent climate related financial risk disclosures for use by companies, banks, and investors in providing information to stakeholders.

In 2017 the TCFD published its final recommendations. The Task Force recommendations were structured around four thematic areas that represent core elements of how organisations operate - Governance, Strategy, Risk Management, Metrics and Targets. The 2017 report summarised these as follows

1. **Governance:** *“Disclose the organization’s governance around climate-related risks and opportunities.”*
2. **Strategy:** *“Disclose the actual and potential impacts of climate-related risks and opportunities on the organization’s businesses, strategy, and financial planning where such information is material.”*
3. **Risk Management:** *“Disclose how the organization identifies, assesses, and manages climate-related risks.”*
4. **Metrics and Targets:** *“Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.”*

In the United Kingdom, the Department for Work and Pensions (DWP) has consulted upon (in January 2021) and issued final Regulations (***The Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021***) on TCFD reporting by Private Sector Pension Schemes. These set out how private sector schemes are required to report against the TCFD framework. These Regulations came into force from 1 October 2021. The DWP Regulations do not apply to the LGPS as the DWP has no role in relation to the Regulations relating to the governance and investment of the LGPS. This responsibility lies with the DLUHC.

A Consultation to amend the LGPS Regulations to apply Climate/TCFD reporting to Local Government Pension Funds was expected by early 2021. As already stated, (in Section 1 of this paper) the SAB made very clear representations to DLUHC in July 2022 requesting that there be no further delay to issuing a Consultation to enable *“the necessary regulations and associated guidance to be introduced by April next year.”* The SAB letters to the DLUHC of 15 July 2022 and 21 July 2022 (referred to in Section 1 of this paper) clearly indicated that SAB considered that urgently issuing a Consultation on Climate/TCFD reporting was more important than a Consultation on Investment Pooling. This was because if the LGPS as a whole lacked a Regulatory framework to report on climate risks and progress the LGPS as a Scheme could appear, through absolutely no fault of its own, not to be serious when it comes to Climate/TCFD reporting. Of course, any such perception would be absolutely and totally erroneous. In contrast the DWP had already put in place Regulations on Climate/TCFD reporting which came into force from 1 October 2021 for Private Sector Pension Schemes with assets over £5bn and will come into force for Private Sector Pension Schemes with assets over £1bn from 1 October 2022.

A Consultation in respect of proposals to require LGPS administering authorities (LGPS Funds) in England and Wales to assess, manage and report on climate-related risks, in line with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD) was, as stated in Section 1 of this paper, issued by the DLUHC on 1 September 2022. The full title of the Consultation is ***“Local Government Pension Scheme (England and Wales): Governance and reporting of climate change risks.”***

As Paragraph 8 of the Consultation states individual LGPS Pension Funds such as the Nottinghamshire County Council Fund (known as in the LGPS Regulations as Administering Authorities (AA’s) of which there are 86 in the LGPS) *“are already required to consider factors that are financially material to the performance of their investments, including environmental, social, and corporate governance considerations. They also must have a policy stating how such considerations will be considered in setting their investment strategy. The aim of the proposals in this consultation document is to build on that position by ensuring that the financial risks and opportunities arising specifically from climate change are properly understood and effectively managed by AAs, and that they report transparently on their approach”*

Paragraph 9 of the Consultation states *“The government’s view is that the requirements for the LGPS should set as high a standard as for private schemes. We have therefore made the requirements for private schemes the starting point for our proposals but have aimed to take account of the unique features of the LGPS including its local administration and democratic accountability through the AAs.”*

It is important that the Nottinghamshire Fund carefully considers, and responds as it considers appropriate, to this Consultation as the regulatory requirement to report on Climate change risks will lie with individual LGPS Funds rather than their Investment Pool. The consultation lasts from 1 September to 24 November 2022.

4. Good Governance in the LGPS

The Good Governance in the LGPS project was initiated by the SAB in 2018. The project sought to fundamentally enhance and strengthen the governance of the individual LGPS Funds in England and Wales. The project took place over three phases which progressively developed a broad range of proposals. Two broad ranging stakeholder working groups (the Standards & Outcomes Group and the Compliance & Improvement group) were established at Phase II to work with Hymans Robertson who were tasked with co-ordinating the project. The Advisor to the Nottinghamshire Pension Board was a member of both working groups and the Phase III Implementation Group. The detailed proposals of the Good Governance in the LGPS project in the Phase II report which were further developed in the Phase III report may be summarised as follows:

- The MHCLG (now the DLUHC) to produce Statutory Guidance to establish new governance requirements for Funds to effectively implement the proposals from the Good Governance in the LGPS project.
- Each Administering Authority (LGPS Fund) must have a single named officer responsible for the delivery of all LGPS related activity for the Fund – “the LGPS Senior Officer”
- Each Administering Authority must publish an annual Governance Compliance Statement that sets out how they comply with the governance requirements for LGPS Funds as set out in the new Statutory Guidance.
- Enhancements to the requirements in relation to - Conflicts of Interest, Knowledge and Understanding, Service Delivery including Business Planning/Budgeting, and performance against a key set of indicators.
- Each Administering Authority be required to undergo a biennial Independent Governance Review and, if applicable, produce the required improvement plan to address any issues identified.

In February 2021, the SAB received the final Phase III report, considered, and approved an Action Plan based on the final report. It was agreed that the Board's Chair (Councillor Roger Phillips) would write to the (then) Local Government Minister Luke Hall MP inviting him to consider the Board's Action Plan.

The Action Plan consists of formal requests from the SAB to the Government to implement the proposals of the Good Governance in the LGPS project. Given DLUHC were represented on both the Phase II Working Groups and the Phase III Implementation Group it is highly likely that the Action Plan will be positively received by the DLUHC. The Action Plan includes the Recommendations in the Phase III report, the consequent proposed actions for DLUHC either by Regulation or Statutory Guidance, and work to be undertaken by SAB.

The approval of the Phase III report by SAB and the submission of the Action Plan to the Government bring closer the implementation of the project's proposals. However, implementation of proposals by the DLUHC (likely to be closely but not exactly derived from those of SAB) requires a formal Consultation. Based on statements from SAB, arising from discussions with DLUHC it became clear that the Good Governance in the LGPS proposals, thought submitted to Government in early 2021, would potentially not form part of the (expected) Autumn 2022 Consultation but would be held over until later. Given the likely delay to some parts of the (previously expected) Autumn 2022 Consultation it would seem that any Consultation on requiring national implementation of the project proposals will not be issued until well into 2023 at the earliest.

Notwithstanding this Consultation delay some Funds are seeking to implement (some of) the proposals of the Good Governance in the LGPS Project prior to the issuing of Regulations/Statutory Guidance from DLUHC and further SAB guidance. The Nottinghamshire Fund may wish to consider if, from the perspective of enhanced Fund governance, it would be beneficial to implement some of the proposals from the SAB Good Governance in the LGPS project prior to any statutory requirement to do so. Any such decision is ultimately a matter for the Pension Fund Committee advised by Officers.

5.Age Discrimination in the LGPS (commonly referred to as “McCloud”

The Public Service Pensions Act 2013 which reformed all the major public service pension schemes from 2014 or 2015 included provision for protections for older members designed to ensure they would not be worse off as a result of the introduction of the new schemes. In 2018 the Court of Appeal ruled that in the case of the Judges' and Firefighters' Pension Schemes this was (age) discriminatory against younger members. In July 2019, the Government confirmed that there would be changes to all public service pension schemes, including the LGPS, to remove this age discrimination. This whole issue is now commonly referred to as “McCloud.”

On 16 July 2020, the then MHCLG issued a Consultation called “**Amendments to the statutory underpin**” to address the age discrimination identified in the LGPS. However, given the age discrimination in the LGPS and other public service pension schemes had resulted from the Public Service Pensions Act 2013 there was a need for revision to primary legislation before the LGPS Regulations could be amended. On 11 May 2021, the Government confirmed that a Public Service Pensions and Judicial Offices Bill would introduce amendments to incorporate the McCloud judgment into public service pension schemes. On 13 May 2021, in a Ministerial Statement, Luke Hall MP, the then Minister of State with responsibility for the LGPS, confirmed that it was intended that these remedial Regulations “*will be retrospective to 1st April 2014.*” Referring to the Consultation of July 2020 it was confirmed that key elements of this would form changes to the LGPS Regulations which would be made after the Public Service Pensions and Judicial Offices Bill had become an Act.

The Public Service Pensions and Judicial Offices Act came into effect from 10 March 2022. In an update issued by the DLUHC on 27 July 2022 it was stated that “*Later this year*” the DLUHC will publish its formal response to the July 2020 Consultation and also “*an updated version of the draft regulations implementing the McCloud remedy.*” Given that this statement was issued by the DLUHC **after** the July 2022 Ministerial changes it appears that the Consultation response and draft Regulations to remedy McCloud, which had been expected during the calendar year 2022, will still be issued this year.

However, there is already clarity regarding the overall nature of the remedy from the Ministerial Statement of 13 May 2021 and a letter issued from the Head of Local Government Pensions at the DLUHC on 22 March 2022 which suggested that for purposes of the 2022 Actuarial Valuations Funds apply the following:

- *It should be assumed that the current underpin (which only applies to those members within 10 years of their NPA at 31 March 2012) will be revised and apply to all members who were active in the scheme on or before 31 March 2012 and who join the post 1 April 2014 scheme without a disqualifying service gap.*
- *The period of protection will apply from 1 April 2014 to 31 March 2022 but will cease when a member leaves active service or reaches their final salary scheme normal retirement age (whichever is sooner).*
- *Where a member remains in active service beyond 31 March 2022 the comparison of their benefits will be based on their final salary when they leave the LGPS or when they reach their final salary scheme normal retirement age (again whichever is sooner).*
- *Underpin protection will apply to qualifying members who leave active membership of the LGPS with an immediate or deferred entitlement to a pension.*

- *The underpin will consider when members take their benefit so they can be assured they are getting the higher benefit.*

The update from the DLUHC on “McCloud” issued on 27 July 2022 provided clear assurance that the Government intends to act in a timely fashion to seek to put in place Regulations and Statutory Guidance to enable the 86 individual LGPS Funds (Administering Authorities) in England and Wales to apply a finalised remedy to the benefit entitlement of individual members of the LGPS. The DLUHC communication of 27 July 2022 included the following: “*Later this year, we intend to publish the Government’s response to our 2020 consultation, in which we’ll set out our decisions on the matters covered in that consultation...*”

Alongside the Government response, we intend to publish an updated version of the draft regulations implementing the McCloud remedy. The updated draft regulations will reflect the new powers in Chapter 3 of Part 1 the 2022 Act governing the statutory underpin, as well as technical feedback we received at the 2020 consultation and any changes in policy. To ensure the updated draft regulations are accurate in light of the changes made, they will be subject to a further period of consultation early in 2023. At that time, we will also consult on other aspects of the McCloud remedy which did not feature in our original consultation (for example, compensation and rates of interest). The regulations will be made later in 2023 and will come into force on 1 October 2023. We intend to issue statutory guidance on the implementation of McCloud in 2023 following a period of consultation.

This approach will ensure that the regulations, when made, will reflect all aspects of the remedy and have been appropriately scrutinised. We would encourage LGPS administrators to begin taking steps towards the implementation of McCloud remedy following the publication of the Government response, and will shortly be holding a meeting with software suppliers to discuss the implementation of the McCloud remedy to this timetable.”

In conclusion, there is now clarity as to the remedy for “McCloud” in the context of the LGPS particularly in the light of the enactment of the Public Service Pensions and Judicial Offices Act 2022, and the statements from the DLUHC issued on 22 March 2022 and 27 July 2022. However, for the Nottinghamshire County Council Fund (and every other individual LGPS Fund) there is a huge amount of work to be undertaken, by the Pensions Administration Team, to apply the finalised remedy (when fully issued and known) to the benefit entitlement of individual members of the LGPS.

John Raisin

15 September 2022.

John Raisin Financial Services Limited
Company Number 7049666 registered in England and Wales.
Registered Office Market House, 10 Market Walk, Saffron Walden, Essex, CB10 1JZ
VAT Registration Number 990 8211 06