OXFORDSHIRE COUNTY COUNCIL

Pension Fund Committee
Friday, 7 June 2019

ADDENDA

5. Minutes

The Committee is **RECOMMENDED** to approve the minutes of the meeting held on 8 March 2019 (**PF3**) subject to the following amendment:

Minute 12/19 – page 6, sentence 2 to read 'Over the quarter, assets had depreciated by £190m, ***a drop of over 7%*** to £2.3m' (amendment in bold italics).

and to receive information arising from them.

10. Review of the Annual Business Plan 2019-20

Paragraph 17, line 3 of the report to be amended from:

'…which show the total greenhouse has emissions for the portfolio relative to annual turnover' to:

'…which show the total greenhouse ***gas*** emissions for the portfolio relative to annual turnover' (amendment in bold italics)

12. Administration Report

As covered in paragraph 31 of the report PF12 and recommendation (c), please see attached draft response to the consultation on 'Changes to the Valuation Cycle and Management of Employer Risk.'

13. Annual Review of Pension Fund Policies

Page 123 – Investment Strategy Statement – Asset Allocation

In the table on page 23, the secured income line was missed, which also requires a correction to the Total Assets Line:

Asset Class	Target Allocation (%)	Range (%)
Secured Income	5	4 – 6
Total Other Assets	30	24 – 36

The date in the 4th paragraph for the final transition should be August 2021

Following discussion at the pre-meeting with the Chairman, Deputy - Chairman and Opposition Spokesperson Officers were asked to draft an amended recommendation (b) in respect of the Investment Strategy Statement. The revised recommendation is as follows:

(b***) approve the revised Investment Strategy Statement as set out in Annex 2, noting the changes as discussed in the report and***

(i) endorse the current approach and direction of travel as set out in the Addressing Climate Change Position Statement, including:

- ***the integration of consideration of environmental and social risks, as well as good governance and stewardship into all decision-making processes***
- ***contributing to a more sustainable and resilient financial system***
- ***ensuring all portfolios across all asset classes are carbon and climate aware***
- ***decarbonising the listed portfolios, and developing measurable objectives and targets***
- ***accessing positive climate impact investment opportunities. such as the 35% investment in renewable energy funds within the infrastructure portfolio***
- ***active engagement with the underlying companies through asset managers, engagement and voting specialists and collaborative forums with other investors***
- ***improving the transparency of reporting including carbon footprinting and fossil fuel exposure and the impacts of our engagements***

(ii) ask Officers to set up a Climate Change Workshop in the Autumn to discuss how to further develop the above approach and contribute to the Climate Change Policy being developed by Brunel, seeking participation from a wide range of stakeholders to ensure a balanced discussion; and

(iii) note the view of Brunel that in light of the above approach, they do not consider a top down approach to divestment to be an appropriate strategy for its clients.

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Oxfordshire Pension Fund
www.oxfordshire.gov.uk/pensions

OXFORDSHIRE COUNTY COUNCIL

Date: 7 June 2019
Our Ref: SJC
Your Ref:

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Sent by email to LGPensions@communities.gov.uk

Dear Sir/Madam

Local Government Pension Scheme:
Changes to the Local Valuation Cycle and the Management of Employer Risk

Thank you for the opportunity to comment on the above consultation document issued in May 2019. This response is on behalf of the Oxfordshire Pension Fund Committee acting in its role of Administering Authority and was agreed at their meeting on 7 June 2019. We have structured this response using the headings and questions contained in the consultation document.

<u>Changes to the local fund valuation cycle</u>

1. As the Government has brought the LGPS scheme valuation onto the same quadrennial cycle as the other public services, do you agree that LGPS fund valuations should also move from a triennial to a quadrennial valuation cycle?

   Yes – we agree it makes sense to ensure that the scheme and local valuations are undertaken on the same cycle to avoid any unnecessary additional work, and that decision are made on consistent data.

2. Are there any other risks or matters you think need to be considered, in addition to those identified above, before moving funds to a quadrennial cycle?

   We note the statement that the move to quadrennial cycles will deliver greater stability in employer contribution rates and reduce costs. We do not agree that this is necessarily so and refer to the further proposals in the document that introduce the potential for interim valuations for the whole fund or changes to individual employer contribution rates. These proposals recognise the risk of extending the period between valuation cycles, and therefore introduce the option for more frequent variations in employer contributions and therefore greater costs.

INVESTORS IN PEOPLE

3. Do you agree the local fund valuation should be carried out at the same date as the scheme valuation?

   Yes – for the reasons given in 1 above.

Transition to a new LGPS valuation cycle

4. Do you agree with our preferred approach to transition to a new LGPS valuation cycle?

   No – whilst in normal times we would accept that a rates and adjustment certificate for a three year period followed by a second certificate for a further two year period would provide greater continuity and potentially greater funding certainty than a five year cycle with the option for an interim valuation, we are currently facing major uncertainty in the face of the McCloud judgement and the pausing of the cost capping mechanism. At the present time there is no certainty as to whether the McCloud judgement will be upheld, and if so, the cost of any remedy put in place. As such, there can be no certainty over whether the cost cap will indeed be breached and whether scheme changes will be required. We therefore have no certainty over the impact of future judgements on individual employers, nor the timing of such judgements. In these circumstances, we believe a five year cycle with the option for an interim valuation to be timed in line with certainty over the McCloud judgement and the cost cap proposals is the better approach.

Ability to conduct an interim valuation of local funds

5. Do you agree that funds should have the power to carry out an interim valuation in addition to the normal valuation cycle?

   Yes – whilst we strongly believe that interim valuations should be exceptional given the long-term nature of the LGPS, we accept that there will be occasions where to not address a significant change between valuations could lead to much larger changes in contribution rates at the next formal valuation (e.g. the publication of the McCloud case and cost cap mechanism as referred to above).

6. Do you agree with the safeguards proposed?

   Yes - On the basis we believe that an interim valuation should be an exceptional event, we are happy with the levels of the proposed safeguards.

Review of Employer Contributions

7. Do you agree with the proposed changes to allow a more flexible review of employer contributions between valuations?

   Yes, although we have some concern about limiting the flexibility to certain groups of employers within the Funding Strategy Statement. One of our tax-raising employers recently out-sourced the majority of its staff. We would not want to be restricted from asking for a new employer contribution rate in these circumstances.

Guidance on setting a policy

8. Do you agree that Scheme Advisory Board guidance would be helpful and appropriate to provide some consistency of treatment for scheme employers between funds in using these new tools?

   Yes – given that a number of scheme employers now sit in more than one Fund, it would be useful to have guidance from the Scheme Advisory Board aimed at providing consistency of approach between Funds when dealing with the same circumstances and employers. We would not want the advice to be overly prescriptive, not overly detailed, but to set out in broad terms the exceptional circumstances when these new flexibilities should be considered.

9. Are there other or additional areas on which guidance would be needed? Who do you think is best placed to offer that guidance?

   We have not identified any further areas at this time.

Flexibility in recovering exit payments

10. Do you agree that funds should have the flexibility to spread repayments made on a full buy-out basis and do you consider that further protections are required?

    We agree that it is appropriate to amend the Regulations to introduce greater flexibility into the cessation arrangements. Oxfordshire Pension Fund like many others has sought to deliver a number of the objectives of this section of the consultation through side agreements and would welcome the more formal legal footing of having the flexibility set out within the Regulations.

    We do not believe though that it would be helpful for the Regulations to be over prescriptive and believe that the individual Funds working with their Actuary and independent advisers should have the freedom to determine the period over which any deficit can be repaid, taking into account the size of the deficit and the financial strength of the individual scheme employer. We also note that the current Regulations do not prescribe that any exit deficit should be calculated on a full buy-out basis and believe that the Regulations should not be changed to prescribe this, but to leave the current position unchanged, where the actuarial assumptions are at the discretion of the Fund and their Actuary.

    We believe the current Regulatory requirements on the Fund and the Actuary provide sufficient protections to ensure that decisions taken are in the interest of the Fund and all scheme employers as a whole.

Deferred employer status and deferred employer debt arrangements

11. Do you agree with the introduction of deferred employer status into LGPS?

    Yes – as noted above, the Oxfordshire Pension fund has sought to deliver a similar model through side agreements and would welcome the more formal legal footing provided by having the arrangements allowed through the Regulations

12. Do you agree with the approach to deferred debt arrangements set out above? Are there ways in which it could be improved for the LGPS?

    Yes – we believe that the Regulations should provide a Framework and that the Funds are required to set out the relevant events which would trigger the ending of deferred employer status within their Funding Strategy Statement. The relevant events set out in the paper reflect those current set out in our side arrangements, though we normally specify any change in financial rating as a relevant event in respect of the assessment of the financial covenant of the employer (e.g. ratings by one of the major agencies such as Moody's or Fitch, or a national body such as the Annual Financial Assessment carried out by the Social Housing Pension Scheme). Our current arrangements require a review of the current arrangements following a relevant event, but do not create the automatic termination. This would be subject to the discretion of the Fund having reviewed the impact of the relevant event. For example, within one of our current arrangements, a Housing Association merged with another body creating a relevant event. On review though, it was determined that the merger strengthened the financial covenant of the employer, so the arrangement was allowed to continue, with the relevant changes to the legal documents to reflect the new employer's legal status.

    We also allow as a relevant event the option for the scheme employer to terminate the agreement by payment of the full low risk cessation valuation.

13. Do you agree with the above approach to what matters are most appropriate for regulation, which for statutory guidance and which for fund discretion?

    As noted above, we believe that the Regulations should apply the general framework which sets up the facility to define an employer as a deferred employer, and requires each Fund to set out within their Funding Strategy Statement the relevant events which would trigger a review of the current arrangements (as noted above, we do not believe a relevant event should trigger an automatic termination of the arrangements, but allow the Fund to terminate the arrangements on review of the impact of the change). We would welcome guidance on these matters but believe that this should come from the Scheme Advisory Board with final discretion on the operation of the arrangements with the Funds.

<u>Summary of options for management of employer exits</u>

14. Do you agree options 2 and 3 should be available as an alternative to current rules on exit payments?

    Yes – as set out in our responses above.

15. Do you consider that statutory or Scheme Advisory Board guidance will be needed and which type of guidance would be appropriate for which aspects of these proposals?

    As noted in the consultation document, a number of Funds, including Oxfordshire, have been operating equivalent arrangements to those now proposed through side agreements put in place with exiting employers. Whilst we welcome the legal clarity that the change in Regulations will bring to these practices, we would not wish to see detailed prescriptive guidance on these matters which would cut across our current arrangements. We would therefore wish to see the guidance restrict to the issues that should be considered, with discretion at Fund level as to how they apply the new flexibilities taking into account the profile of their employers, levels of deficit etc.

Exit credits and pass-through

16. Do you agree that we should amend the LGPS Regulations 2013 tp provide that administering authorities must take into account a scheme employer's exposure to risk in calculating the value of an exit credit?

    Yes – we fully support the principle that the calculation of an exit credit should be consistent with any risk sharing arrangements put in place with a scheme employer and which are taken into account when determining the value of a cessation payment.

17. Are there other factors which should be taken into account in considering a solution?

    The main advantage we see in the introduction of the new flexibilities around the payment of a cessation valuation are that it ensures the payment is more in line with the actual cost of the pension benefits payable in respect of the scheme employers former scheme members, than any figure calculated by reference to a range of future financial assumptions. It would be useful to explore whether similar flexibilities can be introduced in respect of exit credits to ensure that the remaining scheme employers are not disadvantaged where an exit credit is over generous as the assumptions used in any exit credit overestimated financial returns or underestimated the length pension benefits would be in payment. Similarly, if flexibilities can be identified, this would help ensure that exiting employers received a fair share of any surplus within the Fund following payment of outstanding liabilities.

Further education corporations, sixth form college corporations and higher education corporations

18. Do you agree with our proposed approach?

    We have real concerns about the proposed approach in terms of the implications for the cash flow of our Fund, our future investment strategies and the precedent that such an approach sets. We do though understand the reasoning behind the proposed approach, and the fact that scheme employers are currently exploring various options normally associated with outsourcing significant groups of staff to reduce the long-term costs of their current LGPS membership. We believe that the current problems stem from the failure of the last fundamental review of the LGPS to deliver an affordable and sustainable scheme, and in the absence of future changes to address this point, we accept that the proposed approach provides a more manageable solution to the issues faced by the impacted sectors.

    Going forward though, if the HE and FE scheme employers within the Oxfordshire Fund take advantage of the proposed changes to remove the option for new non-teaching staff to join the LGPS, we will see a more rapid move to become cash negative, which in turn will require a significant review of our investment strategy to ensure we have sufficient liquid resources to pay pension liabilities as they fall due. Where this means a switch from long term growth generating assets to lower risk more liquid assets, we may well see calls for the development of separate investment strategies to ensure the remaining scheme employers are not impacted by the overall reduction in investment returns.

    A key element of the introduction of such a proposal will therefore be clear communications between the Fund and their Actuary and the HE/FE employers to ensure they understand the significant impact that any decision to remove future staff members from the LGPS will have on their current employer contribution rates, and their short-term financial position. The proposed flexibilities in respect of cessation payments will be helpful in managing these issues.

If the proposed changes are accepted, we would be concerned as to other groups of scheme employers within the LGPS would seek similar arrangements, specifically academy schools. If a similar approach was to be agreed for the academy schools we would see a serious threat to the long term sustainability of the LGPS.

Public Sector Equality Duty

19. Are you aware of any other equalities impacts or of any particular groups with protected characteristics who would be disadvantaged by the proposals contained in this consultation?

    In the same way as the proposal would have the potential to introduce equality issues between current and new staff within the impacted sectors, the proposal has the potential to introduce equality issues between non-teaching staff working within 6th form provision in academy and maintained schools and those providing 16-18 year old provision in the Sixth Form College Corporations and FE Colleges.

We hope you find these comments helpful in taking this consultation forward.

Yours sincerely

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On Behalf of the Oxfordshire Pension Fund Committee

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