SUPERANNUATION FUND COMMITTEE

Wednesday, 1 December, 2021

10.00 am

Council Chamber, Sessions House, County Hall, Maidstone

AGENDA

SUPERANNUATION FUND COMMITTEE

Wednesday, 1 December, 2021, 10.00 am		Ask for:	**Theresa Grayell**
Council Chamber, Sessions House, County Hall, Maidstone		Telephone:	**03000 416172**

Membership

Conservative (8):	Mr C Simkins (Chairman), Mr N J D Chard (Vice-Chairman), Mr P Bartlett, Mrs P T Cole, Mr P Cole, Mr P C Cooper, Mr J P McInroy and Mr J Wright
Labour (1):	Ms M Dawkins
Liberal Democrat (1):	Mr D S Daley
Green and Independent (1):	Mr P Stepto
District Council (3)	Cllr J Burden, Cllr P Clokie and Cllr N Eden-Green
Medway Council (1)	Cllr R Thorne
Kent Active Retirement Fellowship (2)	Two vacancies
UNISON (1)	Mr J Parsons
Staff Representative (1)	Vacancy

UNRESTRICTED ITEMS

(During these items the meeting is likely to be open to the public)

1 Apologies and Substitutes

2 Declarations of interest by Members in items on the agenda for this meeting.

3 Minutes of the meeting held on 8 September 2021 (Pages 1 - 10)

4 Pension Fund Business Plan (Pages 11 - 18)

5 Fund Employer and Governance Matters (Pages 19 - 80)

6 Pensions Administration (Pages 81 - 84)

7 Report from the Pension Board meeting - verbal

8 ACCESS update (Pages 85 - 92)

9 Fund Position (Pages 93 - 104)

10 Date of next meeting

The next meeting of the committee will be held on **Thursday 3 February 2022**, commencing at 10.00 am at Sessions House, County Hall, Maidstone.

Motion to exclude the press and public for exempt business

That, under Section 100A of the Local Government Act 1972, the press and public be excluded from the meeting for the following business on the grounds that it involves the likely disclosure of exempt information as defined in paragraph 3 of part 1 of Schedule 12A of the Act.

Paragraph 3 – Information relating to the financial or business affairs of any particular person (including the authority holding that information)

EXEMPT ITEMS

(During these items the meeting is likely NOT to be open to the press and public)

11 Governance review presentation (Pages 105 - 220)

12 Pension Fund Cash Flow (Pages 221 - 224)

13 Manager presentation - Schroders

14 Equity Downside Protection - update (Pages 225 - 242)

15 Investment Strategy - TO FOLLOW

16 Pension Fund Risk Register (Pages 243 - 248)

17 Responsible Investment update (Pages 249 - 254)

Benjamin Watts
General Counsel
03000 416814

Tuesday, 23 November 2021

In accordance with the current arrangements for meetings, representatives of the Managers have been given notice of the meeting and will be in attendance for their items.

KENT COUNTY COUNCIL

SUPERANNUATION FUND COMMITTEE

MINUTES of a meeting of the Superannuation Fund Committee held in the Council Chamber, Sessions House, County Hall, Maidstone on Wednesday, 8 September 2021.

PRESENT: Mr C Simkins (Chairman), Mr N J D Chard (Vice-Chairman), Mr P Bartlett, Cllr P Clokie, OBE, Mrs P T Cole, Mr P Cole, Mr J P McInroy, Mr J Parsons, Mr P Stepto, Cllr H Tejan (Substitute for Cllr G Hackwell) and Mr J Wright.

ALSO PRESENT: Mr R Sinnott

IN ATTENDANCE: Ms Z Cooke (Corporate Director of Finance), Mrs B Cheatle (Pensions Manager), Mrs A Mings (Treasury and Investments Manager, and Acting Business Partner for the Kent Pension Fund), Ms S Surana (Principal Accountant - Investments), Mr S Tagg (Senior Accountant - Pension Fund) and Miss T A Grayell (Democratic Services Officer).

UNRESTRICTED ITEMS

22. Membership update
(Item 1)

The committee noted its new membership and the Chairman welcomed new Members to their first meeting.

23. Apologies and Substitutes
(Item 2)

Apologies for absence had been received from Cllr John Burden, Cllr Nick Eden-Green, Paul Cooper, Mel Dawkins and Cllr Gary Hackwell. The Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, Peter Oakford, was also unable to join the meeting.

Cllr Habib Tejan was present as a substitute for Cllr Hackwell.

24. Declarations of interest by Members in items on the agenda for this meeting.
(Item 3)

Mr P Bartlett declared an interest in agenda item 17 as he was employed by the Bank of New York Mellon, the parent company of Insight, which was managing the equity downside protection programme. He stated that he would not participate for that item.

25. Minutes of the meeting held on 23 June 2021
(Item 4)

It was RESOLVED that the minutes of the meeting held on 23 June 2021 are correctly recorded and that a paper copy be signed by the Chairman when this can be done safely. There were no matters arising.

26. Committee Work Programme 2021-22

(Item 5)

1. Mrs Mings introduced the report and advised that an additional meeting of the committee may be required in November to discuss the recommendations of the governance review and the ongoing work on responsible investment.

NOTE: an additional meeting was subsequently arranged for 23 November 2021.

2. It was RESOLVED that the information set out in the report be noted, with thanks

27. Internal Audit Action Plan Update (verbal)

(Item 6)

1. Mrs Mings advised the committee that Barnett Waddingham had now submitted their report and recommendations to the County Council and this could be discussed at the additional meeting mentioned as part of the work programme item above. Ms Cooke added that plans were in pace to create and recruit to a new post of Head of Service, to bring together the Pensions and Treasury functions.

2. It was RESOLVED that the verbal update be noted, with thanks.

28. Training Update

(Item 7)

1. Mrs Mings introduced the report and outlined imminent training sessions with Mercer, Barnett Waddingham and Mrs Cheatle's team. The Chairman emphasised the importance of training sessions to keep Members' knowledge and awareness up to date.

2. It was RESOLVED that the information set out in the report be noted, with thanks.

29. Pension Fund Business Plan

(Item 8)

1. Mrs Mings introduced the report and advised the committee on progress since the June meeting. A further update and accounts would be reported to the December meeting. The Chairman added that the restructure of the Finance function was a major undertaking and would necessarily take some time.

2. It was RESOLVED that the information set out in the report be noted, with thanks.

30. Fund Employer and Governance Matters

(Item 9)

1. Mrs Mings introduced the report and responded, with Mr Tagg, to comments and questions from the committee, including the following:

   a) concern was expressed about the extent to which the fund could impose security mechanisms, including bonds with employers. Mrs Mings advised that security arrangements applied when an employer left the scheme and reassured the committee that, if any employer should cease trading, there would be no risk to that company's pensioners, dependant pensioners or deferred pensioners. Mr Tagg clarified that different funds around the country may apply different types of security, including bonds and ‘pass-through’ arrangements;

b) asked if some employers could instead opt to join another scheme which might demand a lower level of security, Mrs Mings advised that any local government public sector employer based in Kent had no option but to join the Kent scheme; and

c) the Chairman advised that, in Academy grouping arrangements, Kent’s risk was limited only to its own schools.

2. The committee RESOLVED to note the report and to agree:

a) to the proposed Funding Strategy Statement and associated policies, in light of the results of the consultation;

b) to accept alternative forms of security provided by admission bodies, irrespective of the tax raising powers of the letting authority, subject to the following:-

   i) a satisfactory assessment of the financial strength of the letting authority; and

   ii) that the detail of any pass-through agreement and / or guarantee is captured in the associated admission agreement.

c) to the admission to the Kent County Council Superannuation Fund of Cater Link Ltd (re Education for the 21st Century Academy);

d) that a Deed of Modification may be entered into with Enterprise (AOL) Ltd;

e) that the Chairman may approve the minutes relating to recommendations c) and d) at the end of today’s meeting; and

f) that, once legal agreements have been prepared for matters c) and d), the Kent County Council seal can be affixed to the legal documents.

31. Pensions Administration
(Item 10)

1. Mrs Cheatle introduced the report and undertook to keep the Chairman updated with work to address the technology problems experienced by pensions staff. Ms Cooke added that a watching brief would be kept on this issue.

2. Discussion then moved on to the breach of LGPS regulations by the Police, set out in the report, which had previously been reported to and discussed by the Pension Board. The board had disagreed with the view and advice of officers that the breach did not need to be reported to the Pensions Regulator and had resolved that it should indeed be reported. Mrs Cheatle and Ms Cooke then responded to comments and questions from the committee, including the following:-

a) in deciding whether or not to report the breach, it was important to consider if there had been detriment to any scheme member as a result of the breach;

b) asked for reassurance that the issue had been taken seriously, and what action had been taken by the Police to address the breach, Mrs Cheatle advised that she had asked the Police to provide a written account of the steps taken. It was believed that a shortage of staff arising from covid restrictions coinciding with maternity leave had led to the breach of procedure. The council was consequently in the uncomfortable situation of having to decide whether or not to submit a report. Ms Cooke advised that some other authorities had experienced the same situation and that dialogue was underway to seek to prevent a recurrence in the future; and

c) asked about the required timeframe for reporting such a breach, Mrs Cheatle advised that there was no prescribed timetable but, generally, an earlier report was better. Ms Cooke advised that the content of such a report was not prescribed.

3. It was RESOLVED that the update be noted and the Pension Board's decision regarding the breach of the scheme regulations be endorsed.

32. Report from the Pension Board Meeting (verbal)
(Item 11)

1. As the board Chairman, Mr R Thomas, was unable to attend, Mrs Mings gave a verbal update of the discussion at the Pension Board meeting on 1 September 2021, including discussion of the breach of the LGPS regulations, as set out above.

2. It was RESOLVED that the verbal update be noted, with thanks.

33. Fund Position
(Item 12)

1. Mrs Mings introduced the report, about which there were no questions

2. It was RESOLVED that the report be noted, with thanks.

34. Date of next meeting
(Item 13)

It was noted that the next regular meeting of the Committee would be held on Wednesday 1 December 2021.

NOTE: an additional meeting was subsequently arranged for 23 November 2021 to receive updates on the governance review and the work of the responsible investment group.

35. Motion to exclude the press and public for exempt items

The committee RESOLVED that, under Section 100A of the Local Government Act 1972, the press and public be excluded from the meeting for the following business on the grounds that it involves the likely disclosure of exempt information as defined in paragraph 3 of part 1 of Schedule 12A of the Act.

EXEMPT ITEMS

Open access to minutes 36, 38, 39, 41 and 42

Summary of minutes 37 and 40
(where access to those minutes remains restricted)

36. ACCESS Update

(Item 14)

1. Mrs Mings introduced the update report and responded to a question about the level of savings the Kent fund had achieved so far this year as a result of the pooling arrangements.

2. It was RESOLVED that the information set out in the update be noted, with thanks.

37. Fund Manager Presentation - Baillie Gifford

(Item 15)

Gareth Roberts of Baillie Gifford was present for this item at the invitation of the committee.

1. Mr Roberts thanked the committee for inviting him and presented a series of slides which set out the composition, value and performance of the portfolio which Baillie Gifford managed on behalf of the Kent fund. This included Baillie Gifford's approach to responsible investment and environment, social and governance issues. He responded to comments and questions of detail from the committee about these issues.

2. The Chairman thanked Mr Roberts for attending.

3. It was RESOLVED that the information set out in the presentation and given in response to comments and questions be noted, with thanks.

38. Pension Fund Cashflow

(Item 16)

1. Mrs Mings and Ms Surana introduced the report and, with Mr Sinnott, responded to comments and questions from the committee relating to the required level of cash balance and rates of interest.

2. It was RESOLVED that the information set out in the report and given in response to comments and questions be noted, with thanks.

39. Equity Downside Protection Update

(Item 17)

1. Mr Sinnott introduced the report, about which there were no questions.

2. It was RESOLVED that the information set out in the report be noted, with thanks.

40. Investment Strategy

(Item 18)

1. Mrs Mings introduced the report and Mr Sinnott introduced the quarterly report from Mercer Ltd. They responded to comments and questions of detail and the committee considered each of the four recommendations individually.

2. It was RESOLVED that the information set out in the report be noted and that three of the four recommendations in the report be agreed, the fourth be not agreed and one new resolution be added to provide a way forward for another of the issues covered in the report.

41. Responsible Investment Update
(Item 19)

1. Mrs Mings and Mr Sinnott introduced the report, upon which there were no questions.

2. It was RESOLVED that the recommendations set out in the report be agreed and that a further report on responsible investment be submitted to the additional meeting of the committee scheduled for 23 November 2021.

42. Pension Fund Risk Register
(Item 20)

1. Ms Surana introduced the report, highlighted changes to the risk register since last reporting to the committee in June 2021 and responded to a question about the calculation of risk F1.

2. It was RESOLVED that the information set out in the report be noted, with thanks.

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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From:	Chairman Superannuation Fund Committee Corporate Director of Finance
To:	Superannuation Fund Committee – 1 December 2021
Subject:	Pension Fund Business Plan
Classification:	Unrestricted

Summary:

To advise the Committee of the progress made to date on the 2021-22 business plan and related outturn for 2021-22.

Recommendation:

The Committee is recommended to note the report.

FOR INFORMATION

1. Introduction

1.1 The Committee is asked to note the updated business plan and costs incurred to deliver the plan forecast for 2021-22.

2. 2021-22 Business plan

2.1 The Fund's business plan has been updated to reflect progress made to date and anticipated for 2021-22 and a copy is at appendix 1.

2.2 Members are asked to particularly note the following developments:

i) As part of the development of the Fund's RI policy committee members have completed an ESG beliefs survey with results being considered at a special meeting on 23 November.

ii) The Committee approved the updated Funding Strategy Statement following consultation with employers and other interested parties, at its September meeting and this has been published to the website.

iii) The Committee approved the updated Investment Strategy Statement at its meeting in September and this has been published to the website.

iv) The Fund accounts and audit timetable has been extended to the end of November. The Committee is to be asked to approve the Fund report before the 1 December deadline.

v) KCC is progressing the implementation of the restructure of the finance support for the Fund in line with the recommendations of the Barnett Waddingham review.

vi) Barnett Waddingham have completed their review of the governance of the Pension Fund and have issued their report. There will be a presentation on their findings and recommendations to members at the Committee meeting on the 1st. It is anticipated that during 2021-22 efforts will be focused on the implementation of the recommendations.

3. Changes to the Committee's work programme

3.1 At its meeting on 8 September the Committee was advised of the need to hold extra meetings. As referred to in paragraph 2.2 i) an extra meeting took place on 23 November to cover RI matters as well as consideration of the report and accounts. The Governance review will be covered at the meeting on 1 December.

3.2 Dates of future meetings have changed and the extra meeting planned for February will take place on 3 February. The plan is for the agenda to include training on RI issues as well as consideration of the ACCESS ESG guidelines. The next quarterly meeting will be on 30 March 2022.

4. 2021-22 forecast

4.1 The forecast costs to support the 2021-22 business plan are expected to amount to some £4.84m compared to the budget of £5.07m, a reduction of £230,000. Both Pension administration costs and Investment accounting and governance staffing costs are forecast to be lower than originally anticipated due to the later than planned recruitment of additional staff agreed as part of the implementation of the recommendations of the review of the finance function. These savings are offset by higher fees relating to the equity protection programme and actuarial costs.

4.2 It is anticipated that the resources required to support the changes to the Fund's governance arising from the Barnett Waddingham review will be provided from within the restructured Treasury and Investments team with support from Democratic Services colleagues.

5. Pension Fund Management Costs

5.1 The table below details forecast costs for 2021-22 compared to budget for the delivery of the Fund's business plan.

	Budget 2021-22	**Forecast 2021-22**
	£ '000	**£ '000**
Pensions Administration	3,610	3,356
Pension Payroll Services	226	226
Payment services	17	17
Financial Services	69	69
Administration Expenses	**3,922**	**3,668**
Actuarial Fee including cost of valuation	250	310
Legal Fees	50	25

Direct recovery of actuary, legal fee, and admin costs	-225	-230
Subscriptions	46	46
ACCESS pooling costs	115	115
Investment Accounting and Oversight costs	600	529
Performance Measurement Fees	30	30
Investment and governance consultancy	180	176
Equity Protection consultancy*	30	*105
Other professional advice	20	20
Governance and Oversight Expenses	**1,096**	**1,126**
Audit fee	50	50
Total	**5,068**	**4,844**

*Includes Equity Protection restructuring advice cost that was not factored in the budget

6. Review of the Finance support for the Fund

6.1 As previously reported progress has been made with implementing the recommendations of the Barnett Waddingham review.

6.2 Recruitment of the proposed Head of Pensions and Treasury is in hand and the Treasury and Investments team is being restructured with existing staff moving to new roles within the team and the recruitment of a graduate accounting trainee and a Treasury Accountant. Most staff have commenced their new roles and training is in hand to cover their new responsibilities.

6.3 The review recommended the recruitment of 3 project officers to support the Pensions Administration team and the recruitment of these staff is underway.

6.4 Pension administration and Fund investment, accounting and oversight costs are expected to be higher in 2021-22 than in 2020-21 as a result of the restructure however this increase is less than budgeted due to the restructure and recruitment being completed later than originally planned.

Alison Mings, Acting Business Partner – Kent Pension Fund

T: 03000 416488

E: Alison.mings@kent.gov.uk

November 2021

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Kent Pension Fund Business Plan

Action No.	Description	Accountable Officer(s)	Proposed 2021-22 activity	November 2021 update

1. Investment Strategy

1.1	Implement the revised asset allocation agreed by Superannuation Fund Committee on 9 February 2018.	Zena Cooke / Alison Mings	Finalise monitoring and reporting for equity protection programme	Implementation of the UK cover pending rise in FTSE100 to trigger point. Update on the restructure of global protection to be reported to the December committee Currency hedging review to be rolled forward into future asset investment strategy review
1.2.1	Strategic review of asset allocation taking account of results of the 2019 valuation	Zena Cooke / Alison Mings / Sangeeta Surana	Engage investment consultant to undertake review Q1, report outcome to June committee	Review deferred to Q3 2021-2022
1.2.2	Implement the agreed recommendations of the strategic asset allocation review	Zena Cooke / Alison Mings / Sangeeta Surana	Engage investment consultant to advise on new investment options including ACCESS funds, and selection of managers	See 1.2.1
1.3	Manage the transition of investments including to the ACCESS pooled funds	Alison Mings / Sangeeta Surana	Transition fixed Income sub-fund investments as already agreed to the ACCESS platform Implement other transitions arising from recommendations of strategic asset allocation review	Timing for fixed income sub-fund transition to be reviewed
1.4	Monitoring the performance of investment managers and funds.	Zena Cooke / Alison Mings / Sangeeta Surana	Investment Managers attending quarterly committee meetings Monthly flash reports, quarterly fund performance reports Investment consultant attending every committee meeting. Quarterly manager reviews. Asset allocation review at every meeting against Rebalancing Framework	
1.5	Develop enhanced Responsible Investment (RI) / Environmental Social and Governance (ESG) policy / reporting	Alison Mings Sangeeta Surana Katherine Gray	Ongoing - RI working group monthly meetings, recommendations to the committee, training for the committee on RI developments	RI beliefs survey completed, committee meeting on 23 November to consider outcome and next steps
1.6	Investment Consultant procurement	Sangeeta Surana Alison Mings	Ongoing management of Investment consultant contract	
1.7	Update investment strategy statement (ISS) reflecting CIPFA guidance and best practice	Alison Mings Sangeeta Surana	ISS to be updated with assistance from the investment consultant reflecting revised strategic asset allocation	Updated ISS approved by Committee at its September meeting and published to the website
1.8	Custody contract	Sangeeta Surana Katherine Gray	Complete procurement of a long-term custody contract Q2 and manage transition to new provider if required.	Procurement completed. New contract awarded from 1 August 2021

2. ACCESS Pool

2.1	Support the Chairman in his role on the Joint Committee (JC).	Alison Mings	Quarterly meetings	
	Membership of the S151 group	Zena Cooke	Quarterly meetings before the Joint Committee meetings	
2.2	Membership of the Officer working group (OWG) and other working groups to support the progress of the pooling agenda	Alison Mings Sangeeta Surana Katherine Gray	Continue to support the progression of pooling in ACCESS through participation in working groups as required. Most of the current working groups are expected to continue in 2021-22	Continued membership of OWG, Active listed assets sub-group, Reporting sub-group, Non-listed assets sub-group, Investor user group RI task and finish group, Custody procurement task and

Kent Pension Fund Business Plan

Action No.	Description	Accountable Officer(s)	Proposed 2021-22 activity	November 2021 update
				finish group – work complete,
2.3	Support the role of host authority and Access Support Unit (ASU)	Alison Mings	Kent Democratic Services providing clerking support to the JC	
2.4	Ensure the Superannuation Fund Committee and Board are kept fully informed on ACCESS issues.	Alison Mings	Quarterly updates for the board and committee	

3. Governance and employer matters

Action No.	Description	Accountable Officer(s)	Proposed 2021-22 activity	November 2021 update
3.1	Support the Superannuation Fund Committee and the Pension Board members to effectively undertake their roles and ensure that appropriate training is available.	Zena Cooke / Alison Mings	Put in place permanent resources and agreed management structure within the KCC finance function Implement updated training plan See actions 3.7 and 3.8	Report on the review of KCC finance support received 23 April. Recommendations implemented in October / November 2021. Training programme launched 1 April
3.2	Prepare the Fund's annual accounts and report including compliance with cost transparency requirements and with revised reporting guidelines	Sangeeta Surana / Katherine Gray	Complete accounts and report in line with timetable agreed with KCC Chief Accountant and external auditors.	Accounts and audit timetable extended to end November. Accounts sign off by G&A Committee 30 November and report approval 1 December 2021 committee
3.3	Response to consultations and regulation changes	Alison Mings / Barbara Cheatle	ongoing	ongoing
3.3.1	Employer flexibilities	Alison Mings	Work with the Fund Actuary on implementing changes re exiting employers.	Updated FSS agreed by the Committee at its September meeting, following consultation with employers and other interested parties, and published to the website
3.3.2	McCloud remedy	Barbara Cheatle	Implement changes required, see action 4.5	
3.3.3	Public Sector Exit Payments	Barbara Cheatle	Implement changes required, see action 4.6	No changes required as legislation withdrawn
3.4	Actuarial triennial valuation	Fund actuary / Alison Mings / Steve Tagg / Barbara Cheatle	Planning for 31 March 2022 valuation	
3.5	Update Funding Strategy Statement (FSS)	Alison Mings / Stave Tagg	FSS to be updated taking account of advice from Governance consultant	See 3.3.1
3.6	Fund actuary contract	Alison Mings / Steve Tagg	Ongoing management of actuary contract	
3.7	Review governance arrangements considering internal audit recommendations.	Zena Cooke / Alison Mings	Complete review and implement recommendations	Report received. To be shared with the Board and Committee at their next meetings in November and December 2021 respectively. Work in hand on implementation of recommendations.
3.8	Undertake review of finance resources considering internal audit recommendations.	Zena Cooke / Alison Mings	Implement recommendations Q1	Implementation Q2 and Q3 2021-22

4. Administration

Action No.	Description	Accountable Officer(s)	Proposed 2021-22 activity	November 2021 update
4.1	Roll out i-Connect employer self service	Barbara Cheatle	Further rollout planned	Discussions and planning ongoing with larger employers and other employers onboarded
4.2	Preparation of annual benefit illustrations for despatch to members by the statutory deadline	Barbara Cheatle	Ongoing	
4.3	Follow up GMP (guaranteed minimum pension) reconciliation exercise	Barbara Cheatle	HMRC have confirmed errors in previous information supplied for GMP reconciliation and so rework required by external company	Following HMRC confirming errors in previous information supplied for GMP reconciliation rework carried out by external company. New reconciliation queries to be actioned before stage 3 can be commenced.
4.4	Develop plan for introducing member	Barbara Cheatle	Planned roll out to members	Details of how to register for

Kent Pension Fund Business Plan

Action No.	Description	Accountable Officer(s)	Proposed 2021-22 activity	November 2021 update
	Self Service (MSS)			member self-service supplied to deferred members in statements despatched in July and to active members in September
4.5	McCloud remedy project - changes to LGPS following the McCloud judgement	Barbara Cheatle	Project to commence once remedy agreed	Project to commence once remedy agreed. Pilot actioned with one employer based on guidance before launch to all employers
4.6	Exit payments £95k cap	Barbara Cheatle	Implementation of changes per LGPS regulations and guidance	Legislation withdrawn, awaiting further information

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From:	Chairman Superannuation Fund Committee Corporate Director of Finance
To:	Superannuation Fund Committee – 1 December 2021
Subject:	Fund Employer and Governance Matters
Classification:	Unrestricted

Summary:

This report provides information on Fund employers and an update on the government consultation on the cost control mechanism. It also provides details of a proposed agreement with an employer for a contribution instalment plan and admission matters.

Recommendations:

The Committee is asked to note the report and to resolve to agree:

a) to entering into an employer contribution instalment payment plan with Sevenoaks Leisure Ltd;

b) to the admission to the Kent County Council Superannuation Fund of Birkin Cleaning Services Ltd (re Maritime Academy);

c) to the admission to the Kent County Council Superannuation Fund of Dolce Ltd (re The Academy of Woodlands);

d) to the admission to the Kent County Council Superannuation Fund of Town & Country Cleaners Ltd (re Maritime Academy);

e) to the admission to the Kent County Council Superannuation Fund of Purgo Supply Services Ltd (re Leigh Academy Trust);

f) that the Chairman may sign the minutes relating to recommendations a) to e) at the end of today's meeting; and

g) Once legal agreements have been prepared for matters a) to e) the Kent County Council seal can be affixed to the legal documents.

FOR DECISION

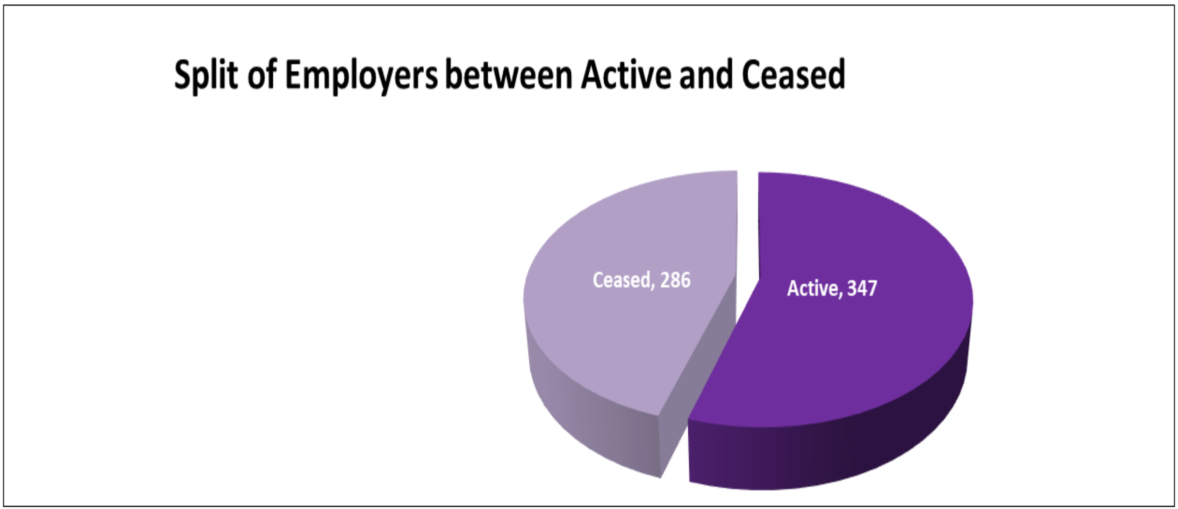
1 Introduction:

1.1 This report sets out information on employer related matters for the 6 months ending 30 September 2021.

1.2 It also provides an update on Fund employers and an update on the government consultation on the cost control mechanism. A payment instalment plan agreement with Sevenoaks Leisure Ltd and a number of admission matters.

2 Fund Employer update

2.1 There was a total of 633 employers in the Kent Pension Fund on 30 September 2021, an increase of 1 from 30 June 2021.



2.2 The number of active employers regularly paying contributions increased by 7, 4 were new to the Fund, 2 employers changed their payroll provider, and 1 ceased employer became active again. 6 employers ceased to have active members in the Local Government Pension Scheme (LGPS). The ceased employers no longer have active contributing members in the LGPS and the Fund has an existing or future liability to pay any pensions.

2.3 The following table lists employers who joined the Fund as well as those who ceased to have active members in the Fund during the 6 months to 30 September 2021.

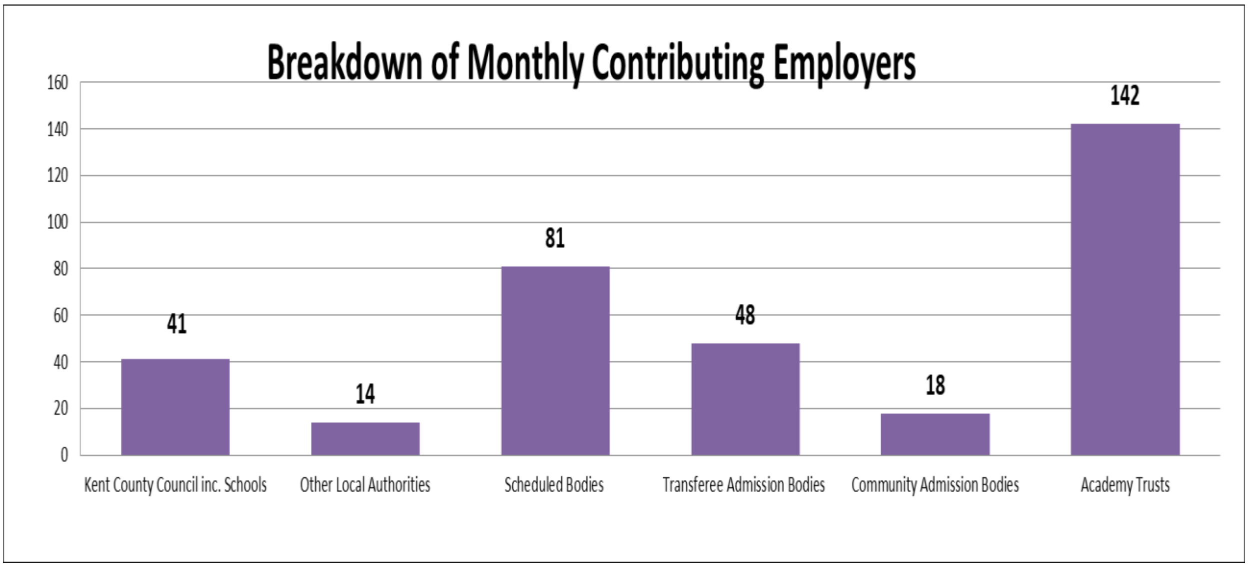
New Employers	**Effective date**
Admission Bodies	
Churchill Contract Services Ltd (re Thinking Schools Academy Trust)	1 September 2019 (backdated admission)
Scheduled Bodies	
Canterbury Environment Company Ltd	1 February 2021 (backdated)
Kite College	1 May 2021 (backdated)
Academy Trusts	
Inspire Trust	1 April 2021

Ceased / Merged to Trust Employers	Effective Date
Admission Bodies	
Kent College Canterbury	31 January 2021 (late notification of last active member leaving)
Rochester Care Homes Ltd	31 March 2021
Deep Beat Entertainment Ltd (Medway Park)	18 May 2021
Deep Beat Entertainment Ltd (Strood)	18 May 2021
Busy Bee Cleaning Services Ltd	31 July 2021
Academy Trusts	
Village Academy Trust	31 May 2021
Brook Learning Trust	31 August 2021
Scheduled Bodies	
Kent Magistrates Courts Committee	31 March 2021

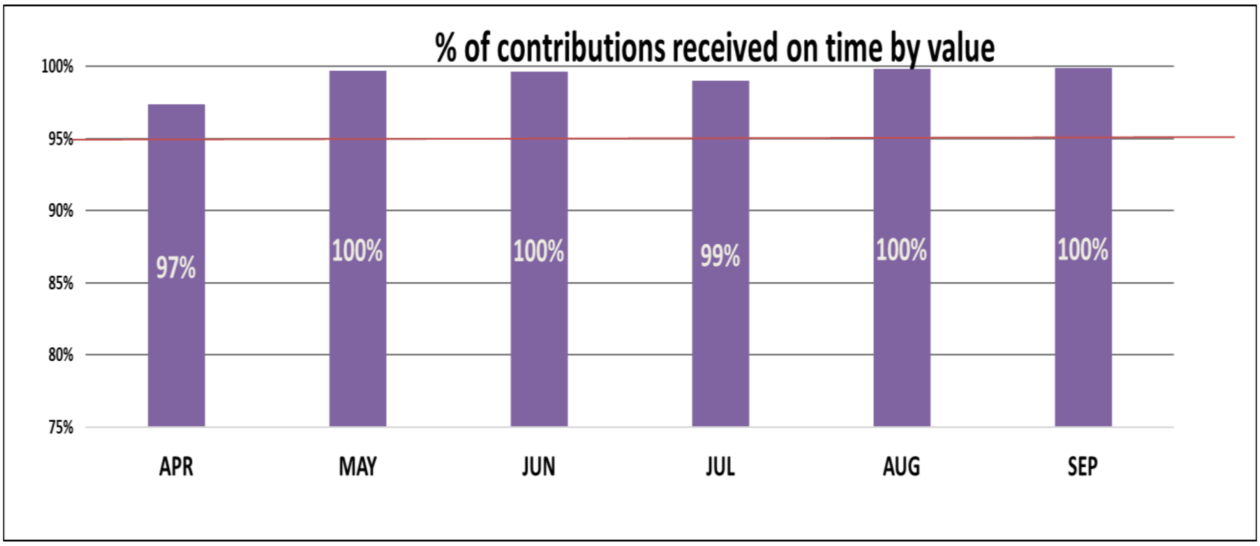
2.4 In the 6 months to September 2021 the Fund received £133.6m from employers in respect of their monthly contributions (employer and employee) as follows:

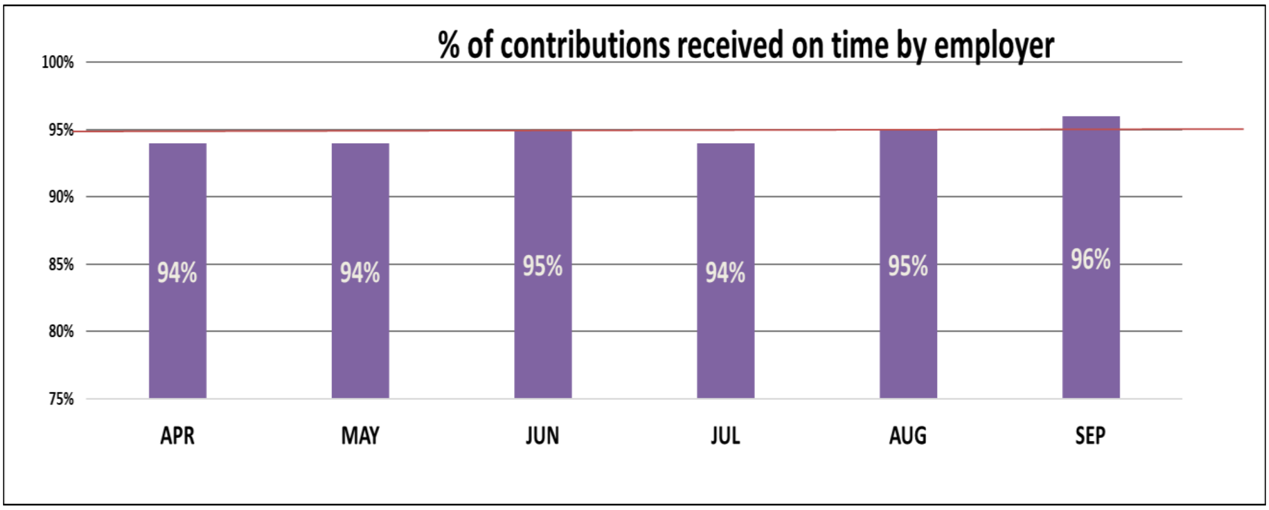
	Received Early	**Cash on 19th**	**Received Late**	**Total**
	£	**£**	**£**	**£**
April	12,840,115	8,765,012	587,525	22,192,651
May	12,279,932	9,762,932	60,322	22,103,186
June	12,716,335	9,642,629	76,950	22,435,554
July	13,282,861	8,791,062	224,129	22,298,052
August	12,766,590	9,576,083	40,569	22,383,242
September	13,069,099	9,086,697	30,949	22,186,746
Total	**76,954,932**	**55,624,415**	**1,020,444**	**133,599,431**

2.5 The following table shows employers from whom the Fund receives monthly contributions by Employer Group. Note the KCC figures reflect the council's and schools' relationships with several payroll providers.



2.6 Officers continue to monitor the receipt of these contributions and the following two charts show the % of employer contributions received on time by two different measures; by value and by number of employers. The Key performance indicator (KPI) of 95% for % of contributions received on time by employer was not achieved in April, May or July due to backdated admissions and some Parish Councils having issues with their bank. Since August we have achieved our KPI of 95% each month.





3 Government consultation on the cost control mechanism

3.1 As previously reported, HM Treasury ran a consultation on proposed changes to the cost control mechanism from June through August 2021. On 4 October the Government published their response to the consultation and a copy of their response is at appendix 1.

3.2 The Government has advised that it is pushing ahead with the proposed reforms, and they should be in place for the 2022 LGPS valuation, so

- Removing the allowance for the legacy schemes
- Widening the current 2% corridor to 3% of pensionable pay
- Adding an economic check, essentially as a sense check of the mechanism's results.

3.3 New LGPS regulations implementing these reforms were made on 7 October 2021, effective from 8 October 2021. The Fund is discussing these with Barnett Waddingham and a further update will be provided at future meetings of the Committee and Board.

4 Sevenoaks Leisure Ltd (SLL)

4.1 SLL is a community admission body which joined the Superannuation Fund on 1 February 2004 following a transfer of staff from Sevenoaks District Council (SDC). The district council is not the scheme employer party to the admission agreement because the LGPS regulations did not require this at the time.

4.2 Since March 2020 SLL's business activity has been seriously impacted by the effects of the pandemic and officers have been in regular dialogue with the company regarding payment of the employer and employee contributions. This matter was reported to the Pensions Regulator in July 2020.

4.4 In December 2020 in consultation with Sevenoaks District Council SLL formulated a recovery plan which anticipates a return to a profitable trading position in 2022.

4.5 Despite some delays Sevenoaks Leisure has now paid all employee contributions in full however arrears of employer contributions amounting to some £350k remain outstanding. The final statutory deadline for the employer contributions to be paid is the 31 March 2022 as per the Rates and Adjustment certificate from the 31 March 2019 valuation.

4.6 Further to correspondence with officers Sevenoaks Leisure submitted proposals on 27 October 2021 for paying off these arrears as follows:

a) Immediate settlement of the March 2020 employer contributions of £18,149.39 and these were received on 29 October 2021.

b) An instalment plan for the outstanding 2020/2021 and 2021/2022 contributions.

- Officers shared advice from the Fund's actuary Barnett Waddingham with SLL including repayment plans which include interest in line with the 2019 valuation assumptions. On 19 November SLL submitted a proposal to the Fund for payment in monthly instalments over a maximum of 6 years in line with the actuary's advice, commencing February 2022.

- It is our understanding that Sevenoaks Leisure are not in a position to pay the arrears in full at the present time it is therefore proposed that we agree to the plan for monthly payment of employer contribution arrears over a maximum of 6 years.

c) Payment of future monthly employer contributions starting from November 2021 which are due by 19 December 2021.

4.7 There is no impact on the company's active, deferred, pensioner and dependant pensioner members whose benefits are set out in the LGPS regulations.

4.8 Barnett Waddingham have advised that as a percentage of the Fund's total assets, the outstanding debt of £350k is less than 0.01%.

4.9 Officers will continue to monitor payments by SLL and provide an update at future meetings of the Committee and the Pension Board.

5. Admissions matters

5.1 The following organisations have applied retrospectively for admission to the Superannuation Fund to ensure the continuity of pension arrangements for staff.

5.2 The admission applications have been made under Schedule 2 Part 3 1(d) (i) of the LGPS Regulations 2013, as amended, and under this regulation the admitted body is required to provide some form of security.

5.3 The completed questionnaires and supporting documents provided by the applicants have been examined by officers to ensure compliance with the LGPS Regulations, and Invicta Law has given favourable opinions.

6 Birkin Cleaning Services Ltd (re Maritime Academy Trust at Featherby Nursery, Infants and Junior Schools)

6.1 Maritime Academy Trust has awarded a 3 year contract with a possible 2 year extension for cleaning services from 4 May 2020. This involves the transfer of 5 employees to Birkin Cleaning Services.

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6.2 The Fund actuary has assessed the employer contribution rate as 26.3% and Maritime Academy Trust as the scheme employer, has agreed to act as guarantor to the admission agreement which will include the terms of the guarantee. A satisfactory assessment of the financial strength of the Academy has been undertaken.

7 Dolce Ltd (re The Academy of Woodlands)

7.1 The Academy of Woodlands has awarded a 1 year rolling contract for catering services from 6 September 2021. This involves the transfer of 4 employees to Dolce Ltd.

7.2 The Fund actuary has assessed the employer contribution rate as 24.9% for a closed agreement and the Academy of Woodlands as the scheme employer, has agreed to act as guarantor to the admission agreement which will include the terms of the guarantee. A satisfactory assessment of the financial strength of the Academy has been undertaken.

8 Town and Country Cleaners Ltd (re Maritime Academy Trust at Danecourt School)

8.1 Medway Council has awarded a 3 year contract with a possible 1 year extension for cleaning services from 1 August 2021. This involves the transfer of 6 employees to Town and Country Cleaners.

8.2 The Fund actuary has assessed the employer contribution rate as 27.1% for a closed agreement and the Bond for the first year as £9,000.

9 **Purgo Supply Services Ltd (re Leigh Academy Trust)**

9.1 At their meeting on 13 March 2020 the Committee agreed to the admission to the Fund of Purgo Supply Services Ltd relating to a 3 year cleaning contract with a possible 2 year extension awarded by Leigh Academy Trust from 1 August 2019.

9.2 The Fund Actuary had assessed the employer contribution rate as 21.8% and the Bond for the first year as £13,000 based on a closed agreement for 7 employees.

9.3 It has now been agreed that an open agreement is required allowing for both the initial staff transfer and subsequent staff transfers covered by the same commercial contract, some 18 staff in total.

9.4 The Fund Actuary has reassessed the employer contribution rate as 25.7% and Leigh Academy Trust as the scheme employer, has agreed to act as guarantor to the admission agreement which will include the terms of the guarantee. A satisfactory assessment of the financial strength of the Academy has been undertaken.

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November 2021

HM Treasury

Public Service Pensions: cost control mechanism consultation

Government response to the consultation

October 2021

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Public Service Pensions: cost control consultation

Government response to the consultation

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This publication is available at: www.gov.uk/official-documents.

Any enquiries regarding this publication should be sent to us at public.enquiries@hmtreasury.gov.uk

Contents

Executive summary

The cost control mechanism was introduced following the recommendations of the Independent Public Service Pensions Commission (IPSPC) in 2011. It is a mechanism designed to ensure a fair balance of risk between members of public service Defined Benefit (DB) pension schemes and the Exchequer (and by extension taxpayers).

The cost control mechanism was first tested at the 2016 valuations. Provisional results raised the question of whether the cost control mechanism, as currently designed, is too volatile. Following this, at HM Treasury's request, the Government Actuary (GA) conducted a review of the cost control mechanism. The review was commissioned amidst concern that the mechanism was not operating in line with its original objectives. The GA's final report to HM Treasury containing his findings and recommendations was published on 15 June 2021.

Having considered the GA's report, the Government held a consultation between 24 June 2021 and 19 August 2021 to seek views on three key proposals to reform the mechanism, all of which were recommendations by the GA:

- **Moving to a 'reformed scheme only' design** so that the mechanism only considers past and future service in the reformed schemes, and costs related to legacy schemes are excluded. This ensures consistency between the set of benefits being assessed and the set of benefits potentially being adjusted;

- **Widening the corridor from 2% to 3% of pensionable pay.** This aims to achieve a better balance between stability and responsiveness of the cost control mechanism; and

- **Introducing an economic check.** The GA's report noted that "It does not seem possible for the mechanism to be able to protect taxpayers unless it considers more of the factors affecting the actual cost of providing a pension." Currently the mechanism does not include changes in long-term economic assumptions and therefore cannot consider the actual cost to the Government of providing pension benefits. The Government proposes introducing an economic check so that a breach of the mechanism would only be implemented if it would still have occurred had any changes in the long-term economic assumptions have been considered.

HM Treasury received 61 responses in total from a broad range of respondents. These have been considered in detail.

Changes to the core mechanism

Reformed scheme only design

The majority of respondents supported the Government's proposal to move to a reformed scheme only design and agreed that it did not seem fair for the costs of legacy schemes to impact the benefits received by relatively younger members in the reformed schemes. They agreed that as the mechanism can only adjust benefits in the reformed schemes, it seems fair to exclude the impact of legacy schemes.

A small minority felt that the current approach was preferable, as many members have service in both the legacy and reformed schemes, and so the mechanism should account for all these costs.

Others felt that a future service only design, (whereby the mechanism would only account for the costs of future service in reformed schemes) would be even fairer for relatively younger members in the reformed schemes, as they would not be affected by the impact of any past service costs of relatively older members, the impact of which will increase over time.

In line with the majority of respondents, the Government believes that a reformed scheme only design is necessary to ensure the right balance of risks between members and the Exchequer and to improve stability. A reformed scheme only design will mean that the risk of costs associated with legacy schemes will be transferred to the Exchequer, but the Government believes it is right for the Exchequer to bear this risk in order to reduce intergenerational unfairness.

Wider corridor

A majority of respondents agreed with the proposal to widen the corridor, and a slight majority agreed that the corridor should be set at +/-3% of pensionable pay. They welcomed the fact that widening the corridor would lead to a more stable mechanism by minimising the frequency of breaches, which will lead to fewer changes in benefits or member contributions. They felt that a corridor size of +/-3% was appropriate, and will strike the right balance between stability and effective cost control.

However, some favoured retaining a +/-2% corridor on the basis that a wider corridor, while providing more stability, would also diminish the cost control provided by the mechanism. Many respondents raised concerns that a wider corridor would exacerbate the "cliff-edge" nature of the mechanism which means larger changes in costs can occur without remedial action. Many argued that a proportional cost corridor, where the size of the corridor would vary depending on the size and costs of that scheme, would be more appropriate.

The Government considers that a +/-3% corridor would strike the right balance between providing effective cost control and a stable mechanism. A corridor size larger than this would not be appropriate as it would allow costs to diverge by too much before being brought back to target. The Government considers that while the "cliff-edge" risk exists, a wider corridor is necessary to ensure a more stable mechanism. The Government believes that a consistent corridor design for all schemes is preferable to a proportional cost corridor. A consistent corridor size limits the absolute change in costs that can occur across all schemes before a breach is triggered. The Government does not consider that just because a scheme is more expensive from the outset, it should be allowed to let costs change by a greater absolute amount. Furthermore, the Government considers that a proportional cost corridor would be overly complex and more difficult for members to understand than the current consistent corridor design, potentially eroding transparency and trust in the mechanism.

Economic check

Responses on the proposal for an economic check were mixed; similar numbers of respondents supported and opposed the proposal. Some argued that it would lead to a more stable mechanism and also help avoid benefit reductions if the wider economic outlook improved but individual scheme costs rose. Many raised concerns that this proposal may be a breach of the 25-year guarantee, and that it had been agreed when the mechanism was set up that changes in the SCAPE discount rate would not impact member benefits. Many also raised concerns that the economic check would not be transparent or objective and would make the mechanism subject to government interference.

Respondents with links to the Local Government Pension Scheme (LGPS) were consistently of the view that if an economic check was adopted, linking it to expected long-term GDP would not be appropriate for the LGPS. The LGPS, as a funded scheme, looks to achieve investment returns to ensure a minimum call on future local taxpayers by maintaining a pension fund able to meet all future liabilities. They argued that this is a fundamentally different situation to the unfunded schemes, where taxpayers are directly responsible for paying the cost of public service pensions.

The Government has considered all responses and maintains the view that an economic check should be introduced for all schemes, with further consideration required for potential allowances for the LGPS. The economic check will operate in line with the GA's recommended design and will be linked to the OBR's independent and objective measure of expected long-term GDP growth and the long-term earnings assumption. The economic check may potentially be linked to the SCAPE discount rate if the methodology remains linked to expected long-term GDP growth. The SCAPE consultation response will be published in due course; the Government has considered any relevant points raised as part of that consultation here.

In the Government's view, the main purpose of the economic check is to ensure consistency between benefit changes and changes to the long-term economic outlook. This approach ensures that there will be a higher bar for benefit increases to be awarded if the country's long-term economic outlook has worsened. This will equally apply to benefit cuts if the long-term economic outlook has improved. The Government can confirm that the economic check will apply symmetrically, operating in the exact same way in relation to floor breaches as it would to ceiling breaches. It will operate purely mechanically and transparently, with no scope for interference from individuals or groups, either from within the Government, or outside.

The Government has taken into consideration the concerns raised by LGPS stakeholders that an economic check linked to expected long-term GDP growth is not appropriate for the funded LGPS. The Government recognises the different nature of the LGPS. However, on balance, the Government still believes that the economic check as a whole is an appropriate proposal for LGPS.

As noted by respondents, the purpose of LGPS investments is to minimise the cost pressures facing LGPS employers who will meet the balance of costs. If the cost of benefits goes up the responsibility will fall on local authorities, who are funded to a significant extent by local taxpayers and other LGPS employers. Similar to the reason for the economic check for the unfunded schemes, the purpose of an economic check in the LGPS is to ensure consistency between benefit changes and changes in the wider economic outlook. Whilst the financial health of individual local authorities is not directly linked to expected long-term GDP growth, the Government would still expect a link between the economic performance of the UK and the financial health of local authorities.

HM Treasury will work with the Department for Levelling up, Housing and Communities and LGPS stakeholders to consider whether it is desirable for the England and Wales Scheme Advisory Board (SAB) process to be adapted in line with the principles of the economic check. The Government also acknowledges that the SABs in Scotland and Northern Ireland may wish to consider introducing a similar process to the England and Wales SAB, and will work with colleagues in the Devolved Administrations if they feel it would be desirable to do so.

Next steps

The Government is aiming to implement all three proposals in time for the 2020 valuations. It is necessary to implement the reformed scheme only design and the economic check through expanded powers in primary legislation, when parliamentary time allows, and then by making Treasury Directions under those powers in due course. The wider cost corridor will be implemented to a longer timeline via secondary legislation.

Chapter 1
Introduction

Background

The establishment of the cost control mechanism

1.1 The cost control mechanism (CCM) is a mechanism designed to ensure a fair balance of risk with regard to the cost of providing public service Defined Benefit (DB) pension schemes between members of those schemes and the Exchequer (and by extension taxpayers). It was introduced following the recommendations of the Independent Public Service Pensions Commission (IPSPC) in 2011. Whilst the IPSPC recommended a mechanism to protect the Exchequer from increased costs, the final mechanism negotiated between the Government and member representatives is symmetrical and so also maintains the value of pensions to members when costs fall.

1.2 The original objectives of the CCM can be summarised as follows:

1. To protect the Exchequer (and by extension taxpayers) from unforeseen costs;
2. To maintain the value of a public service DB pension scheme to its members; and
3. To provide stability and certainty on member benefit and contribution levels – the mechanism should only be triggered by 'extraordinary, unpredictable' events.

1.3 For each scheme, the mechanism assesses certain aspects of the costs of providing that scheme compared to a base level ("the employer cost cap"); if, when the mechanism is tested, those costs have decreased/increased by more than a specified percentage of pensionable pay compared to the employer cost cap, then member benefits in the relevant scheme are increased/reduced to bring the cost of that scheme back to target. The target cost is the same as the employer cost cap. So, there is effectively a corridor either side of the target cost, with a margin representing the 'ceiling' and 'floor'. If costs fall below the lower margin (a "floor breach"), then benefits must be increased to bring costs back to target. If costs increase above the upper margin (a "ceiling breach"), then benefits must be reduced.

1.4 The Government made provision to establish the CCM in the Public Service Pensions Act 2013 ('the Act'). Following consultation with member representatives, the Government set out in a policy paper[1] how the mechanism would operate and the Treasury made directions to put this policy into effect.

The 2016 valuations

1.5 The first test of the mechanism was at the 'as at' 31 March 2016 valuations ("the 2016 valuations"). Provisional results indicated floor breaches across all schemes for which results were assessed. It was in the context of these provisional results that the Government announced that it was asking the Government Actuary (GA) to review the cost control mechanism.[2] The Government's intention is that the cost control mechanism is only triggered by 'extraordinary, unpredictable events'. The key drivers of the indicative floor breaches were a reduction in assumed future pay increases (caused by short term pay restraint) and a reduction in assumed life expectancy. The Government did not consider that either short term pay restraint or a change in future projections of life expectancy fit the category of 'extraordinary, unpredictable events', raising the question of whether the cost control mechanism, as currently designed, is too volatile. Meanwhile, employer contribution rates increased by up to 9% of pensionable pay before the impact of the CCM. But the preliminary results of the CCM for all schemes showed a floor breach which would have further increased employer contribution rates and costs to the taxpayer.

1.6 The cost control element of the 2016 valuations was paused due to the uncertainty arising over the value of member benefits following the judgments in the McCloud and Sargeant litigation, and with it so was the GA's review of the CCM. On 16 July 2020, alongside the publication of the Government's consultation on addressing the discrimination identified in the McCloud and Sargeant judgments, the Government announced that the pause of the cost control element of the 2016 valuations process would be lifted and the GA's review of the CCM would proceed.[3] In addition, the Government announced that the costs associated with addressing the discrimination would be considered when completing the cost control element of the 2016 valuations.[4]

1.7 Whilst amending directions instructing schemes on how to complete the cost control element of the 2016 valuations are yet to be finalised, and will be published in due course, early estimates indicate that some ceiling breaches are likely. If normal statutory procedure were followed, any ceiling breaches would lead to a reduction in member benefits in order to bring costs back to target. The Government decided that there should not be reductions to member benefits as a result of completing the cost control element of 2016 valuations, particularly based on a mechanism that may not be working as originally intended. The Government has therefore announced that, should results identify ceiling breaches once finalised, the impact of these will be waived. This means that the benefit reductions that would be

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1 https://www.gov.uk/government/publications/public-service-pensions-actuarial-valuations-and-the-employer-cost-cap-mechanism

2 https://questions-statements.parliament.uk/written-statements/detail/2018-09-06/hcws945

3 https://questions-statements.parliament.uk/written-statements/detail/2020-07-16/HCWS380

4 Policy note - cost cap unpause and McCloud costs.docx (publishing.service.gov.uk)

expected following such ceiling breaches will not be implemented. As a result, where results show that costs in a scheme fall within the corridor or above the ceiling, benefit levels will not be changed as a result of the 2016 valuations.

1.8 The Government has, however, committed to delivering the impact of any floor breaches that occur. This means that when results have been finalised and implemented, any benefit improvements that are due will be delivered via increases in benefit accrual and/or reductions in member contributions in respect of service from 1 April 2019. The Government has introduced legislation to waive ceiling breaches in the Public Service Pensions and Judicial Offices Bill, which is currently before Parliament having been introduced into the House of Lords on 19 July 2021.

Government Actuary's Review and Consultation

1.9 The GA concluded his review in May 2021 and his final report was published on 15 June 2021.[5] The GA noted that:

- **Legacy schemes (i.e. those in place before the 2014/2015 reforms) were the main driver of the floor breaches** seen in the provisional results of the 2016 valuations. The breaches were caused primarily by a reduction in assumed pay increases and a reduction in the rate of increase of life expectancy. The GA considers that these costs relate to risks that have largely been mitigated in the reformed schemes: salary risk is mitigated by the career average (CARE) design of the schemes and most workforces mitigate the longevity risk by the link between Normal Pension Age (NPA) and State Pension age (SPA).[6] Although the mechanism assesses costs in both the legacy and reformed schemes, the impact of any breaches can only be delivered through changes to reformed schemes. The GA comments that "it is not clear to me why these residual risks in the legacy schemes should continue to influence the level of benefits in the reformed schemes".

- It was a **"perverse outcome"** that the 2016 valuations resulted in employer contribution rates increasing, whilst provisional cost control results found that all schemes breached the floor. If they had been confirmed, floor breaches would have led to benefit improvements, resulting in a further increase to employer contribution rates. The GA finds that this outcome was primarily driven by the fact that the cost control mechanism does not currently account for the change in the SCAPE discount rate, which is used to determine employer contribution rates.[7]

- **The current corridor is too narrow** and will lead to excessive volatility in the mechanism. The GA notes that even under a reformed mechanism,

5 https://www.gov.uk/government/publications/cost-control-mechanism-government-actuarys-review-final-report

6 Most of the reformed schemes have a Normal Pension Age (NPA) linked to the member's State Pension age (SPA) (the age at which a State Pension can be received). There are exceptions for the armed forces, the police and firefighters, where the NPA is set at 60 for those retiring from active service.

7 Superannuation Contributions Adjusted for Past Experience (SCAPE) is the methodology used to value unfunded public service pension schemes. It uses a 'SCAPE discount rate' to convert the value of future pension payments into today's terms.

the current corridor would still mean a high likelihood of frequent breaches.

1.10 In the context of these findings, the GA made a series of recommendations on how the CCM could be reformed to bring it more in line with its objectives.

1.11 Between 24 June 2021 and 19 August 2021, the Government sought views on proposals to reform the cost control mechanism. The consultation document set out the Government's response to the GA's report and proposed changes to the mechanism. The Government proposed three changes to the mechanism in the consultation, all of which were recommended by the GA:

- **Moving to a 'reformed scheme only' design** so that the mechanism only considers past and future service in the reformed schemes, and costs related to legacy schemes are excluded. This ensures consistency between the set of benefits being assessed and the set of benefits potentially being adjusted;
- **Widening the corridor from 2% to 3% of pensionable pay.** This aims to achieve a better balance between stability and responsiveness of the cost control mechanism; and
- **Introducing an economic check.** The GA's report noted that "It does not seem possible for the mechanism to be able to protect taxpayers unless it considers more of the factors affecting the actual cost of providing a pension." Currently the mechanism does not consider the wider economic situation when determining whether breaches of the mechanism should result in a change to member benefits. The Government proposes introducing an economic check so that a breach of the mechanism would only be implemented if it would still have occurred had any changes to long-term economic assumptions been considered.

1.12 The Government believed these proposed changes would establish a fairer balance of risks between the Exchequer and scheme members and create a more stable mechanism. The Government sought views on these proposed changes in its consultation.

1.13 The GA's review and the consultation applied to all public service schemes covered by the CCM. These schemes are set out in Annex A.

1.14 In parallel to this consultation, the Government also held a separate consultation on the methodology used to determine the discount rate for setting employer contribution rates in the unfunded public service schemes (the SCAPE discount rate). The Government is considering responses to that consultation separately and will set out its response in due course; the Government has considered any relevant points to the CCM raised as part of that consultation here.

Stakeholder engagement

1.15 As part of his review, the GA held a stakeholder event attended by member and employer representatives from across the public service pension schemes from England, Wales, Scotland and Northern Ireland. At the event, the GA gathered views on the current functioning of the mechanism and whether there should be any changes made to it. The GA considered stakeholders' views in carrying out his review.

1.16 Following publication of his final report, the GA chaired a webinar which discussed his assessment of the current mechanism and recommendations on possible changes to the mechanism, followed by a Q&A. Speakers also included members of the team that assisted the GA with his review, and an introduction from HM Treasury officials.

1.17 Following publication of its consultation on proposed changes to the cost control mechanism, HM Treasury ran a number of engagement sessions in July and August 2021 to ensure stakeholders were given the opportunity to express their views directly to the Government. Meetings were held with members of Scheme Advisory Boards (SABs)[8] from across the UK relating to each public service workforce, which are made up of member, employer, and administrator representatives. These sessions also allowed stakeholders to seek clarification on any of the proposals. Most stakeholders followed up with formal written responses and the feedback received during the stakeholder sessions and in formal written responses has been considered in deciding the final policy proposals.

1.18 HM Treasury also held a further engagement session with the Local Government Pension Scheme (LGPS) England and Wales SAB in August 2021 to discuss the proposals in more detail, given the difference in the way the LGPS is funded.

1.19 In addition, the Chief Secretary to the Treasury (CST) met with the General Secretary of the Trades Union Congress (TUC) and a delegation of other Trade Union leaders. This allowed the TUC to share their views with the CST on behalf of their member organisations, which stretch across the public sector and are affected by the consultation.

1.20 Stakeholder engagement will remain important as the Government looks to implement changes to the cost control mechanism. HM Treasury will continue to engage with stakeholders directly where necessary, and through relevant government departments responsible for the different public service pension schemes.

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[8] Statutory bodies, created by the Public Service Pensions Act 2013, that advise responsible secretaries of state on potential changes to public service pension schemes and advise on the administration and management of the relevant schemes. The SABs usually consist of representatives of the relevant employers, employees and administrators.

Responses to the consultation

1.21 Consultees were asked to respond to a total of 7 questions. Responses to each question were considered in making final policy decisions, and in the drafting of this response.

1.22 Responses to the consultation were received in email form and presented in different formats. Each answered all, some or none of the questions asked in the consultation document. While some responses did not necessarily address the specific questions posed in the consultation document, all responses have been considered appropriately.

1.23 The Government has undertaken quantitative and qualitative analysis of the responses, and the common themes and views are summarised within this document. Whilst trade unions and other representative bodies represent a large portion of public service workers, it should be noted that the Government recognises that the number of responses received does not accurately represent all public service pension scheme members. Therefore, any quantitative data has its limitations and has been handled with caution during the decision-making process. Where we have supplied data in this document, it is to simplify and summarise responses and provide the reader with a sense of trends – the Government did not treat respondents' answers in a binary way (agree or disagree) when forming its final policy.

1.24 HM Treasury received 61 responses from a broad range of respondents. These included trade unions and other member representative bodies, Scheme Advisory Boards (SABs), government agencies, actuarial and pensions specialists and pension scheme administrators. A wide range of trade unions and other member representative bodies, including but not limited to the Trades Union Congress (TUC), Prospect, the Public and Commercial Services Union (PCS), the British Medical Association, the National Education Union (NEU), the Scottish Police Federation and the Defence Police Federation, responded to the consultation, representing over 3.5 million public service workers.

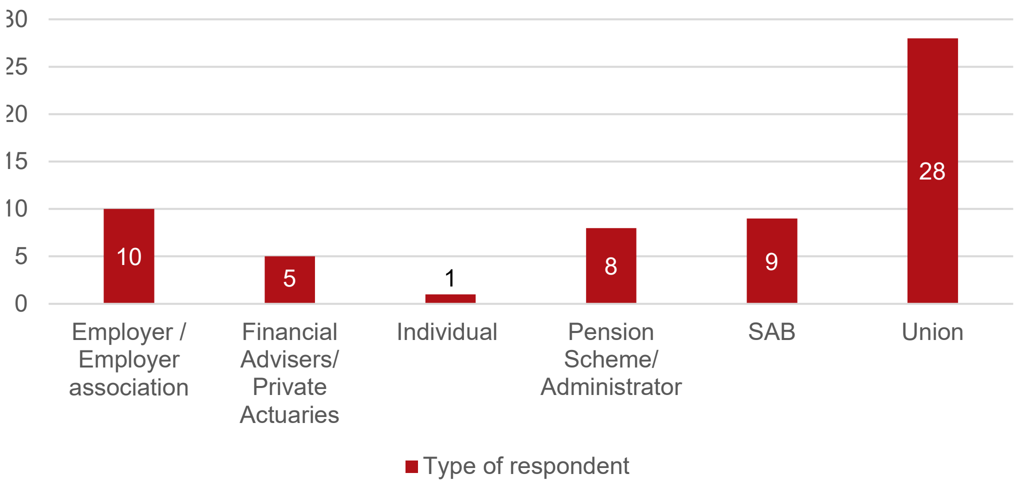
1.25 The 61 responses came from the following stakeholders:

- 9 SABs, representing the NHS (England & Wales), NHS (Scotland), Teachers (Scotland), Police (England & Wales), Police (Scotland), Local Government (England & Wales), Firefighters (England), and Firefighters (Scotland) Schemes.
- 28 trade unions and member representative bodies.
    - Of these, 10 predominantly represent members in schemes for teachers, 4 in schemes for police, 2 in schemes for firefighters, 2 in the scheme for civil servants, 1 in NHS schemes, 1 in schemes for local government, 1 in the scheme for the armed forces, and 7 across multiple schemes.
- 10 employers and employer associations.
    - Of these, 5 predominantly employer members in schemes for teachers, 2 in schemes for local government, 1 in schemes for firefighters, 1 in the scheme for the armed forces, and 1 in multiple schemes.

- 8 pension schemes and administrators.
    - Of these, 7 administer Local Government pension funds and 1 administers multiple schemes.
- 5 financial advisors and consulting actuaries.
- 1 individual.

1.26 A broad range of responses were received, as shown in Chart 1.A, which have been used to identify views and issues from members and bodies in relation to all the main pension schemes. The responses have usefully informed our assessment of the equalities impacts of the policy options, and in line with the Government's duty to have regard to the need to eliminate discrimination, advance equality of opportunity, and foster good relations in formulating its response.

Chart 1.A: Chart



Chapter 2

Changes to the core mechanism

Reformed scheme only design

Proposal

2.1 At present, the cost control mechanism assesses costs relating to active members in the legacy schemes as well as all members in the reformed schemes. The mechanism does not assess costs relating to deferred and pensioner members in the legacy schemes. In its consultation, the Government proposed excluding costs related to the legacy schemes so that, going forward, the mechanism would only consider costs associated with members in the reformed schemes (both past and future service).

2.2 A reformed scheme only design would ensure consistency between the set of benefits being assessed and the set of benefits potentially being adjusted. Under the current cost control mechanism, costs relating to active members with service in legacy schemes are assessed, but rectification can only occur in the reformed schemes. A reformed scheme only design would only assess and adjust benefits in the reformed schemes.

2.3 The consultation also set out that this proposal would reduce intergenerational unfairness as it would mean that comparatively younger members no longer experience changes to their benefits based on the cost of providing benefits to comparatively older members with past service in a legacy scheme.

2.4 Question 1 in the consultation asked whether respondents agree that a reformed scheme only design would achieve the right balance of risk between scheme members and the Exchequer (and by extension the taxpayer) and would create a more stable mechanism.

Responses

2.5 In total 60 stakeholders responded to Question 1. A high majority of respondents agreed with the proposal to move to a reformed scheme only design.

2.6 Many respondents noted that only benefits from the reformed scheme can be adjusted by the mechanism and therefore it is reasonable for the mechanism to only assess the costs of the reformed scheme.

"By reducing the size of the past service component, this would lead to a more stable mechanism, which could potentially increase confidence in the system for both members and employers. It seems reasonable to ensure that only those benefits that can be adjusted by the mechanism are considered in the assessment of cost."

Trades Union Congress (TUC)

2.7 Many respondents also agreed that this proposal would reduce intergenerational unfairness, as it seems unfair that relatively younger members in the reformed schemes should bear the risks relating to the final salary legacy schemes. They agreed that the reformed scheme only design would create a more stable mechanism over the short-medium term. Some respondents noted that stability is a key consideration of the mechanism, because frequent changes to benefits and/or contributions add more complexity to schemes and can create confusion among members.

"The NEU believes a reformed scheme only design is fairer on intergenerational grounds. This is especially the case for those members who join after April 2022 (the current proposed date to move all active members into the career average schemes). It seems unfair to make these members in particular bear risks relating to the previous final salary schemes."

National Education Union (NEU)

2.8 Some respondents noted that creating the "right" balance of risks between scheme members and the Exchequer is a different objective to that of creating a more stable mechanism, although the proposal to include both past and future service from reformed schemes in the mechanism represents a reasonable compromise between these aims.

2.9 Some respondents favoured the current design of the mechanism which takes account of costs in both the legacy and reformed schemes, and noted that a reformed scheme only design does not reflect that many members will have service in both the legacy and reformed schemes. They felt that changes in the value of final salary benefits should be taken into account when determining whether reformed scheme benefits should change, and that a cost control mechanism should cover all liabilities, not just those of the reformed schemes or future benefits.

2.10 Alternatively, a small minority of respondents argued for a future service only mechanism. They felt that the mechanism is designed to rectify any future service benefits and therefore an approach that only accounts for the revised costs of future benefits may be more appropriate. They argued that past service benefits in the reformed schemes will inevitably increase over time, and that where the impact of past service is included, but only future benefits are changed, intergenerational unfairness occurs. Therefore, they felt that a future service only design will preserve fairness for future joiners to schemes. Additionally, they felt that a reformed scheme only design will only have a short-term impact on intergenerational fairness as the value/cost of past service will build up over time. Some respondents were also concerned that one of the justifications the Government provided for rejecting a future service only design in its consultation was that it would make it *"difficult for the Government to respond to changes in overarching pension legislation which impacts past service costs or to respond to court judgements which impact past service, such as McCloud."* They felt it was not appropriate that a decision on reforming the cost control mechanism should be influenced by what they claimed was the Government's desire to avoid any future costs arising from any future wrongdoing.

> "The proposed inclusion of both past and future service reformed scheme benefits seeks to address the competing objectives of maintaining the value of a public service defined benefit pension scheme to members, and protecting the exchequer from unforeseen costs. Stability will be important for confidence on both issues and member benefit and contribution rates are of importance to members. The SPF however is less persuaded this approach will have as stark an impact as is suggested on intergenerational unfairness. Although we consider this is a likely short-term outcome, we feel it is important to observe that past service benefits will inevitably increase in value over time. The potential impact of this on the cost cap and the weighting this will add to potential floor or ceiling breaches appear obvious. The very nature of cost cap reviews could see breaches that were essentially driven by past service experience (and by default, usually by the oldest members) being addressed by changes (either in contribution rates and/or benefits) being borne by younger scheme members."
>
> Scottish Police Federation

2.11 A small number of respondents also raised questions about the potential interaction between the McCloud remedy cost and cost sharing under a reformed scheme-only design, and what impact this would have on the 2020 valuations.

2.12 Several respondents with an interest in the Local Government Pension Scheme (LGPS) noted that a reformed scheme only design may be more difficult to achieve for LGPS given the effect of the underpin[1], and it was not made clear in the consultation how the underpin will be treated under this design. They also noted that unlike for the unfunded schemes, where the risk of legacy benefits would be borne by the Government, for the funded LGPS the risk of legacy benefits would fall entirely on LGPS employers.

[1] The Local Government Pension Scheme for England and Wales (LGPS) was reformed in 2014 and all members were transferred to the reformed scheme. LGPS members in scope will be protected by an underpin in respect of any accruals from 1 April 2014 to 31 March 2022. This will provide, within the reformed scheme, whichever is the higher: the pension under the reformed scheme or the pension they would have been entitled to under the legacy scheme.

Government response

2.13 The Government has considered the responses received and remains of the view that a reformed scheme only design achieves the right balance of risks between members and the Exchequer, improves stability of the mechanism and reduces intergenerational unfairness. As set out above, this view was shared by the majority of respondents. The Government recognises that creating the right balance of risks between scheme members and the Exchequer and creating a more stable mechanism are not the same aim. However, the Government feels that a reformed scheme only design will allow the mechanism to better meet both aims. Although it means that the risk associated with legacy scheme costs will be transferred to the Exchequer, the Government believes this is the right approach to take in order to reduce intergenerational unfairness and ensure the mechanism is fairer to younger members who did not previously have access, or had access for a shorter time, to the legacy schemes.

2.14 It is acknowledged that many members will have service in both the legacy and reformed schemes. However, from 1 April 2022, it is intended there will be no members accruing benefits in the legacy schemes, and members with legacy scheme benefits will gradually leave active membership over the coming decades. The GA found that a key cause of the floor breaches seen in the provisional results of the 2016 valuations was the impact of the legacy schemes. The Government believes it is right that as the mechanism can only adjust the benefits of the reformed schemes, it should only account for the costs associated with the reformed schemes. This is emphasised by the fact that the IPSPC concluded that the structure of the legacy schemes was unfair and unsustainable, so it would not seem appropriate for these schemes to continue to influence the level of benefits in the reformed schemes.

2.15 The Government also recognises that the past service component of the reformed schemes will increase over time, and that a future service only design would therefore further reduce intergenerational unfairness and increase stability. However, the Government does not believe that the Exchequer should bear the entire risk of costs associated with past service in the reformed schemes. The mechanism was designed to protect both taxpayers and members, and the Government believes that a future service only design would not adequately protect taxpayers from unforeseen increases in costs. Additionally, the Government remains of the view that a future service only mechanism would restrict its ability to respond to future developments, such as changes in overarching legislation or court cases which may impact the value of past service benefits, such as McCloud. If a future development were to retrospectively impact the value of past service in the reformed schemes for members (for example following a legal judgment), and therefore increase the value of schemes to members, then it would be accounted for in the cost control mechanism, in line with the pre-determined framework for assessing costs. It should also be noted that under this approach, if the value of the past service component of the reformed schemes falls, the CCM would take account of this.

2.16 The Government will provide further details on how the reformed scheme-only design will be implemented at the 2020 valuations and beyond, and the extent to which there will be any interaction with the McCloud remedy at future valuations, in due course.

2.17 In relation to LGPS, the Government notes that removing the impact of legacy schemes means that these risks sit with employers. The Government acknowledges that the arrangements for budgeting for and funding LGPS employer contributions are different from the unfunded schemes. It is also acknowledged that the implementation of the reform scheme only design may be different for the LGPS given the presence of the underpin within the reformed schemes. However, the Government still believes that a reformed scheme only design is appropriate for LGPS, and that it is still fair and appropriate to remove the impact of the legacy schemes from LGPS for the same reasons as set out above, including to reduce intergenerational unfairness. The Government will work with LGPS stakeholders to consider the most appropriate way to implement this proposal for LGPS at the 2020 and subsequent valuations, including the treatment of the underpin, and provide further details in due course.

Wider corridor

Proposal

2.18 The corridor is currently set at +/-2% of pensionable pay for all schemes. In its consultation, the Government proposed widening the corridor to improve the stability of the mechanism. The Government set out that it considered a corridor of +/-3% of pensionable pay to be appropriate when applied to a reformed scheme only mechanism, which will increase the stability of the mechanism while also continuing to provide effective cost control.

2.19 Question 2 in the consultation asked for views on the Government's intention to widen the corridor. Question 3 asked for views on whether the proposed corridor size of +/-3% is appropriate.

Responses

2.20 Both questions 2 and 3 were responded to by 59 stakeholders each. A majority of respondents agreed with the proposal to widen the corridor, and a slight majority agreed that the corridor should be set at +/-3% of pensionable pay. That majority welcomed the fact that widening the corridor would lead to a more stable mechanism by minimising the frequency of breaches, which will lead to fewer changes in benefits or member contributions. They felt that a corridor size of +/- 3% was appropriate, and will strike the right balance between stability and effective cost control. However, their view was that +/-3% should be the absolute maximum size of the corridor.

2.21 A key concern amongst those who favoured retaining a +/-2% corridor was that although a wider corridor would increase stability, it would mean that changes would be too infrequent which would diminish cost control. They did not consider the estimated breach frequency of every 5 valuations[2]

[2] based on modelling provided by the Government Actuary's Department

(therefore every 20 years) expected under the current corridor to be too frequent.

> "SLS agrees with the proposal to widen the corridor to develop a more stable cost control mechanism, as per the Government's stated intention. A wider corridor will reduce volatility, leading to fewer changes in benefits or member contributions. However, it is possible that any subsequent changes will, by their definition, be greater in exacerbating the "cliff edge" nature of the cost control mechanism."
>
> School Leaders Scotland (SLS)

2.22 A majority of respondents, including many of those who agreed with the proposal for a widened corridor and supported the corridor size of +/-3%, as well as those who disagreed, raised concerns that widening the corridor exacerbates the 'cliff edge' nature of the mechanism. This is because under a wider corridor, larger changes in costs can occur without any remedial action. They noted that this would mean changes in costs between +/-2 to 3% could go unaddressed for long periods of time and argued this could cause problems to go undetected. They argue that this would increase the scale of rectification necessary when a breach does occur, which would mean significant benefit changes for members once the mechanism was triggered. A proposal put forward to mitigate the risk of dramatic changes in benefits was that when a breach occurs, the mechanism could allow schemes to bring costs back to a level within the corridor to rectify the breach, rather than back to the employer cost cap.

2.23 An alternative suggestion to manage the cliff edge risk was that schemes could be provided with discretionary powers to adjust benefits if costs moved within the corridor e.g. that schemes would have the option, but not the obligation, to adjust benefits if costs moved between +/-2% and +/-3%. They argued that providing schemes with this type of flexibility would allow for earlier and milder interventions.

2.24 Many respondents expressed concerns that a +/-3% corridor would still not lead to stability for certain schemes. They argued that a proportional cost corridor, where the size of the corridor would vary depending on the size and costs of that scheme, would be more appropriate. They felt that schemes have different overall pension costs, so a +/- 3% corridor may be proportionally narrower or wider for certain schemes versus others. They argued that while an average scheme is estimated to expect a breach frequency once every 10 valuations under a reformed scheme design with a +/-3% corridor (based on modelling from the Government Actuary's Department), schemes with higher costs could expect a breach more frequently. On this point, respondents argued that different public services have different characteristics and different workforce challenges to deal with, so sector-specific approaches may be more appropriate.

"As a scheme with a higher total long-term cost than most other public service pension schemes, we are concerned that, even with a widening of the corridor to +/-3% of pensionable pay, we may still be more likely to suffer breaches as a result of events that are not out of the ordinary, due to the fact that the cost corridor is proportionately narrower for the FPS than other public service pension schemes. For example, a 3% corridor would require a 15% increase in long-term costs for the Teachers' Pension Scheme but only a 10% increase for the FPS, for the cost cap to be breached. Therefore, while the "average" scheme might expect a breach only once every 40 years, the Fire schemes might expect a breach more frequently than this. If instead the 40 years breach was set consistently between schemes, this could be achieved by setting the corridor as equal to the 15%, say, of the cost of the scheme. Thus, if the corridor was set at +/-3%, say, for the Teachers' Pension Scheme (which had a 2012 long-term cost of 20.5%), then the proportionate corridor for the FPS, would be +/-4.4%."

Firefighters' Pensions (England) SAB

2.25 The Police Pension SAB argued that in absence of proportional cost corridor, a consistent +/-4% corridor for all schemes may be more appropriate to improve stability for those schemes with higher costs too. Some suggested that the Government should ask the GA to provide modelling specifically for each individual scheme, rather than base a decision on modelling for an average scheme. A small minority expressed concerns on whether the estimates of expected breach frequencies could be relied upon.

2.26 Some respondents felt that widening the corridor did not seem necessary if the proposal for an economic check was put in place. Similarly, a small number of respondents felt that a wider corridor would be unnecessary if a reformed scheme only design is adopted, and only supported implementing one or the other.

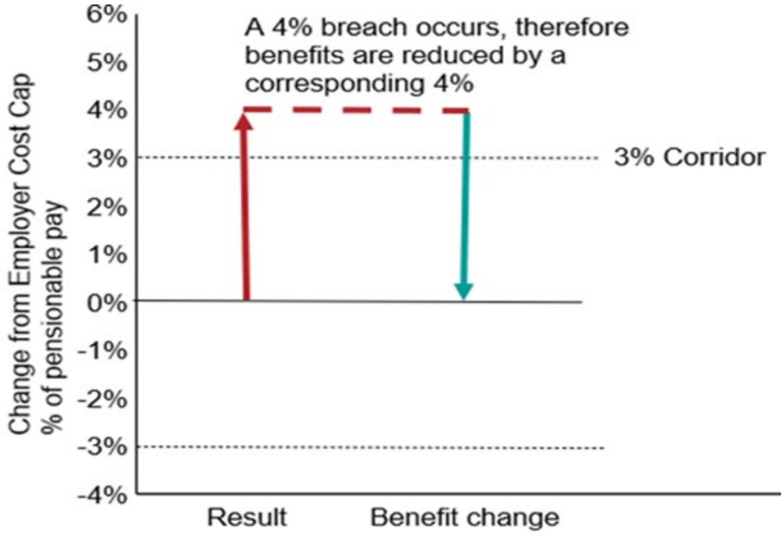
Government response

2.27 The Government recognises that a wider corridor increases the cliff edge nature of the mechanism, and that this means larger changes in costs can occur without any remedial action. This was highlighted in the GA's report and the Government considered this risk carefully as part of the consultation process. To clarify, a wider corridor will not mean that different action would need to be taken if a breach beyond +/- 3% was observed. For example, a breach of +/-4% would still require the same changes in benefits under either a +/-2% or +/-3% corridor. This is illustrated in the diagram below.

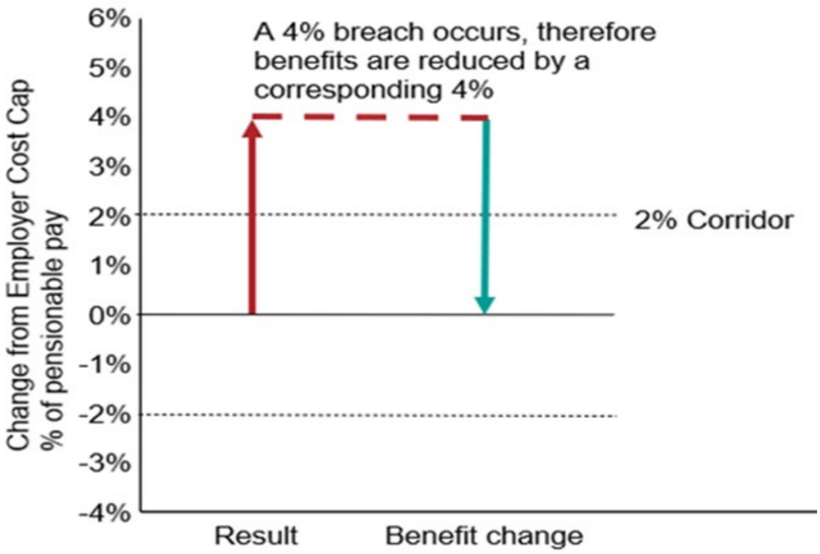
Box 2.A: Corridor width illustrations

Scenario: the costs increase by 4% of pensionable pay from the employer cost cap in a single valuation. Regardless of whether the corridor is +/-2% or +/-3%, the same level of benefit change will occur.

3% corridor



2% corridor



Illustrations provided by the Government Actuary's Department

2.28 However, a +/-3% corridor will mean that cost changes between +/-2-3% will not trigger a breach and require rectification, which could lead to a larger than otherwise breach occurring at subsequent valuations. For example, if at one valuation the results were +/-2.5% and then at the next were +/-3.5%. The Government considers that, although this risk exists, a wider corridor is necessary to ensure a more stable mechanism and limit the frequency of benefit changes. The Government considers that a +/-3% corridor would strike the right balance between providing effective cost control and a stable mechanism. A corridor size larger than this would not be appropriate as it would allow costs to diverge by too much before being brought back to target.

2.29 It is also not correct to assume that if a scheme shows cost changes between 2-3% at one valuation, then that automatically means that costs would either stay at that level or move further in the same direction at subsequent valuations and therefore result in a breach that would be larger than under a smaller corridor. Multiple factors affect the cost of a scheme. It is perfectly possible that a scheme may see a small increase in costs at one valuation, and then a reduction in costs at the next due to a change in factors. A wider corridor of +/-3% may prevent confusion and disruption for schemes and members by reducing the likelihood that smaller, temporary fluctuations in costs within the corridor will lead to benefit changes, which may then be reversed at subsequent valuations.

2.30 In response to the proposal to mitigate large benefit changes when breaches occur by allowing schemes to bring costs back to a level within the corridor rather than back to the target of the employer cost cap, the Government does not believe such an approach would provide effective cost control. Bringing costs back to the level of the cap once the +/-3% corridor is breached ensures that costs are brought back to the original level. If costs are only brought back to the edge of the corridor or to within e.g.1% of the employer cost cap, then that means the mechanism would not be maintaining value to members or fully protecting taxpayers (because as soon as costs have increased by more than 3% they will always be higher than their original level). That might result in more frequent breaches and reduce stability. Furthermore, if the approach was to allow either the Government or scheme to determine the appropriate level to bring costs back to, depending on the size of the breach, this would introduce a level of subjective decision making into the process, contrary to the transparent and mechanical process which the Government believes it is very important to maintain.

2.31 In relation to a proportional cost corridor, the GA mentioned in his report that it would be reasonable to consider this. However, the GA did not recommend this approach over a consistent corridor as a percentage of pensionable pay. The Government has considered this option and does not believe that it would be a better approach. A consistent corridor size limits the absolute change in costs that can occur across all schemes before a breach is triggered. The Government does not consider that just because a scheme is more expensive from the outset, it should be allowed to let costs change by a greater absolute amount. Furthermore, the Government considers that a proportional cost corridor would be overly complex and more difficult for members to understand than the current consistent corridor design, potentially eroding transparency and trust in the mechanism. It is important that members understand the mechanism operates consistently and transparently across all the public service pension schemes. Therefore, the Government chose not to consult on this option, and maintains the view that it is preferable to have a consistent size corridor, based on a specified percentage of pensionable pay, across all schemes. A proportional corridor could also raise concerns of fairness, as wider corridors for schemes with higher costs may appear to benefit members of some schemes over others. It could lead to a position where there is the same change in costs in two different schemes with different cost corridors (but that represent a consistent proportional cost); the scheme with a narrower cost corridor could see benefits or contribution rates adjusted whereas a scheme with a relatively wider proportional cost corridor would not. The Government acknowledges that a +/-3% corridor may result in greater stability for some schemes compared to others. However, the Government maintains that on balance, the same size corridor applied uniformly to all schemes is the fairer solution.

2.32 Similarly, the Government does not believe it would be beneficial to provide schemes with a discretionary power to adjust benefits if costs changes are observed within the +/-3% corridor. Such a discretionary power would rely on schemes reaching agreement between employers and members on whether to adjust benefits if e.g. a movement in costs between 2-3% was observed. The Government believes it is important to maintain the mechanical and objective nature of the CCM, whereas this approach would introduce an element of subjective decision making which the Government believes would increase complexity, erode transparency and reduce trust in the process. Furthermore, a key advantage of the +/-3% corridor is that it will reduce the frequency of breaches and lead to increased stability and certainty over benefit levels, which this approach will not provide to the same degree. Additionally, the lack of a consistent approach across all schemes may raise issues of fairness, as it could lead to cases where two schemes experience the same change in costs, but one agrees to adjust benefits and the other does not. The Government believes it is important to ensure that all schemes are subject to the same general rules, and that rectification action is only taken when breaches occur outside of the +/-3% corridor.

2.33 Some respondents felt that implementing a wider corridor alongside the reformed scheme only design was unnecessary. However, modelling from the Government Actuary's Department suggests that a +/-2% corridor under a reformed scheme only design would still result in expected breaches on average every 5 valuations (every 20 years), which the Government believes would be too frequent and not in line with the aim of a stable mechanism that is only triggered by unforeseen and unpredictable events. The Government believes that an estimated breach frequency of every 10 valuations (every 40 years) provides the right balance between stability and effective cost control.[3]

[3] Please note that these estimated breach frequencies are provided as a high-level indication only. They are of course just estimates based on a certain set of parameters, the actual frequency at which breaches occur is unknown and may well differ from these estimates. Furthermore, if the estimated breach frequency is for example "once every 5 valuations" for an individual scheme that does not mean it is expected to happen exactly every 5 valuations. It may mean that a scheme still breaches either the floor or ceiling at the next scheme valuation, whereas another scheme may breach after another 2, 3 or 4 valuations. Although in practice there will be a strong degree of correlation between the outcomes for different schemes.

Chapter 3
Economic check

Proposal

3.1 Currently, the cost control mechanism does not consider the long-term economic outlook (such as changes in expected long-term GDP or the long-term earnings assumption) when determining whether breaches should result in a change to member benefits. The GA recommended introducing an objective and symmetrical technical validation layer, which would only allow a breach to be implemented if it would still have occurred had the long-term economic assumptions been considered. In its consultation, the Government proposed introducing an 'economic check' to the cost control mechanism, in line with the GA's recommended design.

3.2 Under the GA's recommended design, a breach would only be implemented if the cost of a scheme still results in a breach once the impact of any change in the SCAPE discount rate on the cost of the scheme is taken into account. The consultation set out that, depending on the outcome of the review of the SCAPE discount rate methodology, the economic check would be based on objective forecasts of expected long-term GDP growth from the OBR (potentially through the SCAPE discount rate) and would also take account of changes in the long-term earnings assumption. Examples of how the economic check would work in practise are set out at Annex C.

3.3 Question 4 of the consultation asked for views on whether stakeholders agreed with the proposal to introduce an economic check. Question 5 asked for views on whether the SCAPE discount rate, which under its current methodology is linked to expected long-term GDP growth, is an appropriate economic measure for the economic check. Question 6 asked for views on whether, in the case where the SCAPE discount rate methodology changes, expected long term GDP is an appropriate measure, and if not, what other appropriate measures may be.

Responses

3.4 In total, we received 60 responses to question 4, 54 responses to question 5, and 52 responses to question 6.

3.5 In response to question 4, similar numbers of respondents agreed with the proposal to introduce an economic check as disagreed with the proposal. Some respondents were ambivalent, and noted that an economic check may be beneficial, but expressed a number of reservations.

3.6 Respondents who supported the proposals noted that it could help avoid 'perverse outcomes' such as those seen at the 2016 valuations and identified in the GA's final report, where no factors linked to the change in economic growth were considered and help improve stability. They felt it was important that a symmetrical check would also maintain scheme benefits in the event of increased scheme costs but an improved economic outlook.

> "Yes, an economic check makes sense and will help avoid perverse results such as those seen in the preliminary 2016 results where no factors linked to the change in economic growth were considered."
>
> Essex Pension Funds

> "Although the proposals fundamentally alter the cost control mechanism, some form of economic check seems appropriate since it should help to improve the stability of public sector pension schemes and avoid perverse outcomes such as that experienced with 2016 scheme valuations. Stability and affordability for government, employers and scheme members has to be sought to maintain the long-term viability of public pensions."
>
> Fire Officers' Association

3.7 Many respondents expressed concerns this proposal may be a breach of the 25-year guarantee. They argued that the economic check is a significant departure from the process for the cost control mechanism originally agreed between Trade Unions and the Government and that, during discussions at the time, it was strongly suggested by the Government that the originally agreed cost control processes were covered by the guarantee. A related concern was that the Government has previously made explicit promises that employers would meet any costs arising from changes to the SCAPE discount rate, and that such impacts would be excluded from the cost control mechanism as they were not member costs. Relatedly, some also questioned the concept of 'perverse outcomes' presented in the GA's report and noted that the exclusion of SCAPE from the CCM was an intentional decision and so there was no expectation that employer rates and the results from the CCM would move in the same direction.

> "ASCL's view is that the exclusion of the SCAPE discount rate from the cost control mechanism is a fundamental part of its design. So, whilst the discount rate currently has no impact on member's benefits, the proposal introduces a risk of to both members' benefits and contributions being affected by changes in the discount rate."
>
> Association of School and College Leaders (ASCL)

3.8 Many respondents expressed concerns that the check could easily be subject to Government or political interference, and they would need significant assurances that it would operate objectively and transparently. Some felt that the proposed design essentially amounts to a qualitative review and would lead to arbitrary decisions by Government on whether or not to apply the results of a cost control valuation. In contrast to this, others noted that a qualitative breach review, instead of or alongside an economic check, may actually be more appropriate and preferable. They recognised the need to consider the reasons behind a breach if it occurs and consider the appropriateness of any corrective actions. The NHS Scheme Advisory Board (SAB) proposed a form of qualitative breach review where the SAB would provide advice to the Secretary of State if a breach occurs. This would include an assessment of why the breach has occurred, a recommendation of whether any rectification is necessary and, if so, the extent of any such rectification. They argued that this *"places emphasis on qualitative collaboration rather than running more numbers and would be a more open and transparent process."* The SAB urged Government to give serious consideration and directly respond to this alternative proposal.

> "The cost control mechanism needs to operate independently from politics and all stakeholders and scheme members need to feel reassured that the sole purpose is to objectively measure costs without results being subject to wider political issues. Ultimately, UNISON remains unconvinced by the economic check methodology proposed in the consultation and considerable reassurance is needed from HM Treasury to ensure that any economic check is fair, transparent, and free from government manipulation. We also wish to register our concerns as to whether these proposed changes to the cost control mechanism contradict the Government's 25-year Guarantee for not making further scheme reforms and undermine the Proposed Final Agreements struck with schemes."
>
> UNISON

3.9 In relation to what measure of economic growth is appropriate, many expressed a strong view that the discount rate used in the economic check should match the rate used to set employer contribution rates, to avoid perverse outcomes in future. They argued that assumptions used to set employer contribution rates should be consistent with those used in the mechanism and the economic check. They felt that if a methodology based on the Social Time Preference Rate (STPR) was adopted for setting the SCAPE discount rate then the economic check should also be based on STPR. Others argued for the merits of using STPR on its own terms regardless of the SCAPE discount rate methodology. As STPR is a measure used to assess other government investments, they argued that it is also appropriate to assess pension costs, as public service pensions are also a form of government investment.

3.10 Some respondents highlighted that the adoption of a methodology based on expected long term GDP growth to set the SCAPE discount rate in 2011 had contributed towards increased volatility in employer contribution rates over the last 10 years. They argued that if the SCAPE methodology had remained based on STPR, employer contribution rates may not have increased at the 2016 valuations and the 'perverse outcomes' identified by the GA at the 2016 valuation provisional results would not have occurred. They therefore argued that adopting a SCAPE discount rate methodology based on STPR could negate the need for an economic check. They felt that trying to address problems caused by the SCAPE discount rate methodology through the cost control mechanism was inappropriate.

3.11 Some felt that an economic check was an unnecessary addition to the reformed scheme only and wider corridor proposals. Others supported the proposal, but only if applied to a future service only mechanism. Concerns were also expressed by some respondents that an economic check would mean that results which showed a breach may be hidden, and that SABs may not be told about the results of the mechanism before the long-term economic outlook is taken into account.

LGPS responses

3.12 Respondents with links to the LGPS were consistently of the view that if an economic check was adopted, linking it to expected long-term GDP would not be appropriate for the LGPS. They felt that unlike with the unfunded schemes, the SCAPE rate does not directly drive employer costs, which are determined by locally set discount rates, taking advice from fund actuaries as part of the triennial fund valuation process. These locally determined discount rates are designed to track the returns of each LGPS fund's investment strategy, risk appetite and globally diversified asset allocations. The LGPS, as a funded scheme, looks to achieve investment returns to ensure a minimum call on future local taxpayers by maintaining a pension fund able to meet all future liabilities. They argue that this is a fundamentally different situation to the unfunded schemes, where taxpayers are directly responsible for paying the cost of public service pensions.

3.13 Respondents proposed alternative approaches for the economic check. One key alternative was to use an LGPS specific discount rate for the economic check in relation to its application to LGPS. Such a rate could take into account factors that influence the actual discount rates in operation across the LGPS to reflect both future and past investment returns.

"..the SCAPE rate is divorced from the drivers of actual employer contributions in the scheme. These contributions, which are determined locally, use discount rates designed to track the returns of each LGPS fund's investment strategy, risk appetite and globally diversified asset allocations. A discount rate based on the OBR's long-term forecast of UK GDP is entirely appropriate for assessing the future affordability of the unfunded schemes against the projected tax base. The purpose being to ensure the costs of the scheme remain affordable to future taxpayers who will be responsible for meeting those costs. The LGPS, as a funded scheme, looks to set a discount rate for a different purpose. That purpose being to ensure a minimum call on future local taxpayers by maintaining a pension fund able to meet all future liabilities. As such the rate must be able to reflect changes in global asset values given the global nature of the scheme's investments. We would therefore propose that – should the economic check be introduced – it would, for the LGPS, use the changes in an 'LGPS discount rate' rather than SCAPE. Such a rate would take into account the factors which influence the actual discount rates in operation across the LGPS (reflecting both future and past investment returns) and would therefore be much more closely aligned with movements in employer contributions."

LGPS (England and Wales) SAB

3.14 Another alternative was based around the separate but subordinate cost management process that is operated by the LGPS (England and Wales) SAB, and was set up given the key differences between LGPS and the unfunded schemes. The current SAB process operates within and is subject to the CCM. It is broadly similar but can use different assumptions around employee cost elements. It was argued that this SAB process could act as the economic check for LGPS, and would be required to reflect movements in an LGPS specific discount rate as proposed above. It would operate in the same way as the economic check, in that it could not cause or extend a breach – only provide a check on a breach (either way). In operational terms, a breach of the HMT corridor would only result in mandatory recommendations for a change to benefits/contributions if the LGPS SAB process also resulted in a breach.

3.15 The Scottish LGPS SAB also proposed an alternative for a continuous review process rather than the current cost control process which always takes place at one point in time. The SAB suggested that such an approach could be based on a combination of the England and Wales SAB model and work undertaken by GAD, but crucially would be on a continuous basis. This would not however mean that breaches or non-breaches would be measured or that changes would need to be applied more frequently, as any decision to change could come at an agreed point in time.

Government response

3.16 The Government has considered all responses and maintains the view that an economic check should be introduced for all schemes, with further consideration required for potential allowances for the LGPS. The economic check will operate in line with the GA's recommended design and will be linked to the OBR's independent and objective measure of expected long-term GDP growth and the long-term earnings assumption. The economic check may potentially be linked to the SCAPE discount rate if the methodology remains linked to expected long-term GDP growth. The SCAPE consultation response will be published in due course.

3.17 In his report, the GA concluded that the mechanism cannot protect the taxpayer unless it has some allowance for changes in the long-term economic outlook. Ultimately, future taxpayers will pay the costs of any pension benefits accrued now. In the Government's view, the main purpose of the economic check is to ensure consistency between benefit changes and changes to the wider economic outlook. This approach ensures that there will be a higher bar for benefit increases to be awarded if the country's long-term economic outlook has worsened. This will equally apply to benefit cuts if the long-term economic outlook has improved. The Government believes that using an independent and objective measure of expected long-term GDP growth best serves this purpose. For the unfunded schemes, pensions are paid out of general taxation, so the Government feels it is appropriate to introduce an economic check to ensure the mechanism is better able to protect the taxpayer. However, the Government also feels it is equally important to honour the objective to protect the value of schemes to members, and therefore the economic check will operate symmetrically to also protect the value of schemes to members.

3.18 The Government agrees that it is of the utmost importance that an economic check should be implemented in a transparent way, and that the process will be mechanistic and objective. The Government can confirm that the economic check will apply symmetrically, operating in the exact same way in relation to floor breaches as it would to ceiling breaches. It will operate purely mechanically, with no scope for interference from individuals or groups, either from within the Government, or outside.

3.19 The costs of the schemes would be assessed excluding any changes to the long-term economic variables, as they are now, to see if a breach has occurred. If a breach has occurred, in either direction, then the calculation would be repeated with the measure of the wider economic situation – changes in expected long-term GDP and changes in the long-term earnings assumption - taken into account. If a breach had still occurred in the same direction following this second calculation, only then would it be implemented, with the smaller of the two breaches being implemented. In this way, the economic check could offset a breach of either the floor or the ceiling, but it could never cause a breach or increase the size of a breach. The economic check would apply to initial breaches in either direction, so would operate symmetrically.

3.20 The Government does not currently see the value in implementing a subjective breach review, either instead of or alongside the economic check.

The Government believes that a key advantage of the economic check is that it will be mechanistic and transparent, and apply consistently across all schemes. The Government believes it would be difficult to ensure that a subjective breach review could operate in the same way so that members felt that their benefits were being decided in a transparent way.

3.21 In response to the alternative suggestion from the NHS SAB, the Government feels this again raises the same issues as a discretionary power to take action when costs move within the corridor. Such an approach would introduce a level of subjective decision making into the process and not be in line with the Government's intention to maintain an objective, technical and mechanical CCM, and the views of many respondents who wanted reassurance that the check would not be subjective. Such an approach would also not be in line with the main objective of the economic check, to ensure consistency between benefit changes and changes to the wider economic outlook. It is difficult to determine how an individual, group or SAB could make such a judgement without considering long-term GDP projections in any case.

3.22 The Government will shortly respond to its consultation on the methodology used to set the discount rate for setting employer contribution rates in the unfunded public service schemes. The Government invited respondents to provide views what it believes are the two most appropriate possible methodology options for setting the SCAPE discount rate: a methodology based on expected long-term GDP growth and a methodology based on STPR. Respondents were also able to suggest alternative methodologies. In reaching a decision on the SCAPE discount rate methodology, the Government will have regard to the distinct objectives for the SCAPE discount rate, which differ to the cost control mechanism, and points raised by stakeholders in support of consistency between the discount rate and the economic check.

3.23 The Government does not believe that the STPR would be an appropriate measure for the economic check. The STPR is set by HM Treasury as an estimation of society's preference for consumption sooner rather than later and is used by the Government to appraise the value for money of projects which involve short-term public expenditure to deliver future welfare benefits. The STPR is not intended to provide an estimate of the long-term economic outlook.[1] As a result, it does not fulfil the purpose of the economic check: to ensure consistency between benefit changes and changes in the wider economic outlook. Therefore, the measure of long-term economic outlook applied to the economic check will be linked to expected long-term GDP growth for the reasons set out above. The economic check may potentially be linked to the SCAPE discount rate if the methodology remains linked to expected long-term GDP growth.

3.24 The Government recognises that the addition of the economic check is introducing a new step into the process, and that political statements were

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[1] For further details on the Social Time Preference Rate please see Annex 6 of the Green Book. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/938046/The_Green_Book_2020.pdf

made to the effect that the 25-year guarantee would mean that there should be no changes to scheme design, benefits or contribution rates outside of the processes agreed for the CCM. However, the Government does not believe that the proposal for the economic check necessarily breaches the 25-year guarantee. The elements protected by the 25-year guarantee in law are set out in section 22 of the Public Service Pensions Act 2013 and include i) the CARE nature of schemes, ii) member contribution rates and iii) benefit accrual rates. The cost control mechanism is not one of the protected elements. Furthermore, the Government is proposing this change following a thorough and independent review of the mechanism by the GA. As the GA's report makes clear, the CCM processes are not operating properly to serve its objective to sufficiently protect taxpayers. The Government is now seeking to implement the economic check to improve the CCM process and ensure the mechanism is better able to meet this objective, while also ensuring that the mechanism equally continues to protect members.

3.25 Furthermore, the introduction of the economic check will reduce the likelihood that member benefits can be reduced or increased in future, in line with the principles of the 25-year guarantee to provide greater stability and confidence to members on benefit levels. It is right that Government is able to review policy and make changes if it is felt that a key element of a reform is not operating as designed, after following a proper process of review and an open and transparent consultation. The Government is not proposing to make changes to the objectives of the mechanism themselves. However, the Government believes that even if the introduction of the economic check were to contradict previous statements made, it would in any event be justified and proportionate to depart from those statements in the circumstances. The economic check will maintain the technical and symmetrical nature of CCM processes and will never be able to cause benefit reductions, or benefit improvements, only prevent or reduce benefit changes.

3.26 The Government recognises that when the mechanism was set-up, the intention was that changes in the SCAPE discount rate, and by extension changes in expected long-term GDP growth, would be excluded and would not impact on member benefits. However, in line with the GA's recommendations and for the reasons set out above, the Government believes it is now justified and appropriate to introduce the impact of changes in expected long-term GDP growth to the mechanism, albeit in a limited way, through the economic check.

3.27 While some respondents felt that the economic check would be unnecessary under a reformed scheme only design and a 3% corridor, the Government believes all three proposals should be implemented in tandem. Without the economic check, the mechanism will not be able to ensure consistency between benefit changes and changes in the wider economic context. In relation to suggestions that the economic check should only be implemented under a future service only design, the Government does not believe a future service only design would be appropriate for the reasons provided in chapter 2.

3.28 In response to concerns around whether schemes will be notified at future valuations of how schemes costs have changed prior to the application of the economic check, and to ensure transparency, the Government would expect valuation reports to publish results both before and after the impact of the economic check.

Government response for the LGPS

3.29 The Government has taken into consideration the concerns raised by LGPS stakeholders that an economic check linked to expected long-term GDP growth is not appropriate for the funded LGPS. The Government recognises the different nature of the LGPS, which is funded and where money is invested in a diverse range of global assets, and acknowledges that different considerations apply to LGPS. In particular, expected long-term GDP growth is not used to set employer contribution rates for LGPS. However, on balance, the Government still believes that the economic check as a whole is an appropriate proposal for LGPS.

3.30 Firstly, while it is correct that the discount rate used to set employer contribution rates in LGPS will be based on expected investment returns, expected long-term GDP growth should act as a broad proxy for this and therefore the use of the economic check as envisaged would still appear to be relevant. Furthermore, as noted by respondents, the purpose of LGPS investments is to minimise the cost pressures facing LGPS employers who will meet the balance of costs. If the cost of benefits go up the responsibility will fall on local authorities, who are funded to a significant extent by local taxpayers, and other LGPS employers. Similar to the reason for the economic check for the unfunded schemes, the purpose is to ensure consistency between benefit changes and changes in the wider economic outlook. Whilst the financial health of individual local authorities is not directly linked to the expected long-term GDP growth, the Government would still expect a link between the economic performance of the UK and the financial health of local authorities. It is also important to note that the IPSPC reforms were intended to provide some commonality of design and value across the public service pension schemes, particularly for the non-uniformed services, which also requires similarities of approach in valuing and amending schemes. A consistent approach also means that public service workers will not be treated differently in unfunded and funded schemes. Therefore, having considered the alternatives, the Government remain of the view that an economic check linked to expected long-term GDP is appropriate for the LGPS.

3.31 In relation to the 2 alternative proposals, the Government does not consider they would be appropriate to include in the mechanism. An LGPS specific rate based on a best estimate of expected returns would introduce a level of subjectivity into the mechanism, as any discount rate based on future investment returns would be subjective, and there will be a huge range of views on how any particular asset may be expected to perform. As noted above, the Government does not currently believe that introducing a level of subjectivity into the mechanism is desirable, as it may erode transparency and trust in the process. The Government also does not believe there should be a change to the current dynamic between the England and Wales LGPS

SAB process and the cost control mechanism. The Government believes that the current interaction between the 2 separate but linked processes should be maintained. Given the different nature of the LGPS, the Government acknowledges the value of the SAB process in that it can take account of LGPS specific assumptions to provide a recommendation to the Government as part of the cost control valuations.

3.32 HM Treasury will work with the Department for Levelling up, Housing and Communities and LGPS stakeholders to consider whether it is desirable for the England and Wales SAB process to be adapted in line with the principles of the economic check. The Government also acknowledges that the Scottish and Northern Irish SABs may wish to consider introducing a similar process to the England and Wales SAB and will work with colleagues in the Devolved Administrations if they feel it would be desirable to do so.

3.33 In relation to the alternative proposal from the Scottish LGPS SAB, the Government believes this proposal is to effectively replace the cost control mechanism entirely, rather than just reform it. The Government does not wish to fundamentally replace the cost control mechanism with an alternative cost management approach, but to improve its operation.

Other issues raised

3.34 Some respondents raised other issues not directly related to the questions posed in the consultations, which the Government has sought to address below.

3.35 Some respondents noted that they did not believe an 8-week timeline for consultation was long enough to adequately respond to the consultation, especially given the complexity of the topic area and that the consultation was held over the summer period. The Government also received requests from a small number of respondents for a short extension to the consultation deadline towards the end of the consultation period. The Government carefully considered the appropriate period for consultation in advance of launching the consultation, and revisited its justification in light of later requests for an extension. The Government believes that 8 weeks was a sufficient period of time to allow the full range of stakeholders to provide a considered response to the questions raised. However, to ensure that key stakeholders were as informed as possible, and to mitigate concerns about the consultation period, HM Treasury decided to supplement the consultation document by holding several official-led consultation events with employer and member representative groups over the consultation period. The Chief Secretary to the Treasury also met with the TUC to discuss issues raised in the consultation. Additionally, an important consideration was ensuring that the consultation was concluded in time to ensure any changes to the CCM could be implemented in time for the 2020 valuations. As the GA has found, the mechanism is not operating in line with its objectives, and the Government believes it is crucial that the changes outlined above are in place for the next scheme valuations. In light of this, the Government believes that the correct balance has been struck between providing sufficient time for informed and intelligent responses, and the need to implement the reforms in time for the 2020 valuations.

3.36 Some respondents noted that the baseline assumptions and estimates used to set the employer cost caps at the 2012 valuations may be flawed and the Government should consider whether these remain appropriate for the purposes of the CCM or whether they need to be reset. The Government does not believe that the employer cost caps need to be reset based on a new set of assumptions. The Government believes it is normal and expected that actuarial assumptions are updated at each valuation as further experience comes to light and views of the future change. Revised assumptions, such as those seen at the 2016 valuations, are therefore not a reason to reset the employer cost caps. The employer cost caps were set using best estimate assumptions of the costs at the time the reformed schemes were introduced and this policy decision made at the time is not being revisited. This was also not a recommendation made by the GA.

3.37 Many respondents also raised the fact that the 2016 valuation process has not yet been completed, and the Government's decision to include the cost of McCloud remedy within the mechanism at the 2016 valuations. The Government has previously set out the rationale for the decision to reflect the McCloud remedy in completing the cost control element of the 2016 valuations.[2] The Government will finalise the Directions to complete the 2016 process in due course.

3.38 Some respondents noted that changes in life expectancy have an impact on pensions, but the impact of longevity is largely mitigated by the link to the State Pension Age in some of the reformed schemes. The consultation noted that the GA had also considered this issue and set out two considerations for Government in light of this: i) the Government could remove the impact of changing longevity and SPA from the mechanism for the relevant schemes, given they already have mitigation in place; or ii) alternatively, the Government could consider smoothing longevity assumptions given their potentially disproportionate impact on the mechanism and the likelihood for such assumptions to fluctuate. One respondent noted their opposition to these two proposals. However, the Government did not consult on these proposals. As noted in the consultation, the Government will consider these recommendations on longevity to a longer timescale.

Next steps

3.39 The Government is aiming to implement all three reforms to the CCM in time for the 2020 valuations, through the appropriate legislative vehicle. It is necessary to implement the reformed scheme only design and the economic check through expanded powers in primary legislation, when parliamentary time allows, and then by making Treasury Directions under those powers in due course. The wider cost corridor will be implemented to a longer timeline via secondary legislation.

2 https://www.gov.uk/government/consultations/public-service-pension-schemes-consultation-changes-to-the-transitional-arrangements-to-the-2015-schemes/outcome/update-on-the-2016-and-2020-valuations

Annex A
Schemes in scope

A.1 The consultation covered schemes for the following public servants:

- Civil servants;
- The judiciary;
- Local government workers for England, Wales and Scotland;
- Teachers for England, Wales and Scotland;
- Health service workers for England, Wales and Scotland;
- Fire and rescue workers for England, Wales and Scotland;
- Members of police forces for England, Wales and Scotland;
- The Armed Forces.

A.2 The GA's review also considered the corresponding schemes provided in Northern Ireland. Cost control provision for the equivalent and similarly constituted Northern Ireland public service schemes established under the Public Service Pensions Act (NI) 2014 broadly reflects that provided under the Public Service Pensions Act 2013. The consultation welcomed input from interested stakeholders across all of the UK public service schemes.

A.3 Other public servants also have pension schemes which mirror the cost control mechanism, although they are not legislatively required to do so.

A.4 The Local Government Pension Scheme (England and Wales) also has a second and separate cost control mechanism operated by its Scheme Advisory Board. The scheme will consider any necessary changes to this second mechanism in the light of the overall changes made across schemes.

Annex B
Equality impact assessment

B.1 The Government has considered the equalities impacts of these proposed changes. This section records the equalities analysis undertaken in relation to all three reforms to the cost control mechanism, to enable Ministers to fulfil the requirements placed on them by the Public Sector Equality Duty (PSED) as set out in section 149 of the Equality Act 2010.

B.2 Question 7 in the consultation asked for views on any equalities impacts envisaged from the proposals to reform the mechanism which the Government should take account of. The analysis in this section builds on, and updates, the equalities impact analysis undertaken by HM Treasury set out in the consultation document, in light of the responses received to question 7.

B.3 When formulating policy, the government is required to comply with the PSED. The duty requires public bodies to have due regard to the need to eliminate discrimination, advance equality of opportunity and foster good relations between people with different protected characteristics when carrying out their activities. This section includes the assessment of the impacts of the three policies outlined above (reformed scheme only design, +/-3% corridor and economic check), by reference to the protected characteristics identified in the Equality Act 2010 of: sex, age, disability, race, religion or belief, gender reassignment, pregnancy and maternity, sexual orientation and marital or civil partnership status.

B.4 In total, 54 responses to question 7 were received. A majority of respondents believe that these proposals will have an equalities impact, with the impact on age and intergenerational unfairness being the key consideration. However, some respondents also raised equalities impacts in response to questions 1-6, and those comments have also been considered as part of the analysis in this section.

Age

B.5 The Government acknowledges that the policies set out in the consultation response may have different impacts on people depending on their age. It has considered whether those potential impacts are proportionate and justified and has concluded that they are, as set out below.

B.6 Some respondents raised the impact on intergenerational unfairness of the Government's decision to account for the costs of McCloud remedy as part of completing the cost control element of the 2016 valuation process. As the consultation focussed on the three proposed reforms to the mechanism, with the aim of implementing them in time for the 2020 valuations, the

Government has only sought to analyse the impacts of these three reforms in this section. The Government has not sought to address any equalities impacts in relation to decisions relating to the 2016 valuations in this document.

Reformed scheme only design

B.7 Respondents generally felt that a reformed scheme only design would have positive consequences for younger members of the scheme and reduce intergenerational unfairness. They felt that moving to a reformed scheme only design would mean that comparatively younger members will not experience changes to their benefits based on costs associated with relatively older members in the legacy final salary schemes.

B.8 In contrast, some respondents noted that younger members would benefit if reformed scheme benefits were improved if the impact of including legacy scheme costs led to a floor breach. They argued that excluding the impact of legacy service would therefore not necessarily benefit younger members or those with mixed service.

B.9 The move to a reformed scheme only design will have an overall positive impact on intergenerational fairness, although some age-related consequences remain.

B.10 The protected nature of accrued pension rights and the design of the cost control mechanism are such that it is not possible to exactly align the change in costs that trigger a breach with those who will directly be affected by any related rectification. Currently, the cost control mechanism delivers something of an 'intergenerational transfer': past service costs associated with a group of employees who are, on average, older, affect the pension benefits/contributions of a group of employees who are younger on average – though the latter group will include some of the former group. It is inherent in the design of defined benefit schemes that members in a particular scheme mutually share the risks and benefits, and that there are cross-subsidies between members. Whilst such an 'intergenerational transfer' remains within a reformed scheme only cost control mechanism, it is now with respect to a consistent scheme design. This would appear to be more intergenerationally fair than the current mechanism whereby comparatively younger members experienced changes to their benefits based on the cost of providing benefits to comparatively older members with past service in a legacy scheme that the comparatively younger members never had access to.

B.11 However, whilst improving overall intergenerational fairness, a consequence of this change is that if the value of benefits in the legacy schemes to members reduces, there would be no corresponding increase in reformed scheme benefits, which would impact members with significant legacy scheme benefits who are, on average, older.

B.12 On balance, the Government considers that removing the impact of legacy scheme costs from the mechanism will have an overall positive impact on intergenerational fairness, for the reasons set out in chapter 2 above, which most respondents supported. The Government recognises that younger members would also benefit if legacy impacts led to floor breaches, however, if legacy impacts led to ceiling breaches in future, this would mean that younger members would see their benefits reduced as a result of costs relating to the legacy schemes. The Government therefore considers that a reformed scheme only design is fair and proportionate.

Wider corridor

B.13 Some respondents noted that widening the corridor to +/-3% may also have an impact on intergenerational unfairness. They argued that there may be a greater intergenerational impact if the wider corridor led to less frequent benefit adjustments, since those in service following the breach will have their benefits adjusted, whereas relatively older members who will have retired or be closer to retirement would be unaffected or less affected. They argued that more frequent benefit adjustments may be fairer across the age range, because the impact of breaches would be felt more frequently by members across their service.

B.14 The Government recognises agrees that a wider corridor should lead to fewer breaches of the mechanism and fewer benefit adjustments, which may have an impact on intergenerational fairness, depending on the underlying causes of the breach when it does occur. However, a wider corridor may also insulate relatively younger members from smaller and temporary changes in costs related to the past service of relatively older members. The Government maintains the view that the benefits provided by a wider corridor in terms of increased stability and certainty of benefit levels for members make it a justified and proportionate measure to introduce.

Economic check

B.15 Respondents did not raise any particular points on the impact of the economic check on intergenerational fairness.

B.16 The Government considers that the economic check will make it less likely that breaches of the floor and ceiling are implemented through benefit increases or benefit reductions. As the economic check is expected to lead to fewer benefit adjustments, this may have an impact on intergenerational unfairness in the same way as a wider corridor, depending on the underlying causes of the breach when it does occur. However, it may also insulate relatively younger members from benefit changes based on smaller and temporary changes in costs. Furthermore, due to its symmetrical design, it will insulate younger members in relation to both benefit increases and reductions. The Government maintains the view that the benefits provided by a wider corridor in terms of increased stability and certainty of benefit levels for members make it a justified and proportionate measure to introduce. The Government has also set out that it believes the economic check is necessary to protect taxpayers by ensuring consistency between benefit changes and changes in the wider economic outlook whilst also maintaining the value of schemes to members.

Sex

B.17 Some respondents noted that these proposals may have an indirect impact on women, as women are generally overrepresented across the public sector and are more likely to be part-time workers, particularly in certain public sector workforces such as local government.

B.18 The policies outlined apply regardless of sex and to all members regardless of full-time or part-time status. The Government, therefore, does not expect there to be a direct impact on women from these proposals.

B.19 However, the government acknowledges there may be an indirect impact insofar that women have entered the workforce in greater numbers as time has progressed, meaning that they account for a greater proportion of younger cohorts than they do of older cohorts. Therefore, women may be disproportionately affected by proposals which also have a differential impact by age.

B.20 For instance, as women in the workforce in the workforce are more likely to be younger, they might be more affected by the fact that, under a reformed scheme only design, members will not experience changes to their benefits based on costs associated with relatively older members in the legacy final salary schemes. This will disproportionately advantage women where legacy scheme costs would otherwise result in a reduction in benefits.

B.21 Women may be relatively less disadvantaged in the scenario that the value of benefits in the legacy schemes reduces and there is no corresponding increase in reformed scheme benefits, as this would impact members with significant legacy scheme benefits who are, on average, older and so more likely to be male. In contrast, where younger members with no or little legacy scheme benefits, who are more likely to be women, would have previously seen an increase in their benefits in this scenario despite the change in value relating to benefits of earlier cohorts, they will no longer be disproportionately advantaged.

B.22 As set out above, the Government considers that a reformed scheme only design is fair and proportionate. This is particularly so as a reformed scheme only design means more women will be insulated from benefit changes based on changes in costs associated with legacy schemes of which they are relatively less likely to be members, and those legacy scheme costs could otherwise lead to both ceiling and floor breaches.

B.23 Women may also be disproportionately impacted by changes which are expected to reduce the frequency of breaches - the economic check and widened corridor - depending on the underlying causes of the breach when it does occur and whether they are associated with costs for older members, who are more likely to be men. However, women may also be relatively more insulated from smaller and temporary changes in costs related to the past service of relatively older members who are more likely to be men.

B.24 As set out above, the Government believes that the benefits provided by a wider corridor and economic check, in terms of increased stability and certainty of benefit levels for members, make them justified and proportionate measures to introduce. The Government believes these reforms strike an appropriate balance between the the need to protect taxpayers while preserving the value of schemes to members, and the duty to do so in a way that does not unnecessarily disadvantage women. This is evidenced by the fact that women may be either net beneficiaries or net losers of the policy depending on prevailing economic and financial factors unrelated to sex.

Other protected characteristics

B.25 As the policy proposals outlined apply equally to public service pension scheme members, the Government does not consider it likely that there will be direct impacts from these proposals on those with other protected characteristics, such as race or disability.

B.26 However, the Government recognises there may be indirect impacts in relation to race and other protected characteristics. This is because a higher proportion of younger members are likely to have protected characteristics such as disability, sexual orientation or being from an ethnic minority compared to older members. This is through a combination of demographic changes, because members of these groups have entered the workforce in greater numbers over time and because several employers have made efforts to increase diversity among their workforce.

B.27 Consequently, the same analysis set out above in relation to women is also expected to hold in relation to these groups. As members of these groups in the workforce are more likely to be younger, they might be more affected by the fact that, under a reformed scheme only design, members will not experience changes to their benefits based on costs associated with relatively older members in the legacy final salary schemes, who are more likely to be white, heterosexual, and to not disclose a disability. This will disproportionately advantage these groups where legacy scheme costs would otherwise result in a reduction in benefits.

B.28 These groups will also be relatively less disadvantaged in the scenario that the value of benefits in the legacy schemes reduces and there is no corresponding increase in reformed scheme benefits, as this would impact members with significant legacy scheme benefits who are less likely to hold these characteristics. In contrast, where younger members with no or little legacy scheme benefits, of which these groups are more likely to be part of, would have previously seen an increase in their benefits in this scenario despite the change in value relating to benefits of earlier cohorts, they will no longer be disproportionately advantaged.

B.29 The Government considers that a reformed scheme only design is fair and proportionate way of achieving its policy aims. This is particularly so as a reformed scheme only design means later cohorts with less service in legacy schemes, and which are more likely to include members with protected characteristics, will be insulated from benefit changes based on changes in costs associated with legacy schemes of which they are relatively less likely to be part of, which could otherwise lead to either ceiling or floor breaches.

B.30 Members with protected characteristics of race, sexual orientation or disability may also be disproportionately impacted by changes which are expected to reduce the frequency of breaches - the economic check and widened corridor - depending on the underlying causes of the breach when it does occur and whether they are associated with costs for older members, who are less likely to hold these protected characteristics. However, by reducing the frequency of breaches, these measures may insulate members with these protected characteristics from smaller and temporary changes in costs which are related to the past service of earlier cohorts which they are less likely to be part of.

B.31 Again, the Government believes that the benefits provided by a wider corridor and economic check, in terms of increased stability and certainty of benefit levels for members, make them justified and proportionate measures to introduce. The Government believes these reforms strike an appropriate balance between the need to protect taxpayers while preserving the value of schemes to members, and the duty to do so in a way that does not unnecessarily disadvantage members with protected characteristics. This is supported by the fact that members with protected characteristics may be either net beneficiaries or net losers of the policy depending on prevailing factors unrelated to these characteristics.

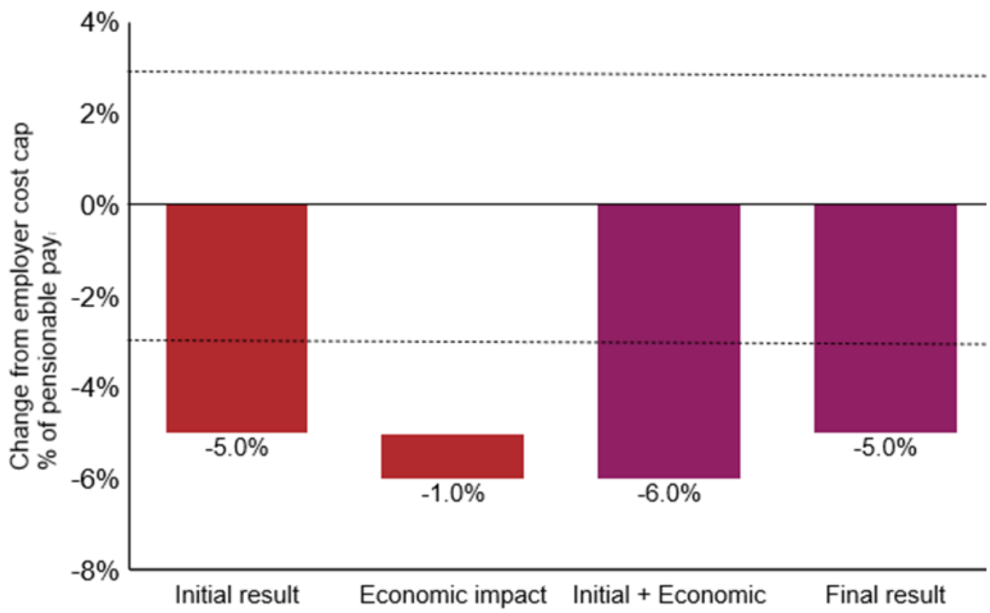
B.32 The Government does not have sufficient evidence to consider the impacts on other protected characteristics not mentioned here. Collecting this data would not have been proportionate as it would have required public service pension schemes to collect and hold new data on its members that it does not currently hold. In making this assessment Government has considered the burden on members and the presumption that public bodies should not hold data on individuals that it does not require to fulfil its core purposes.

Annex C

Economic check illustrations

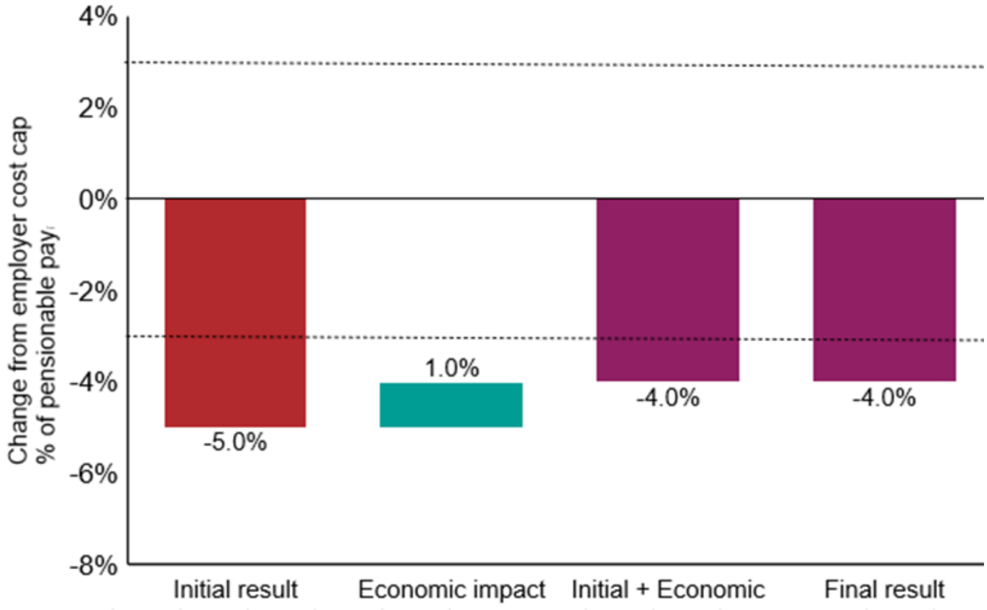
C.1 The following scenarios illustrate how the economic check will work in practice. They are similar to the scenarios included in the consultation document and the Government Actuary's report, but have been updated to consider a +/-3% corridor width.

Box C.1: Scenario 1



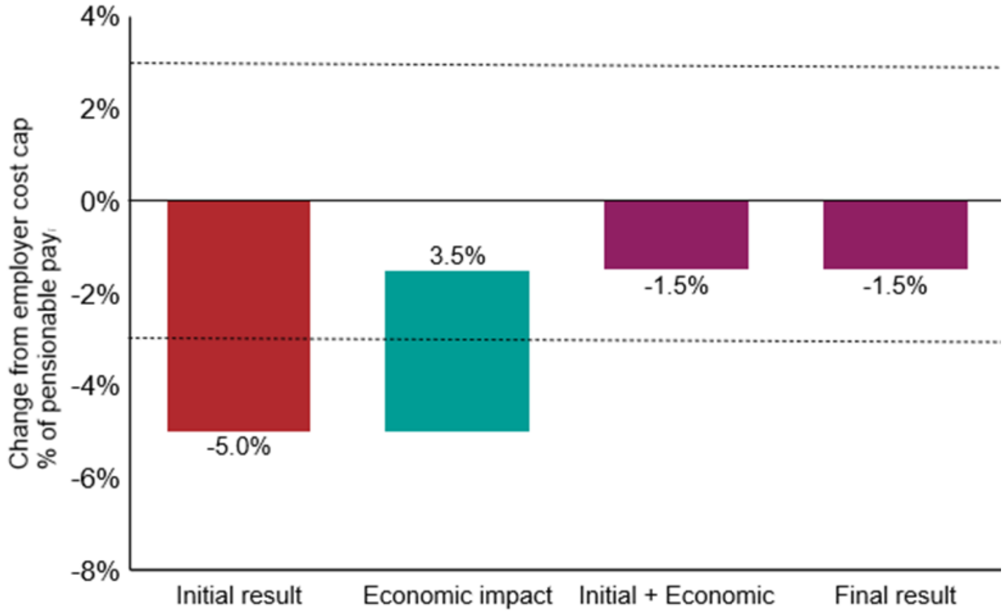
- The initial result of the cost control mechanism is that costs have reduced by 5% of pensionable pay from the employer cost cap
- The discount rate has increased slightly from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would reduce assessed costs by a further 1% of pensionable pay
- The change in discount rate can only offset a breach and cannot cause or contribute to one. Therefore, the final result of the cost control mechanism remains at a reduction of 5% of pensionable pay from the employer cost cap

Box C.2: Scenario 2



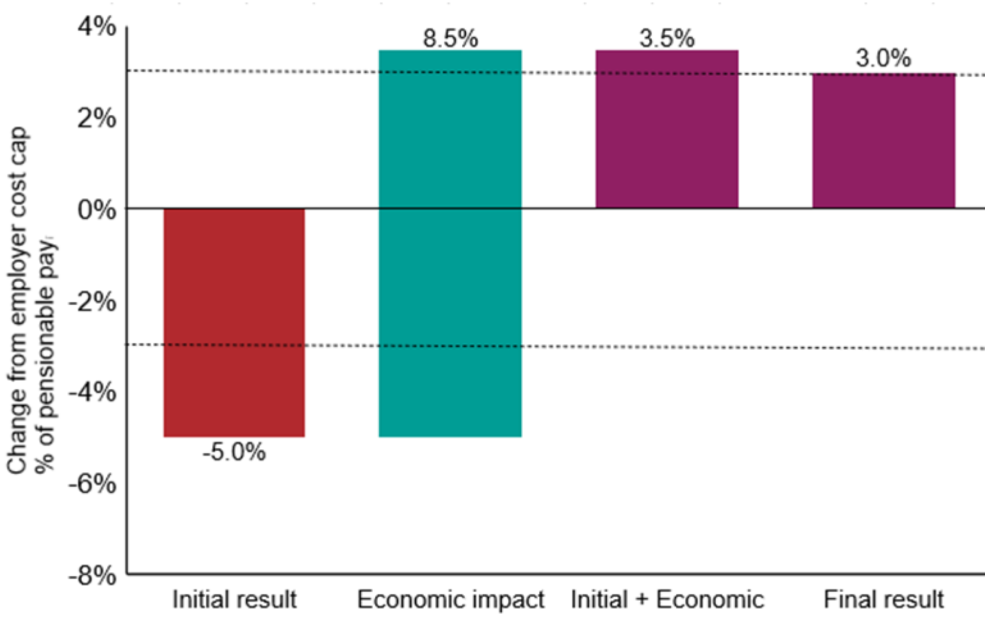
- The initial result of the cost control mechanism is that costs have reduced by 5% of pensionable pay from the employer cost cap
- The discount rate has decreased slightly from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would increase assessed costs by 1% of pensionable pay in isolation
- This impact would partially offset the initial breach with the final result of the cost control mechanism being a reduction of 4% of pensionable pay from the employer cost cap

Box C.3: Scenario 3



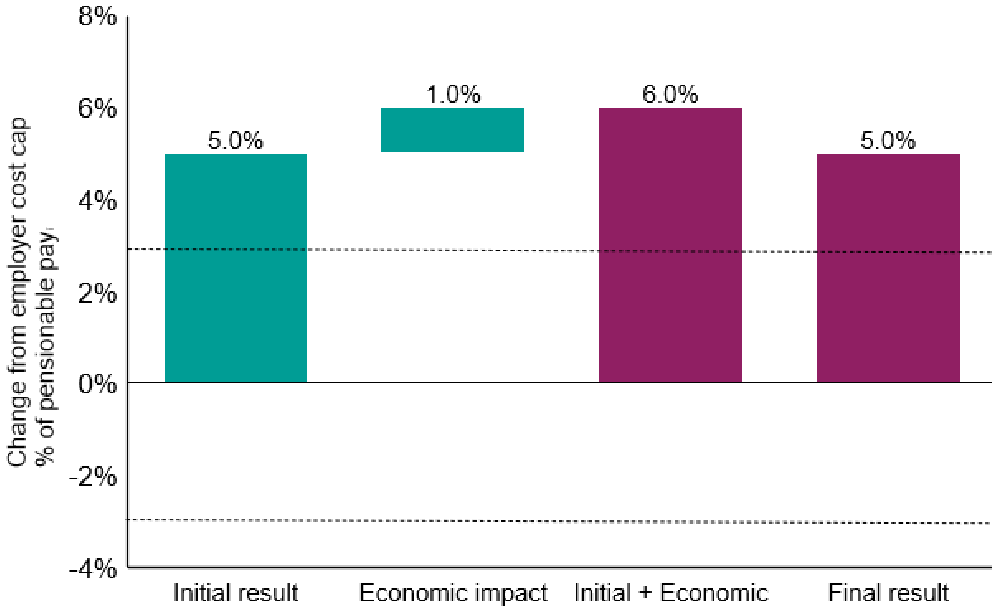
- The initial result of the cost control mechanism is that costs have reduced by 5% of pensionable pay from the employer cost cap
- The discount rate has decreased from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would increase assessed costs by 3.5% of pensionable pay in isolation
- This impact would offset the initial breach with the final result of the cost control mechanism being a reduction of 1.5% of pensionable pay from the employer cost cap. In this scenario the final result is back within the corridor and therefore no benefit changes would occur

Box C.4: Scenario 4



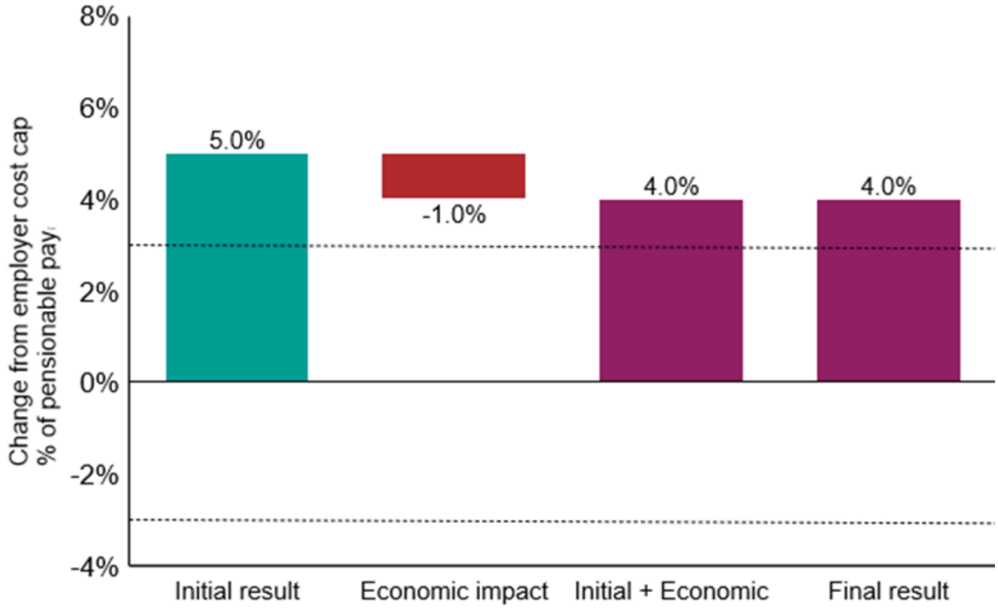
- The initial result of the cost control mechanism is that costs have reduced by 5% of pensionable pay from the employer cost cap
- The discount rate has significantly decreased from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would increase assessed costs by 8.5% of pensionable pay in isolation
- This impact would more than offset the initial floor breach and instead cause a ceiling breach. However the impact of a change in the discount rate can only offset a breach and cannot in itself cause one, therefore no benefit changes would occur
- Note that for illustration purposes the final result is depicted at the edge of the opposite corridor to the initial breach. A decision on what exactly the quoted final result would be in this situation has yet to be made, however the important point is that the final result would be treated as being within the corridor and no breach would occur

Box C.5: Scenario 5



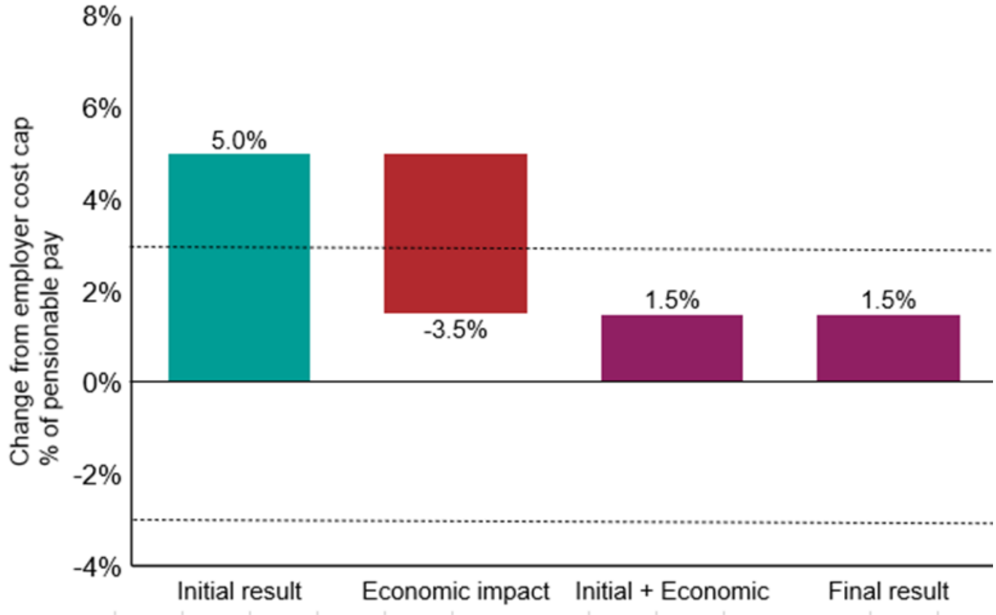
- The initial result of the cost control mechanism is that costs have increased by 5% of pensionable pay from the employer cost cap
- The discount rate has decreased slightly from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would increase assessed costs by a further 1% of pensionable pay
- The change in discount rate can only offset a breach and cannot cause or contribute to one. Therefore, the final result of the cost control mechanism remains at an increase of 5% of pensionable pay from the employer cost cap

Box C.6: Scenario 6



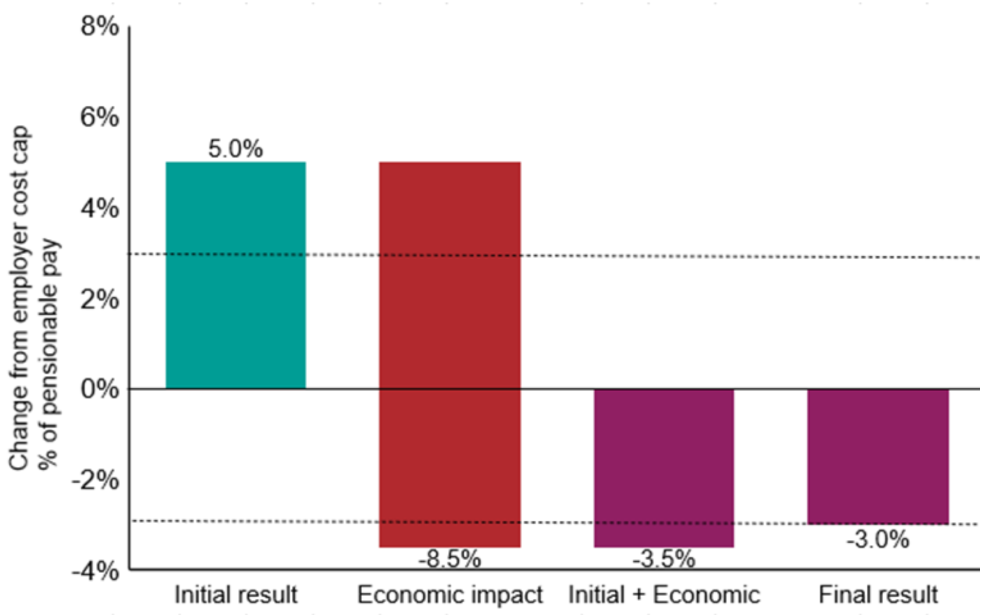
- The initial result of the cost control mechanism is that costs have increased by 5% of pensionable pay from the employer cost cap
- The discount rate has increased slightly from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would decrease assessed costs by 1% of pensionable pay in isolation
- This impact would partially offset the initial breach with the final result of the cost control mechanism being an increase of 4% of pensionable pay from the employer cost cap

Box C.7: Scenario 7



- The initial result of the cost control mechanism is that costs have increased by 5% of pensionable pay from the employer cost cap
- The discount rate has increased from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would decrease assessed costs by 3.5% of pensionable pay in isolation
- This impact would offset the initial breach with the final result of the cost control mechanism being an increase of 1.5% of pensionable pay from the employer cost cap. In this scenario the final result is back within the corridor and therefore no benefit changes would occur

Box C.8: Scenario 8



- The initial result of the cost control mechanism is that costs have increased by 5% of pensionable pay from the employer cost cap
- The discount rate has significantly increased from the 3% a year (net of CPI) rate in force at the time employer cost caps were set. If this were to be recognised in the mechanism it would decrease assessed costs by 8.5% of pensionable pay in isolation
- This impact would more than offset the initial ceiling breach and instead cause a floor breach. However the impact of a change in the discount rate can only offset a breach and cannot in itself cause one, therefore no benefit changes would occur
- Note that for illustration purposes the final result is depicted at the edge of the opposite corridor to the initial breach. A decision on what exactly the quoted final result would be in this situation has yet to be made, however the important point is that the final result would be treated as being within the corridor and no breach would occur

HM Treasury contacts

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From:	Chairman Superannuation Fund Committee Corporate Director of Finance
To:	Superannuation Fund Committee – 1 December 2021
Subject:	Pensions Administration
Classification:	Unrestricted

Summary:

This report brings members up to date with a range of issues concerning the administration of the Kent Local Government Pension Scheme (LGPS).

Recommendations:

The Board is recommended to note the report

REPORT SUMMARY

i) Number of tasks completed in the 6 months to 30 September 2021 have returned to levels achieved prior to the pandemic.
ii) Key Performance Indicators in some areas have been severely impacted by the system problems experienced during the 6 months
iii) System problems stabilise
iv) Update on Annual Benefit Illustrations and reportable breach
v) Introduction of Member Self Service

1. WORKLOAD POSITION

Tasks completed in key areas in 6 months to 30 September 2021 and comparison with previous 4 years

	TOTAL	Retirement Benefit	Corres pondence	Estimate Retirement Benefit	Dependant Benefit	Deferred Benefit	Divorce	Transfer/ Interfund In	Transfer/ Interfund Out
6 mths to 30/09/21	**10,070**	1290	3710	2480	230	1760	200	60	340
2020 -2021	**14,320**	2300	4540	3830	500	1750	320	310	770
2019 - 2020	**19,520**	2480	4280	3900	450	6680	350	490	890
2018 - 2019	**18,120**	2590	5790	3680	530	3910	400	430	790
2017 - 2018	**14,290**	2010	5340	3030	580	1720	330	420	860

Numbers rounded to the nearest 10 for clarity

1.1 As at 30 September 2021 the total number of tasks completed was 10,070. If workloads continue at the same level for the remainder of 2021/22 then the total number of tasks completed during the year will exceed those completed in 2020/21 and will be on a par with 2019/20. The reason for the fall in the number of cases completed in 2020/21 was mainly due to staff being unable to work for periods during that year due to the lack of IT equipment.

1.2 During the 6 months to 30 September 2021 there has been a marked increase in the amount of correspondence and requests for estimates of retirement benefits. This could be due to scheme members considering lifestyle changes following the pandemic. The number of deferred benefits completed has already exceeded the amount completed in the previous year. This is mainly due to the assistance we are receiving from ITM limited with dealing with this category of work.

1.3 The number of transfers of pension rights both into and out of the scheme have fallen as these categories of work were not prioritised at the start of the pandemic however a project has now commenced to deal with these cases.

2 ACHIEVEMENTS AGAINST KEY PERFORMANCE INDICATORS (KPIs)

KPIs in key areas in 6 months to 30 September 2021 and comparison with previous 4 years

	Calculation and payment of retirement benefit	Response to correspondence	Calculation of retirement benefit estimate	Calculation and payment of dependant benefit
KPI	20 days	15 days	20 days	15 days
6 mths to 30/09/21	59%	98%	77%	17%
2020/2021	93%	99%	58%	100%
2019/2020	97%	100%	90%	93%
2018/2019	96%	100%	72%	97%
2017/2018	98%	99%	72%	99%

NB. All target turnaround times commence when we have all the necessary documentation to complete the particular task. Requirement to complete 95% of the recorded KPI tasks, within the agreed target turnaround times

2.2 The table of our performance against our target key performance indicators, especially with regard to retirement benefits and dependant benefits, reflects the problems we have experienced during the 6 months to 30 September with connectivity to our hosted pension administration service. Members will recall that I have reported over several meetings the problems that staff were experiencing culminating in a 10 day period in August when productivity slowed considerably. Although these system issues have eased and stabilised at this time we are still suffering the consequences of these earlier disruptions when completing these areas of work within the KPI timeframe.

3 SYSTEM AND CONNECTIVITY PROBLEMS

3.1 Members will recall at the last meeting that I detailed the problems that staff had been experiencing with regard to the slowness of connection to the hosted service.

3.2 Since that time certain staff have been piloting different ways of connecting to the service with the aid of KCC's IT department and Aquila Heywood. The results show that 2 of the 3 methods being trialled are providing the best results with the added advantage that it would appear using these methods means that pension administration staff will be able to access the service from any area in a KCC building rather than being restricted to especially configured areas.

3.3 A decision with regard to the preferred method of connecting will be decided shortly with the agreement of KCC's IT department with all staff moving to this method after this.

4 ANNUAL BENEFIT ILLUSTRATIONS

4.1 Members will recall that at the last meeting I detailed that as the administrating authority we had not been able to fulfil our statutory responsibility to provide the non uniformed staff, approximately 3,100 scheme members, employed by Kent Police and the Police and Crime Commissioner, with Annual Benefit Illustrations by the 31 August. The reason that we were unable to provide the Illustrations was that we had not received the data required from Kent Police despite providing extended deadlines for the receipt of this data.

4.2. It was decided by members at the last Pension Board meeting, and agreed at the subsequent Superannuation Committee meeting, that this was a material breach of the pension scheme regulations and as such should be reported to the Pensions Regulator. This breach has now been reported.

4.3. Following the meetings dialogue continued with Kent Police to resolve outstanding issues with regard to the data that was provided and to provide a timetable for the receipt of this data in order that arrangements could be made with our printers to provide Illustrations. Provided all queries are resolved Illustrations will be provided before the Christmas break.

4.4. Letters were sent to both the Chief Constable and the Police and Crime Commissioner explaining the situation and asking them to respond to questions raised by the Board and Committee with regard to what circumstances had caused the data not to be submitted in a timely fashion in 2021 and the steps that would be put in place to ensure that the situation did not occur again.

4.5. A response was received on 17 November from the Chief Constable, and on behalf of the Police and Crime Commissioner, explaining the seriousness that they accorded this matter, that they took their pension responsibilities seriously and had examined the circumstances with a view to having a clear understanding of the cause of the circumstances surrounding this event and putting sustainable measures in place to prevent a recurrence.

4.6. A formal proposal is being developed to strengthen the resilience of the management team in the Kent Police Payroll & Pensions team and this is intended to address these circumstances and Kent Police's assessment of the additional work associated with successive legal cases and judgements affecting the administration of pensions.

5 MEMBER SELF SERVICE

5.1 Member Self Service (MSS) is an online secure facility for scheme members to access their individual pension account where they are able to see the current value of their pension and using pension projectors can model different potential scenarios to see what pension savings they could receive at retirement.

5.2 They can also use MSS to go online to inform us of a change of address or a change to their wishes with regard to any death grant that may become payable.

5.3 Details of how to register for MSS were provided in the deferred benefit updates provided earlier in the year and in the Annual Benefit Illustrations provided at the end of August.

5.4 Currently 786 scheme members have registered to use the service, made up of 425 current members and 361 deferred members. Although this number may appear disappointing a deliberate decision was made to start slowly in order to gauge the impact on team members in resolving registration problems etc however this has proved to be manageable and so in future more prominence will be given to this new service both on our website and in future communications.

5.5 MSS is not currently available to pensioner members but we are looking to introduce this in the future with these members being able to view their payslips and P60s online.

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November 2021

From:	Chairman Superannuation Fund Committee Corporate Director of Finance
To:	Superannuation Fund Committee – 1 December 2021
Subject:	ACCESS update
Classification:	Unrestricted

Summary:

This update provides a summary of the activities of the ACCESS pool

Recommendation:

The Superannuation Fund Committee is recommended to note this report

FOR INFORMATION

1. Introduction

1.1 This report is to update the Committee on the work being undertaken by the ACCESS pool.

2. Joint Committee

2.1 The Joint Committee (JC) last met on 6 September and a copy of the notes of the meeting are at appendix 1. Copies of the agenda and unrestricted papers for the 6 September meeting are available at: ACCESS Joint Committee 6 September 2021

2.2 At their meeting the incumbent chairperson, Cllr Mark Kemp-Gee (Hampshire), and vice chairperson, Cllr Susan Barker (Essex), were unanimously re-elected.

2.3 On 6 September the Joint Committee noted the updated business plan which anticipates progress on the following issues:

- Communications
- Responsible Investment
- Implementation Adviser appointment
- BAU evaluation next steps
- Sub-fund performance and implementation
- Contract Management

2.4 The Committee also noted progress on ACCESS costs and a forecast underspend against the budget for 2021-22 of £155k, (£14k per authority) was reported. The underspend reflects savings on staff costs due to the delayed recruitment of additional ASU staff, reduced charges from Essex County Council who act as host authority for ACCESS, and lower than anticipated strategic and legal fees.

3. Recent Activity

3.1 As at 30 September 2021 the Kent Fund had invested in 5 sub-funds in the ACCESS authorised contractual scheme (ACS) operated by Link Financial Solutions, with a combined value of £3.97bn.

3.2 Since the last report to the Board the Officer Working Group (OWG) as well as other working groups with Kent being represented on each group, have continued to meet on a periodic basis. Progress continues to be made on the set up of new sub-funds as well as on the establishment of suitable platforms for pooling non listed assets.

3.3 The Link Investor Day took place on 30 November 2021. Where members were not able to attend, they can request a copy of the recording of each session.

4. Internal audit review

4.1 Governance and Audit Committee at their meeting on 30 November 2021 received a summary of the completed audit review of the governance arrangements for the Fund's investments in the ACCESS pool. A copy of the summary is at appendix 2. The Audit opinion was substantial with very good prospects for improvement.

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November 2021

SUMMARY UPDATE (Part I)
ACCESS Joint Committee (JC):
6 September 2021

Nine ACCESS Authorities were represented. The key matters considered are described below.

Part I Item	Details
Election of Chairman	Cllr Mark Kemp-Gee (Hampshire), incumbent, was unanimously re-elected as Chair of the Joint Committee for a period of two years.
Election of Vice Chairman	Cllr Susan Barker (Essex), incumbent, was unanimously re-elected as Vice Chair of the Joint Committee for a period of two years.
Chairman's remarks	Cllr Kemp-Gee welcomed all Members to the first "in person" meeting of the Joint Committee since March 2020. He extended a particular welcome to Cllr Williams (Northants) to his first Joint Committee.
Minutes of meeting 8 March 2021	Minutes of the Joint Committee meeting of 8 March 2021 were agreed, pending the update to page 5 (sub-fund implementation) item 256, where wording would be amended to read: *"It was noted that the Section 151 Officers of all member Authorities had received a copy of the emerging markets report."*
Business plan, forecast outturn and risk summary	The Committee received an update on the 2020/21 Business Plan and outturn, the 2021/22 budget update, and the risk register. Particular attention was drawn to the planned briefing, to be led by ESG / RI advisers Minerva on the update of the draft ACCESS ESG / RI Guidelines. This event is expected to take place in October. It was highlighted that the 2020/21 outturn had been noted at informal virtual briefing for Elected Members in June and would be brought to the next formal Joint Committee in December. **The Committee:** • **noted the updates in respect of the 2020/21 business plan.**
Communications and Spokespeople	The Committee received an update on the progress of training for ACCESS Elected Member spokespeople which noted that the ASU Director will remain the spokesperson "in the first instance", with Cllr Fox (East Sussex) the spokesperson for responsible investment, Cllr Oliver (Norfolk) covering governance, Cllr Soons (Suffolk) covering media strategy, and Cllr Kemp-Gee (Chair, Hampshire) and Cllr Barker (Vice Chair, Essex) covering political, governmental relations, parliamentary, inter-pool and overall strategy.

	The Committee: • **noted the report, agreed to the proposed Elected Member spokespeople shown above, and noted the associated training arrangements in progress.**
Part II Item	Details
Implementation Adviser procurement	The Committee received a report on the outcome of the process for the procurement of the Implementation Adviser. The process and outcome were discussed and the arrangements for notifications to bidders and standstill period were highlighted. **The Committee:** • **noted the matters highlighted in the report;** • **endorsed the outcome of the procurement exercise; and** • **noted that ECC, as Procurement Lead Authority, will enter into a contract with the winning bidder on behalf of the Councils.**
Sub-fund implementation	The Committee received a report outlining progress on sub-fund implementation and discussion included specific sub-funds that had been anticipated for September launch. **The Committee:** • **noted the report.**
Scheduled Business as Usual (BAU) evaluation	The Committee received a report presentation from Hymans Robertson recapping on the Scheduled BAU evaluation work undertaken during 2020/21 and detailing the background to a series of recommended actions, which had been considered and endorsed by all administering authority s151 Officers and the OWG. **The Committee:** • **noted the presentation from Hymans Robertson; and** • **agreed, by unanimous vote, the report's recommendations;** • **requested a detailed timetable for progressing the approved recommendations.**
Investment Performance, MHCLG return and Annual Report	The Committee noted the Investment Performance report as at 30 June 2021. The total pooled assets of all ACCESS Authorities was £32.602bn on that date having been £31.510bn on 31 March 2021. No sub-fund lunches had taken place within the quarter. An overview was included on the collaborative work with other pools on updates to the annual MHCLG report template. As a consequence, this annual return would be submitted later in September. The Committee received printed copies of the draft Annual Report highlighting key milestones from 2020/21. This enabled each Authority to include a common narrative on pool activity with individual Fund's Annual Report & Accounts publications. A presentational change to the layout of the final table

	was highlighted and agreed. **The Committee:** • **noted the performance report;** • **noted progress with the annual MHCLG return; and** • **recommended the Annual Report for publication by each ACCESS Authority.**
Review of Emerging Markets process	The Committee received a report on the review of the Emerging Markets process. The recommendations outlined potential developments regarding updating sub-fund establishment arrangements and amending relevant governance processes. **The Committee:** • **agreed the seven recommendations of the Emerging Markets review as set out in the Executive Summary.**
Response to the Emerging Markets Review	The Committee received a report outlining the initial response to the recommendations within the Emerging Markets review. **The Committee:** • **noted the report.**
Contract and Supplier Relationship Management	The JC received the regular report covering a number of aspects of Contract and Supplier Relationship management. **The Committee:** • **noted the report.**
Risk Management	The Committee received a report on the Pool's Risk Register. This highlighted that, following approval s151 Officers at their meeting in June 2021, the assessment of risks had moved from a '3x3' matrix to a '4x4' matrix style including dashboard reporting. It was highlighted that the scores for each risk were unchanged to those circulated at the June Elected Member briefing. **The Committee:** • **noted the report.**
Next meeting date	6 December 2021

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Appendix D – Summaries of Completed Audit Reviews

D2 – CS08-2021 – Access Pool

Audit Opinion	**Substantial**
Prospects for Improvement	**Very Good**

Internal Audit concluded that there are strong governance arrangements to monitor and manage pooled investments in line with the Kent Pension Fund Investment Strategy, and effective performance monitoring and reporting mechanisms are in place. The expected benefits and savings from participation in the Access Pool are being realised and effectively reported to stakeholders. Income is being distributed in a timely manner and in line with the agreed arrangements, and effective risk management arrangements are well embedded.

Several key strengths have been identified below. No significant weaknesses were identified.

Two low risk issues have been identified in relation to scoring on the Fund Risk Register and Superannuation Fund Committee risk appetite training. It is recognised that these issues do overlap with a previous internal audit review on Pension Fund Investment Governance, which was issued in December 2019. The issues from this previous review are still under follow up review.

Key Strengths

- The governance arrangements for pooled investments are adequate and in line with the Kent Business Fund Investment Strategy, and appropriate delegations of authority are in place.
- Governance and exit arrangements are appropriately accounted for in contract documents.
- Value for money has been considered prior to investing in ACCESS Pool, and there is a controlled implementation and review method for launching pooled funds to ensure these investments are the best course of action for the Fund.
- Meetings of the ACCESS Joint Committee and Officer Working Group took place as required throughout 2020, with appropriate Council representation.
- There are appropriate information sharing mechanisms between ACCESS Pool and the Fund's representatives, which were applied in practice.
- Appropriate performance monitoring information is submitted and reviewed by the members of the ACCESS Joint Committee and S151 Group.
- The designated ACCESS Support Unit Technical Leads and Contract Manager compile performance reports for the Joint Committee as required.
- Details of savings realised from pooled arrangements are reported to the Superannuation Fund Committee.
- Internal Audit is satisfied that the savings projections for the year were reasonable and appropriate and accurately reported in the Fund's 2019 and 2020 Annual Reports.
  The Fund's net fee savings during 2019/2020 were £1.596m, with a cumulative net saving of £4.024m since the beginning of the pooling project, as reported in their 2020 Annual Report.
- There are controls in place for the management of the Fund's risks.
- Sensible arrangements are in place to govern the distribution of the Fund's income from pooled investments.

Areas for Development

- Scoring within the Fund's Risk Register could be improved.
- Risk appetite training for Superannuation Fund Committee members is not yet captured in the Fund's Training & Development Plan for 2021/22.

Prospects for Improvement

Our overall opinion of **Very Good** for Prospects for Improvement is based on the following factors:

- Internal Audit is satisfied that the management actions provided address our findings in full.

Summary of Management Responses

	No. of Issues Raised	Mgt Action Plan Developed	Risk Accepted and No Action Proposed
High Risk	0	N/A	N/A
Med Risk	0	N/A	N/A
Low Risk	2	2	0

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From:	Chairman Superannuation Fund Committee Corporate Director of Finance
To:	Superannuation Fund Committee – 1 December 2021
Subject:	Fund Position
Classification:	Unrestricted

Summary:

To provide a summary of the Fund's asset allocation and performance.

Recommendation:

The Committee to note the Fund's asset allocation and performance as at 30 September 2021

FOR INFORMATION

1. Introduction

1.1 This report provides an update on the asset allocation and manager performance.

1.2 A copy of the Fund Position Statement is at appendix 1

2. Asset Allocation

2.1 As at 30 September 2021 the Fund's value was £7.85bn, an increase of £76m over the quarter and table 1 below compares the actual asset allocation to that set out in the Fund's Investment Strategy.

Table 1 asset allocation

Asset Class	Value £m	Actual %	Benchmark %	Over / (Under) weight %
UK Equity	1,473	18.8	23.5	-4.7
Global Equity	3,309	42.2	32	10.2
Fixed Income	1,157	14.7	15	-0.3
Private Equity	243	3.1	4	-0.9
Infrastructure	101	1.3	3.5	-2.2
Property	827	10.5	13	-2.5
Absolute Return	548	7.0	8	-1.0
Cash	193	2.5	1	1.5
Total	**7,850**	**100**	**100**	

2.2 Whilst the synthetic equity has helped maintain the total equity exposure of the fund, the returns have been capped by the equity protection programme.

2.3 At the end of the quarter, the total equity allocation of the Fund (including the synthetic equity exposure as well as the value of the equity protection options) is 60.9%. which continues to remain overweight to its strategic allocation of 55.5%. However, for the purpose of the rebalancing decision the impact of the subsequent restructuring of the equity protection programme carried out in October, will have to be considered.

2.4 The Fund is underweight in all other asset classes other than cash managed internally which remains high at 2.5%.

2.5 The Fund has continued to hold cash in view of the uncertain market conditions. Drawdowns for private equity and infrastructure commitments have also been slower than anticipated.

3. Investment performance quarter to 30 September 2021

3.1 The quarter saw a continued moderation in the momentum of the post Covid economic recovery, and the Fund achieved a return for the quarter of 0.98% against a benchmark of 1.79%. These returns appear subdued compared to the stronger performances in the previous few quarters.

3.2 Whilst the initial recovery in 2021 was stronger than initially expected, the recovery is now entering a much tougher phase as policy support starts to be withdrawn, supply chain disruptions continue to escalate, and energy prices and inflation are surging. There has been a lot of debate whether the rise in inflation is transient or permanent. Fears of rate rises have driven up bond yields and at the same time hit equity valuations.

3.3 Performance from most of the Fund's active managers also fell short of benchmark returns, except for Sarasin, M&G and Impax managing global equity portfolios which have benefited from their cyclical and environmental exposures and CQS whose multi asset credit portfolio benefitted from short duration and floating rate exposures. The Schroders Bond portfolio suffered due to long duration and short USD exposures.

3.4 Property returns continued to improve with improvement in rent collections and an increase in the volume of property transactions, whilst the industry is waiting to see the result of the review of the landlord and tenant legislation. Property was the strongest performing asset class this quarter with the strongest performance recorded by the DTZ portfolio although all the Fund's property managers underperformed the benchmark.

3.5 Private equity continued to record a strong growth with double digit figures. The post Covid recovery period has seen an increased deal flow at attractive prices and good businesses have benefitted from the uplift in valuations with the economic recovery.

4. Longer term investment returns

4.1 The Fund has recorded (marginally) below benchmark returns in the 1year period due to its two biggest mandates (Baillie Gifford Global Equities and Schroders UK Equity) which constitute nearly 38% of the fund, underperforming their benchmarks. However, both these mandates and the Fund outperformed in the three-year period.

4.2 The Fund's one-year performance was 15.02% compared to the benchmark return of 16.0% for the same period.

4.3 The one-year performance mainly captured the post covid economic recovery which was reflected in the strong growth in equity markets and the low double digit uplift in property valuations. However, the tech stocks' valuations which peaked in the covid period have seen some unwinding in the latter half of the year. This has mainly affected the Baillie Gifford portfolio which still returned near benchmark returns.

4.4 All active managers in all asset classes have achieved better than benchmark returns in the one-year period except for Baillie Gifford, Schroders (UK Equity) and Pyrford (absolute return) besides M&G and Aegon for property. CQS and Ruffer (with their dynamic investment styles) and Schroders (value strategy) were the star performers in their respective asset classes during this period.

4.5 The Fund achieved an annualised return of 7.59% compared to 5.91% over the three-year period ending September 2021, with global listed equities driving the outperformance.

4.6 Fund manager performance has been mixed over the three-year period with Baillie Gifford achieving a return of 22.36%, more than double its benchmark annual return of 9.32%. Pyrford absolute return, M&G property, and Aegon property funds have been laggards throughout.

4.7 Private Equity returns have been strong during the last three years and had an exceptional rebound post covid. The 'building-up stage' of the bulk of our infrastructure fund investments managed by Partners Group has contributed to the slow movement in valuations in that portfolio.

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November 2021

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FUNDD POSITION STATEMENT

Summary of Fund Asset Allocation and Performance

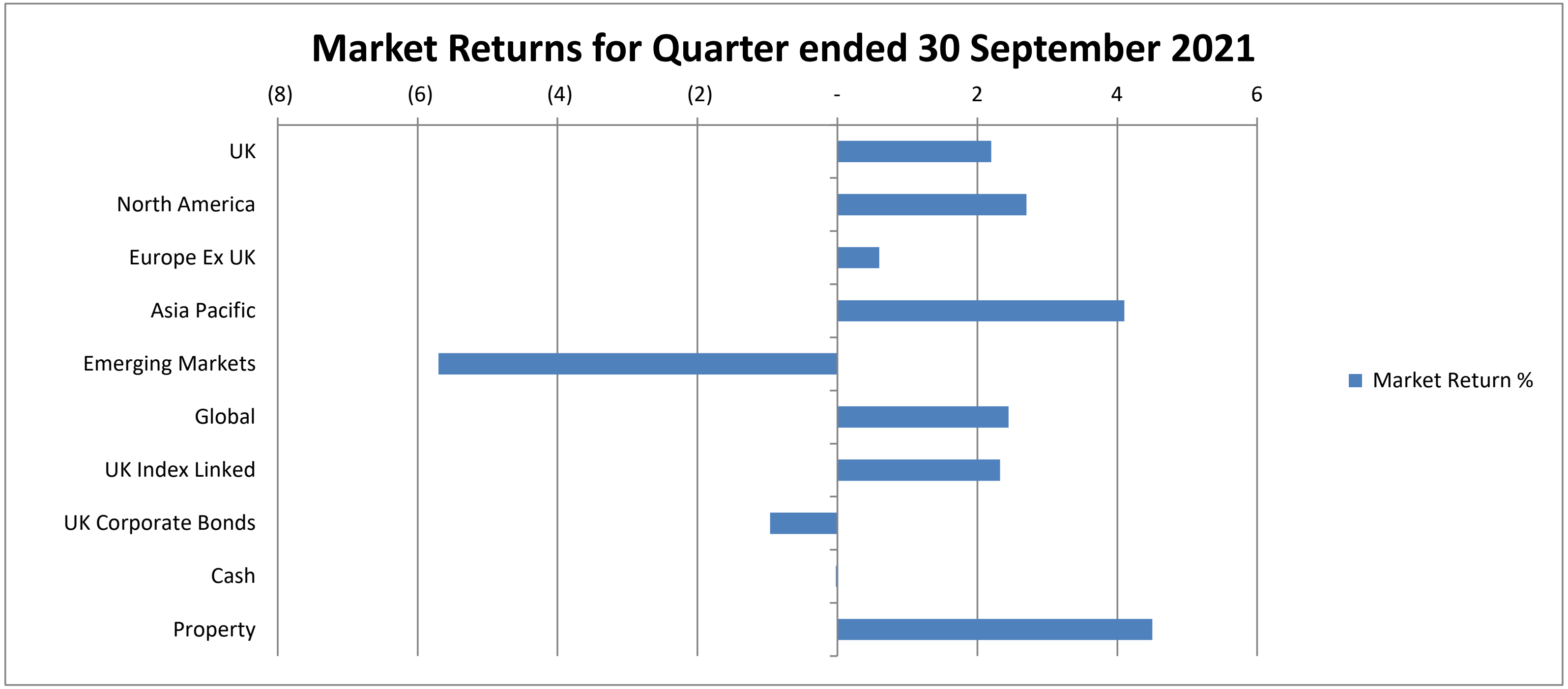
Superannuation Fund Committee

By: Chairman Superannuation Fund Committee
Corporate Director of Finance

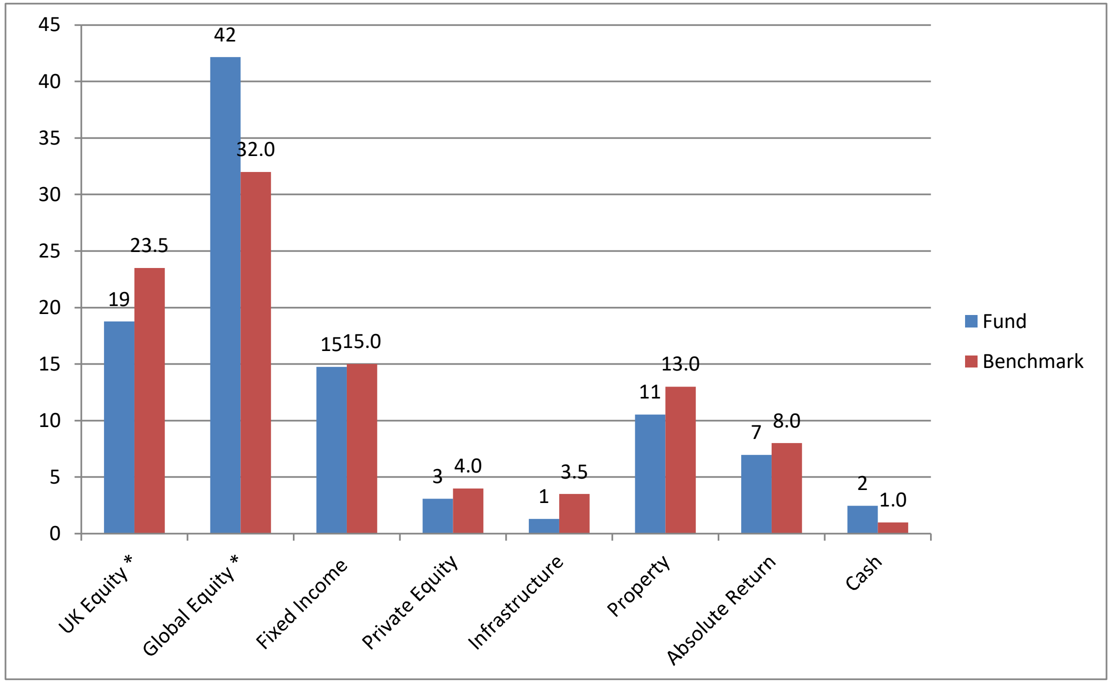
Kent County Council
Superannuation Fund Q2 2021-22

Alison Mings- Acting Business Partner -
Kent Pension Fund

Market Returns for Quarter ended 30 September 2021



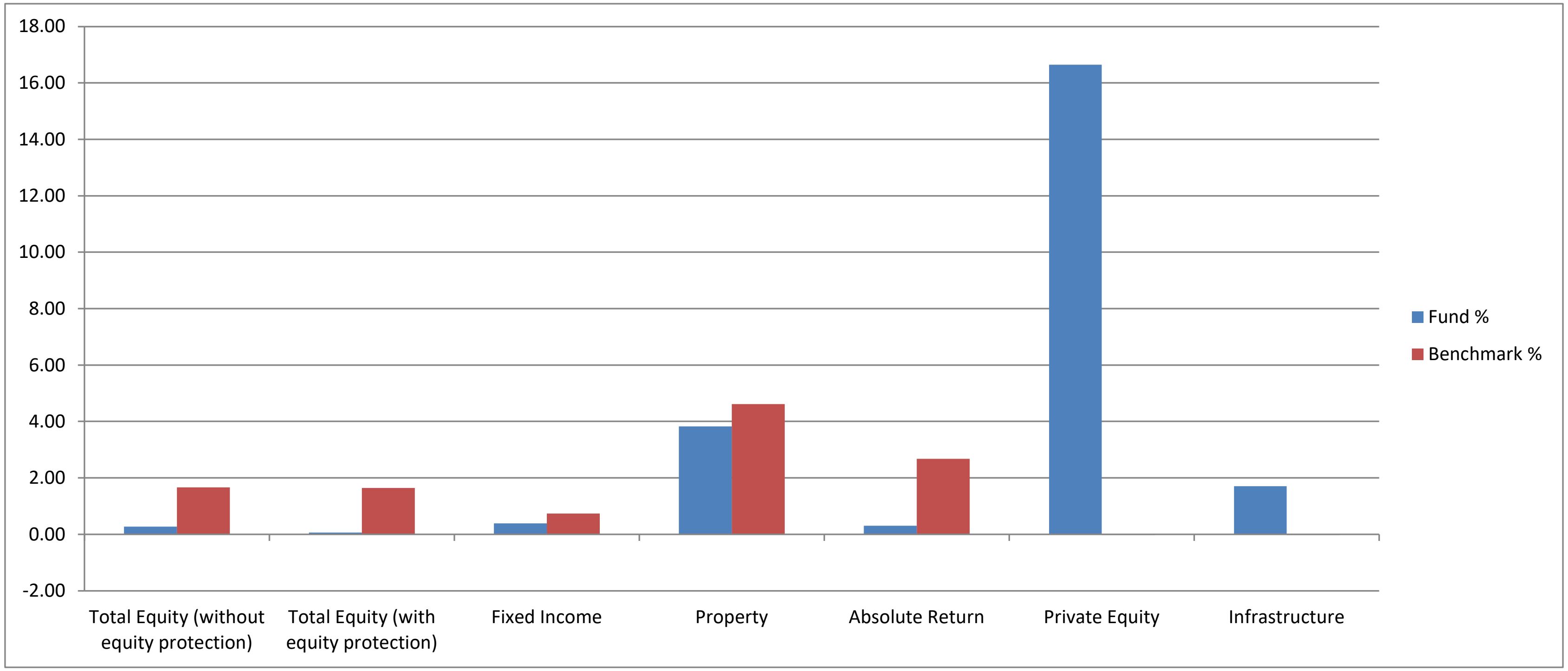
Fund Asset Allocation vs Benchmark as at 30 September 2021



	Fund		Benchmark	Over / (under) weight
Asset Class	**£m**	**%**	**%**	**%**
UK Equity *	1,473	18.8	23.5	-4.7
Global Equity *	3,309	42.2	32	10.2
Fixed Income	1,157	14.7	15	-0.3
Private Equity	243	3.1	4	-0.9
Infrastructure	101	1.3	3.5	-2.2
Property	827	10.5	13	-2.5
Absolute Return	548	7.0	8	-1.0
Cash	193	2.5	1	1.5
Total	7,850	100	100	

* Our synthetic equity exposure with Insight is included in UK and Global Equities

Fund Asset Class Performance for Quarter ending 30 September 2021



Asset Class	Fund %	Benchmark %	Outperformance %
Total Equity (without equity protection)	0.27	1.67	-1.40
Total Equity (with equity protection)	0.06	1.64	-1.58
Fixed Income	0.38	0.74	-0.36
Property	3.82	4.62	-0.79
Absolute Return	0.30	2.67	-2.37
Private Equity	16.64	-0.02	16.66
Infrastructure	1.70	-0.02	1.72

Market Value Summary by Fund Manager as at 30 September 2021

Fund Manager	Asset Class	Market Value as at 30 June 2021 (£m)	Market Value as at 30 September 2021 (£m)	Change in Market Value (£m)	% of Total Fund 30 September 2021
Baillie Gifford - LF ACCESS Global Equity Core Fund	Global Equity	1,870	1,842	-27	23.5%
Schroders - LF ACCESS UK Equity Fund	UK Equity	1,079	1,092	13	13.9%
Insight	Equity Protection Program	532	524	-9	6.7%
DTZ	Direct Property	507	524	17	6.7%
M&G - LF ACCESS Global Dividend Fund	Global Equity	466	480	14	6.1%
Goldman Sachs	Fixed Interest	422	423	2	5.4%
Sarasin	Global Equity	370	379	10	4.8%
Schroders GAV - LF ACCESS Global Active Value Fund	Global Equity	377	376	-1	4.8%
Pyrford	Absolute Return	365	366	1	4.7%
Schroders	Fixed Interest	253	253	-1	3.2%
M&G Alpha Opportunities	Fixed Interest	240	241	1	3.1%
CQS	Fixed Interest	238	240	3	3.1%
Harbourvest	Private Equity	167	195	28	2.5%
Ruffer - LF ACCESS Absolute Return Fund	Absolute Return	181	182	1	2.3%
Fidelity	Pooled Property	144	149	6	1.9%
Partners	Infrastructure	93	101	9	1.3%
Impax Environmental Markets	Global Equity	76	79	3	1.0%
M&G Residential Property	Pooled Property	65	66	1	0.8%
YFM	Private Equity	42	48	6	0.6%
Aegon (Kames)	Pooled Property	44	44	1	0.6%
DTZ Pooled Funds	Pooled Property	43	43	0	0.5%
Woodford	UK Equity	9	8	0	0.1%
Internally managed cash	Cash	193	193	0	2.5%
Total Kent Fund		**7,774**	**7,850**	**77**	**100.0%**

Total investments in ACCESS pooled funds		**3,675**	**3,973**
Percentage of the total Fund		**47%**	**51%**

Performance Returns as at 30 September 2021

	Quarter		1 Year		3 Year (p.a.)	
	Fund	Benchmark	Fund	Benchmark	Fund	Benchmark
Total Fund *	0.98	1.79	15.02	16.00	7.59	5.91
UK Equity						
Schroders - LF ACCESS UK Equity Fund	1.18	2.26	25.32	27.53	4.03	2.28
Woodford	-5.72	2.23	-34.88	27.89	-30.34	3.08
Global Equity						
Baillie Gifford - LF ACCESS Global Equity Core Fund	-1.46	1.54	20.93	21.52	22.36	9.32
Sarasin	2.60	1.37	23.97	22.19	13.10	11.33
Schroders - LF ACCESS Global Active Value Fund	-0.18	1.37	32.71	22.19	7.14	11.33
Impax	4.12	1.37	37.43	22.19	18.08	11.33
M&G - LF ACCESS Global Dividend Fund	3.10	1.37	30.48	22.19	11.71	11.33
Fixed Interest						
Goldman Sachs	0.38	0.86	3.71	3.50	4.37	3.50
Schroders Fixed Interest	-0.39	0.03	3.32	0.09	1.26	0.65
CQS	1.14	1.01	11.05	4.08	--	--
M&G Alpha Opportunities	0.46	1.01	7.59	4.08	--	--
Property						
DTZ	4.30	4.62	18.45	13.62	6.13	4.44
Fidelity	3.84	4.50	16.46	13.19	5.32	3.99
Aegon (Kames)	2.73	4.50	6.92	13.19	0.60	3.99
M&G Property	0.58	4.50	1.22	13.19	1.19	3.99
Private Equity						
Harbourvest	15.20	-0.02	53.94	-0.09	26.95	0.25
YFM	22.66	-0.02	63.83	-0.09	27.26	0.25
Infrastructure						
Partners	1.70	-0.02	-4.07	-0.09	-2.05	0.25
Absolute Return						
Pyrford	0.29	2.67	5.48	9.90	2.83	7.81
Ruffer - LF ACCESS Absolute Return Fund	0.33	2.67	16.01	9.90	8.63	--

* The total fund return includes the impact of the equity protection program, a separate report detailing the performance of the program is provided as a separate report

Fund Manager Benchmarks and Performance Targets

Asset Class / Manager	Performance Benchmark	Performance Target
UK Equities:		
Schroders - LF ACCESS UK Equity Fund	Customised	+1.5% pa over rolling 3 years
Woodford	FTSE All Share	Unconstrained
Global Equities:		
Baillie Gifford - LF ACCESS Global Equity Core Fund	Customised	+1.5% pa over rolling 3 years
Sarasin	MSCI AC World Index NDR	+2.5% over rolling 3 - 5 years
M&G - LF ACCESS Global Dividend Fund	MSCI AC World Index GDR	+3% pa
Schroders - LF ACCESS Global Active Value Fund	MSCI AC World Index NDR	+3% - 4% pa over rolling 3 years
Impax	MSCI AC World Index NDR	+2% pa over rolling 3 years
Fixed Income:		
Schroders Fixed Interest	3 months Sterling Libor	+4% pa over a full market cycle
Goldman Sachs	+3.5% Absolute	+6% Absolute
CQS	Libor + 4%	
M&G Alpha Opprtunities	Libor + 4%	
Property:		
DTZ	IPD Pension Fund Index	≥ 3 year rolling average of benchmark returns
Fidelity	IPD UK PF Property Fund Index	
Aegon (Kames)	IPD UK PF Property Fund Index	
M&G Property	IPD UK PF Property Fund Index	
Alternatives: (Cash / Other Assets)		
Private Equity – YFM	GBP 7 Day LIBID	
Private Equity – HarbourVest	GBP 7 Day LIBID	
Infrastructure – Partners Group	GBP 7 Day LIBID	
Absolute Return – Pyrford	Retail Price Index (RPI)	RPI + 5%
Ruffer - LF ACCESS Absolute Return Fund	Retail Price Index (RPI)	
Internally managed cash – KCC Treasury and Investments team	GBP 7 Day LIBID	

Fund Structure as at 30 September 2021

UK Equities	Global Equities	Fixed Interest	Property	Cash/Alternatives
Schroders +1.5% £1,092 m	Baillie Gifford +1.5% £1,842 m	Goldman Sachs +6.0% Abs. £423 m	DTZ Property £567 m	Internally managed Cash £193 m
Woodford £8 m	M&G +3.0% £480 m	Schroders +4.0% £253 m	Fidelity Property £149 m	Partners Infrastructure £101 m
	Schroders +3.0% - +4% £376 m	CQS £240 m	Aegon(Kames) Property £44 m	YFM Private Equity £48 m
	Impax +2.0% £79 m	M&G Alpha Opps £241 m	M&G Property £66 m	HarbourVest Private Equity £195 m
	Sarasin +2.5% £379 m			Pyrford Abs. Return RPI + 5% £366 m
	Insight Equity Protection £524 m			Ruffer Abs. Return RPI £182 m

Total Fund £7.9 bn

ACCESS fund

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