

Notice of meeting and agenda

Pensions Committee

3.00pm, Monday 16 November 2015

West Lothian Room, Lothian Chambers, High Street, Edinburgh

This is a public meeting and members of the public are welcome to attend

Contact

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1. Order of business

- 1.1 Including any notices of motion and any other items of business submitted as urgent for consideration at the meeting.

2. Declaration of interests

- 2.1 Members of the Committee and members of the Pensions Board should declare any financial and non-financial interests they have in the items of business for consideration, identifying the relevant agenda item and the nature of their interest.

3. Deputations

- 3.1 If any.

4. Minute

- 4.1 Previous Minute 30 September 2015 – Submitted for approval as a correct record (circulated)

5. Reports

- 5.1 Funding Strategy – Employer Appeals – report by the Deputy Chief Executive (circulated)

6. Motions

- 6.1 If any

Carol Campbell

Head of Legal and Risk

Committee Members

Councillor Rankin (Convener), Councillor Child, Councillor Bill Cook, Councillor Orr and Councillor Rose, John Anzani and Richard Lamont.

Information about the Pensions Committee

The Pensions Committee consists of 5 Councillors and 2 external members and is appointed by the City of Edinburgh Council. The Pensions Committee usually meets every eight weeks.

Further information

If you have any questions about the agenda or meeting arrangements, please contact Gavin King, Committee Services, City of Edinburgh Council, City Chambers, High Street, Edinburgh EH1 1YJ, Tel 0131 529 4239, e-mail gavin.king@edinburgh.gov.uk.

A copy of the agenda and papers for this meeting will be available for inspection prior to the meeting at the main reception office, City Chambers, High Street, Edinburgh.

The agenda, minutes and public reports for this meeting and all the main Council committees can be viewed online by going to www.edinburgh.gov.uk/cpol.

Item 4.1 - Minutes

Pensions Committee

2.00pm, Wednesday 30 September 2015

Present

Councillor Rankin (Convener), John Anzani, Councillor Child, Richard Lamont, Councillor Orr and Councillor Rose

Pensions Board Members Present:

Jim Anderson, Simon Belfer, Thomas Carr-Pollock, Linda McDonald, John Rodgers, Rucelle Soutar and Graham Turnbull.

1. Declaration of Interests

Councillor Orr declared a general non-financial interest as a director (treasurer) of Friends of the Earth Scotland.

John Anzani declared a general non financial interest due to Midlothian Council being on the board of trustees of the National Mining Museum of Scotland with this seat currently held by his service manager.

2. Minutes

Decision

To approve the minute of the Pensions Committee of 24 June 2015 as a correct record.

3. Considerations and matters to be raised by the Pensions Board regarding any items on the agenda

Issues were raised on the following:

- Earlier date of circulation of papers preferred – the target for papers being circulated was ten days.
- Impact of transformation programme at the City of Edinburgh Council on the Fund and the Pensions Service – The Pensions Service was outwith the transformation programme and would not be affected by the service cuts. The implications of the programme on the Fund had been planned for and there pension strain costs for the employer would apply.

4. Referrals and recommendations from the Pensions Audit Sub-Committee

Councillor Rose advised the Committee of the discussion and decisions taken at the Pensions Audit Sub-Committee the previous day.

Decision

To note the update.

5. Agenda Planning

Details were provided of potential reports for future Pensions Committee and Pensions Audit Sub-Committee meetings in December 2015 and March 2016.

Decision

To note the agenda planning document.

(Reference – report by the Deputy Chief Executive, submitted.)

6. Audited Annual Report 2015 of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

Audit Scotland had undertaken its statutory audit of the Annual Report 2015 of the three pension funds administered by the City of Edinburgh Council. Only minor presentational changes have been made to the unaudited version. Approval was sought for the annual report and to refer it to the Council for information. The referral to the Council was considered best practice given the Council's statutory role as administering authority of the Lothian Pension Funds.

A representative from Audit Scotland was present for this item.

Decision

- 1) To approve the audited annual report for the year ended 31 March 2015 for the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund.
- 2) To refer the report to Council for information.

(Reference – report by the Deputy Chief Executive, submitted.)

7. Report by the External Auditor on the Annual Report 2015 of Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund

The External Auditor had presented their annual report on the 2014/15 audit of the Lothian Pension Fund, the Lothian Buses Pension Fund and the Scottish Homes Pension Fund.

A representative from Audit Scotland was present for this item.

Decision

- 1) To approve the Annual Report on the 2014/15 audit of the Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.
- 2) To refer the report to Council for information.

(Reference – report by the Deputy Chief Executive, submitted.)

8. Funding Strategy – Employer Appeals

Decision

To note that this item had been withdrawn.

(Reference – report by the Deputy Chief Executive, submitted.)

9. Employers Participating in Lothian Pension Fund

An update was provided on employers who were looking to join the fund, those employers leaving the fund and other matters affecting employers participating in the Fund.

Decision

To note the changes to the employers participating in Lothian Pension Fund.

(Reference – report by the Deputy Chief Executive, submitted.)

10. Pension Fund Governance

Approval was sought for the appointment of the chair of the Pensions Board, a replacement employer representative for the Audit Sub-Committee and the extension of the current Independent Professional Observer contract.

An update was also provided on the ongoing liability of the Pension Committee and the Pension Board members.

Decision

- 1) To note that Eric Adair would continue as Chair of the Pensions Board until March 2016 and that Simon Belfer would replace Eric Adair as the Board employer representative attending the Audit Sub-Committee.
- 2) To approve the continuation of the Independent Professional Observer's role and the extension of the contract for Sarah Smart for a further two years with the changes to the remit.
- 3) To note the update to the legal advice received regarding the personal liability of Committee and Board members.

(Reference – report by the Deputy Chief Executive, submitted.)

11. Service Plan Update

An update was provided on the progress against the 2015-18 Service Plan, performance indicators and the actions required to enable the Fund to meet its key objectives.

Due to its in-house investment expertise, the Fund had been approached to join a working group to develop a business plan for a pool of internally managed investments.

Decision

- 1) To note the progress of the Fund against the 2015-2018 Service Plan.
- 2) To note the Fund's involvement in a working group to develop a business plan for a pool of internally managed Local Government Pension Scheme investments.

(Reference – report by the Deputy Chief Executive, submitted.)

12. Overpayment of Pension

Approval was sought not to pursue recovery of an overpayment of pension, which arose on the death of a pensioner, amounting to £16,254.88.

An overview was also provided on how fraud was mitigated for those claiming a pension from abroad.

Decision

- 1) To not pursue recovery of an overpayment of pension of £16,254.88.
- 2) To provide the Committee and the Pensions Board with the details of the process used by Western Union to prevent fraud.

(Reference – report by the Deputy Chief Executive, submitted.)

13. Risk Management Summary

A summary was provided on the Lothian Pensions Fund's risk management procedures, including details on the operational risk register and quarterly risk overview.

Decision

To note the Quarterly Risk Overview.

(Reference – report by the Deputy Chief Executive, submitted.)

14. Employer Appeals against Funding Strategy, Actuarial Valuation 2014 - Determinations

Decision

To note that this item had been withdrawn.

(Reference – report by the Deputy Chief Executive, submitted.)

15. Employers Exiting Lothian Pension Fund

Decision

To note that this item had been withdrawn.

(Reference – report by the Deputy Chief Executive, submitted.)

Pensions Committee

3.00 p.m., Monday, 16 November 2015

Funding Strategy – Employer Appeals

Item number	5.1
Report number	
Executive/routine	
Wards	All

Executive summary

This report advises Pensions Committee of the key issues which have been raised by the appellants and provides responses to those matters arising. It recommends changes to the Funding Strategy Statement, in relation to funding of liabilities transferred from another employer within the Fund and the frequency of payment of past service deficits.

Links

Coalition pledges

Council outcomes

[CO26](#)

Single Outcome Agreement

Funding Strategy – Employer Appeals

Recommendations

That Committee should:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider;
- 1.2 Note this report;
- 1.3 Note that a further report by the Chief Operating Officer, Deputy Chief Executive, recording the determinations of the employer appeals against the Funding Strategy is provided at item B1;
- 1.4 Note that a further report by the Chief Operating Officer, Deputy Chief Executive, on those employers who propose to cease membership of Lothian Pension Fund is provided at item B2;
- 1.5 Note that the Fund has proposed amendments to the Funding Strategy Statement following the appeals process and has consulted with employers on the proposed changes;
- 1.6 Agree to amend the Funding Strategy Statement to provide that where an employer has been admitted to the Fund arising from the transfer of members of staff from another scheme employer and the ceding employer is in agreement, then funding, including cessation valuations, should be on the ongoing basis;
- 1.7 Agree to amend the Funding Strategy Statement to stipulate that employer contributions in respect of Past Service Deficit, which are expressed as a minimum fixed monetary sum, are payable on a monthly basis, that is one twelfth of the annual total;
- 1.8 Note that the basis of cessation valuations has been considered by the Scheme Advisory Board and agree that the Fund will take cognisance of any guidance in due course.

Context of employer appeals

- 2.1 Pensions Committee, at its meeting on 25 March 2015, considered a report by the Director of Corporate Governance, which proposed a revised Funding Strategy Statement for the 2014 Actuarial Valuation. A key change to the funding strategy was as follows:
- 2.2 “Overall the Fund adopts a long-term investment strategy, aiming to maximise the investment return within reasonable and considered risk parameters and hence minimise the cost to the employer. However employers (with the exception of Transferee Admitted Bodies) who are closed to new members and have less than 5 active members, or are expected to leave the Fund within two valuation periods (6 years), will be assumed to be invested in lower-risk investments i.e. index-linked government bonds. This aims to reduce the degree of short-term change in employer contribution rates in the period prior to the employer leaving the Fund and hence manage risks for both the individual employer and for the Fund as a whole.”
- 2.3 Whilst fully endorsing the proposed funding strategy as a prudent measure to protect the interests of Lothian Pension Fund and its employers, Pensions Committee also recognised that the lower-risk investment contribution strategy may have significant cashflow implications. Accordingly, the revised Funding Strategy Statement was approved with the addition of the following:

Appeal criteria

- 2.4 ‘If there are specific circumstances where an employer may assert that the lower-risk funding strategy would place its future existence in jeopardy and therefore a less prudent funding strategy should prove advantageous to Lothian Pension Fund and the employer, then an appeal may be submitted to Lothian Pension Fund no later than 15 months after the date of the actuarial valuation. An appeal should include an alternative funding proposal recognising the need for the employer to meet their pension liabilities. Any such appeal would be considered by the Director of Corporate Governance (now Chief Operating Officer, Deputy Chief Executive) in consultation with the Convenor of the Pensions Committee, Convenor of the Pensions Audit Sub-Committee and the Independent Professional Observer and the decision reported subsequently to the Pensions Committee. In order for any appeal to be upheld, support from any respective ‘aligned body’ or guarantor would be required, together with approval of the Fund’s Actuary. Should such appeal be successful, then a revised ‘Rates and adjustment certificate’ would be issued. Pending determination of any appeal, the actuarial valuation ‘rates and adjustment certificate would remain applicable’.
- 2.5 An update on the progress of the appeals was provided to Pensions Committee, at its meeting on 24 June 2015, in the report “Funding Strategy Employer Appeals and Cessations”.

Main report

- 3.1 Of the 27 employers affected by the change of funding approach, 14 submitted an appeal by the due date of 30 June 2015.
- 3.2 Of those 14 employers, 6 propose to close their membership of the Local Government Pension Scheme (LGPS) to future benefit accrual, as soon as is possible, and thereby exit the scheme. A formal cessation valuation would be calculated by the Fund Actuary at the relevant date(s). If an employer wishes to pay the cessation debt over a period longer than 5 years, this requires Pensions Committee approval.
- 3.3 Specific coverage of the appeal submissions is provided in separate reports to this meeting of the Pensions Committee. These are shown as “B Agenda” items in order to respect the confidentiality of the employer submissions and financial information.
- 3.4 This report advises of general issues which have been raised by the appellants and provides responses to those matters arising.

Principles for repayment of pension liabilities

- 3.5 At the outset, it may be considered helpful to summarise the key tenets held by the Fund for the repayment of liabilities:
 - a. Liability for pension benefit obligations is the responsibility of the employing organisation.
 - b. Affordability of pension contributions to the employer is a paramount concern for all parties.
 - c. Best interests of the “aligned body”, (i.e. that which will be liable for the pension liabilities if the employer is unable to pay), in mitigating the risk of employer default are served by the employer continuing to exist to meet pension obligations in full.
 - d. Suitable protections to the Fund and aligned body should be incorporated in any such repayment schedule, e.g. security over assets, future revenues and capital receipts.

Outcome of Appeals Process

- 3.6 The Deputy Chief Executive, has determined the outcome of the appeals in consultation with the Convenor of the Pensions Committee, Convenor of the Pensions Audit Sub-Committee and the Independent Professional Observer, this in accordance with the instruction by the Pensions Committee.
- 3.7 The financial position of some employers showed that the contribution rates as certified in the 2014 Actuarial Valuation were indeed unaffordable. The conclusion of the process is as follows:
- the future service rate on the gilts basis is considered to be the minimum contribution in order to ensure that the accrual of new benefits does not increase the deficit on the cessation basis.
 - in the event of active members leaving earlier than anticipated, the Fund should require employers to continue to pay the respective future service rate contributions to the Fund to reduce the deficit.
 - given the disputed interpretation of the clause in the admission agreement (see later) the Fund should look to update the admission agreements of the affected employers.
- 3.8 Financial analysis of the individual employers looking to remain in the Fund is provided in separate reports to this meeting of the Pensions Committee.

Employers Proposing to Exit the Fund

- 3.9 Financial analysis of the individual employers proposing to exit the Fund is provided in separate reports to this meeting analysis of the Pensions Committee. External advice has also been sought on these cases.
- 3.10 The majority of these employers have proposed payment of debt which is less than the deficit on a cessation basis. The proposals typically spread debt repayment over a 5 year period.
- 3.11 For the majority of employers, it is clear that payment of the estimated cessation deficit is unaffordable. In addition, recognition of the cessation deficit on the employer's balance sheet is likely to make the majority of the employers insolvent.
- 3.12 In conclusion, the review of these cases has highlighted that the interests of the Fund as a whole (and any aligned body) may be best served by:
- agreeing debt repayment at a level less than the cessation debt in order to avoid employer insolvency, with an appropriate agreement which allows the Fund to revisit the repayment of the remaining debt at a future date (i.e. the debt would be a contingent liability and hence not recognised on an employer's balance sheet);
 - allowing payment of cessation debt over longer terms rather than insisting on payment as a one-off payment or over shorter terms previously agreed;

- a debt repayment schedule in order to access a share of current cash reserves, rather than these being depleted by further losses;
- obtaining security over any employer assets and/or suitable guarantee where possible;
- seeking, where appropriate, suitable “anti-embarrassment” provisions in legal agreement covering future increase in employer asset values.

3.13 The financial analysis and proposed approach for each individual employer is provided elsewhere on the Committee’s agenda.

General issues raised by the appellants:

3.14 The remainder of this paper highlights general issues raised by employers:

- Interpretation of admission agreements;
- Admission to the Fund on the transfer of staff;
- Cessation valuations (including update on regulations).

Admission basis – wording of legal documentation

3.15 Under the Scheme regulations, the City of Edinburgh Council and predecessor authorities has, as administering authority been able to admit certain bodies to the Local Government Pension Scheme. This is done by way of a legal document, an ‘Admission Agreement’ which sets out the terms of the admission. Most of the Admission Agreements include the following clause: “The Admission Body shall pay to the Authority in respect of each person admitted in the benefits of the Fund in accordance with the terms of this Agreement and for so long as such person remains an eligible employee such monthly sum representing the relevant monthly pension contributions of the person concerned and the Admission Body as would have been paid in to the Fund by the Authority and that person had he been in the direct service of the Authority, adjusted by any increase or reduction which may be certified by the Fund’s Actuary.”

3.16 Some appellants have stated they have received legal advice that the ‘purpose and intention’ of this clause was to place each admission body on an equal footing with the administering authority. Further, they have stated that the terms of the Admission Agreement cannot be adhered to unless the Administering Authority and the Actuary when setting contribution rates have taken into account any circumstances particular to the admission body. As such, appellants have requested clarification as to whether or not the Actuary has or has not taken into account an individual adjustment by any percentage or amount by which in the Actuary’s opinion, contributions at the common rate should be increased or reduced by reason of any circumstances peculiar to the organisation.

3.17 The Fund disputes the stated purpose and intention. The Fund has sought legal advice on the relevant clause. The advice received confirms that contributions are payable by the employing bodies, but more importantly that those

contributions can be increased or reduced as may be certified by the Fund's Actuary. The purpose and intention of the clause is not to place the employing body on an equal footing with the City of Edinburgh Council. The wording "adjusted by any increase or reduction which may be certified by the Fund's Actuary" makes it clear that the contributions payable by each employing body may be different from the contributions payable by the City of Edinburgh Council. The contribution rates for these organisations, as set out in the Rates and Adjustment certificate, (Appendix G of the Lothian Pension Fund 2014 Actuarial Valuation report), are based on the individual circumstances relating to each employing body. Individual employer contributions have applied in the Fund since 2005.

- 3.18 One appellant was admitted to the Fund many years prior to the others and as such the wording in its agreement is slightly different. The Fund's position, however, is that the same principle applies.
- 3.19 The Fund has suggested that legal advisers discuss the arguments to attempt to clarify the position but this has not yet been taken forward.

Admission basis - staff transfer

- 3.20 Three employers are disputing the treatment of liabilities of employees who were previously employed by other organisations (councils) in the Fund.
- 3.21 Lothian Pension Fund has sought specialist legal opinion on the admission of employers following staff transfer from another Fund employer, this being prior to Transferee Admission Bodies being established by previous Regulations. This advice has confirmed that the basis of admission is not relevant for current scheme funding and employer contribution purposes. The Fund and the Fund Actuary must treat each admission body on an individual basis when deciding on the appropriate funding approach.
- 3.22 Employers have an incorrect perception of the treatment of liabilities when these were transferred between employers. Appellants asserted that they received no credit of any assets in respect of liabilities accrued prior to their admission. This assertion is incorrect. In 2002, when bespoke employer funding arrangements were put in place, each recipient employer received 96% funding on an ongoing basis (96% being the overall funding rate at the time).
- 3.23 This arrangement, however, does serve to highlight the inconsistency of the allocation of assets on the ongoing versus the cessation basis. For those employers admitted to the Fund owing to the transfer of members from another Fund employer, and where the ceding employer has agreed to the treatment of the employer as a Transferee Admission Body for funding purposes, it is therefore considered that a cessation basis on the ongoing basis, akin to the treatment of Transferee Admitted Bodies, would be appropriate. An amendment to the Funding Strategy Statement is proposed to effect this change.

Gilts basis for funding and cessation valuations

- 3.24 All organisations have objected to the gilt discount rate being used in the cessation valuation and representations have been made directly to the Scottish Government on this matter.
- 3.25 Various appellants disputed the lower risk contribution and investment strategy which the Fund assigned to those employers in the period close to exit, or at higher risk of an impending cessation event. For example, “There is the prospect that the last member may not retire, triggering a cessation event, for (a number of) years...we are of the view that a move to a gilts based valuation at this point imposes an excessive burden ... given that continuing to invest over this period will in all likelihood reduce the ultimate cost of providing for the liabilities”.
- 3.26 As previously advised to Committee, the principles of cessation valuations, namely the crystallisation of pension liabilities when there are no more active members, are receiving attention nationally across the LGPS. Indeed, the Scheme Advisory Board for the LGPS in England and Wales commissioned a review of deficit management (which includes cessations and the management of the exit of employers from funds) and a report entitled was produced by consultants in July 2015. It is emphasised that, at this stage, this represents only one opinion and remains under consideration by the Board.
- 3.27 In August 2015, the Scheme Advisory Board for the LGPS in Scotland considered representations from some Community Admission Bodies who are concerned that recent cessation valuations may place their organisations in jeopardy. The Scheme Advisory Board has said it is sympathetic to these concerns while recognising that it would be unreasonable to expect other employers to meet the cost of these payments. It also recognised that funds have not changed the way they have dealt with this issue and have been prepared to be as flexible as possible by spreading the costs over a period of time. It may undertake a broader review and any guidance resulting from that the review will be considered in due course by the Fund.
- 3.28 The Fund Actuary remains strongly of the view that, for employers lacking any strong financial covenant (and whose admission did not arise exclusively from the transfer of staff from another scheme employer), it would not be appropriate for the Fund to contemplate any relaxation of the funding bases for cessation valuation, namely using a UK Government bond derived discount rate together with an allowance for mortality improvements. Such a degree of prudence is required in order to protect the interests of the aligned body and/or the remaining employers within the Fund. This stance is entirely consistent with the approach taken by the majority of LGPS administering authorities across the United Kingdom.
- 3.29 Committee should also be aware that the Scottish Government issued a consultation on amendments to the Local Government Pension Scheme

(Scotland) Regulations 2014 on 1 September 2015. One amendment (regulation 21(b)) proposes to provide a grace period of up to three years before a cessation debt payment is required by the fund actuary. This can be applied where an employer has no active members in the scheme and the administering authority believes that the employer is likely to have one or more active members contributing to the fund within the period specified in the suspension notice. A new regulation 25A regarding employer contributions for historic liabilities is proposed to be inserted into the transitional regulations. The new regulation allows flexibility regarding the time period over which cessation debts are paid.

- 3.30 Having discussed the draft regulations with the Fund's Actuary, the Fund has responded to the consultation. A temporary suspension of the need for a cessation debt payment (regulation 21(b)) is believed to be of more relevance in England and Wales because of open Town and Parish Councils which typically might have a single active member and when that employee leaves or retires there may be a delay in replacing the member. It may prove useful in Scotland in isolated cases but there is a danger that this may encourage closed employers bodies that are approaching cessation to admit new members in order to postpone or delay cessation indefinitely. It is difficult to envisage a situation when the Fund, which knows that an employer is closed to new entrants, could issue a "suspension notice".
- 3.31 Further, the fact that funds will in future have the right to recover outstanding liabilities (regulation 25A) relating to such employers is a positive development. However, concern was expressed that the wording of the draft regulations is too vague in terms of what flexibility a Fund should have when setting contributions (certified by an actuary) to recover these liabilities. Preference would be for regulations to set out the principles of how funds should approach this and avoid being overly-prescriptive.
- 3.32 On 30 October 2015 a letter was issued to all LGPS funds in Scotland by the Scottish Government. A copy of the letter is attached as Appendix 1. At the time of writing the implications of the letter are being considered and a verbal update will be provided to Committee.

Employer contributions 2015/16 to-date

- 3.33 Pending determination of the appeals, a number of employers have continued to make employer pension contribution payments for 2015/16 at the previous year's rates, rather than the required minimum contribution, as certified by the Actuary, for the actuarial valuation 2014. This matter will be pursued further with the relevant employers.

Funding Strategy Statement – Past Service Deficit

- 3.34 Employer contributions, as calculated by the Fund Actuary, comprise two elements:

- An estimate of the cost of benefits accruing in the future, referred to as the “future service rate”, which is expressed as a percentage of payroll and;
 - an adjustment for the solvency of the Fund based on the benefits already accrued. If there is a surplus, there may be a contribution reduction; if there is a deficit there may be a contribution increase. For all employers, contributions to cover any Past Service Deficit are expressed as a fixed monetary sum, rather than as a percentage of payroll.
- 3.35 The overwhelming majority of employers are paying the past service deficit contribution on a monthly basis, that is one twelfth of the annual fixed monetary sum, and the small remainder of employers paid in a one-off lump at the start of the year by prior arrangement. However it has come to the attention of the Fund that there may be unintended scope for an employer to interpret that it may defer payment of the total past service deficit contribution up to the last day of the financial year. The Fund Actuary has confirmed that such interpretation would not be in accordance with his intention.
- 3.36 Accordingly, it is recommended that Committee should consult with employers on the proposal that the Funding Strategy Statement should be amended to stipulate that the past service contribution should be paid monthly on a proportionate basis.

Funding Strategy Statement – Amendments

- 3.37 The proposed amendments noted above (change to cessations for employers admitted to the Fund owing to the transfer of members from another Fund employer and the frequency of deficit payments) have been subject to formal employer consultation from 17 to 28 September. With the postponement of the Pensions Committee’s consideration of the Funding Strategy Statement, the consultation was extended to 23 October.
- 3.38 5 written responses to the consultation were received, 4 from individual employers and 1 representing a group of 18 employers (albeit 1 of the 18 named employers is not known to the Fund).
- 3.39 The responses from the four individual employers were supportive of the changes made with one comment that they are ‘sensible and appropriate’.
- 3.40 The group response is attached at Appendix 2. In response to the issues relating to the Funding Strategy Statement:
- 1) Short notice of Consultation Process. The Fund acknowledges that the original consultation period was shorter than is usually the case due to the resource intensive appeals process. The consultation period was however extended to 23 October. The Fund has attempted to keep employers up-to-date as the appeals process has progressed, issuing a number of bulletins to the appellants and holding face-to-face meetings.
 - 2) Employer contributions in respect of Past Service Deficit (PSD). By way of background, the 2011 actuarial valuation was the first which presented PSD contributions as a monetary sum rather than a percentage of pay for all

employers. The rationale was to ensure that PSD contributions were received even if pay reduced. Reference was made in the response to the method of payment of strain costs as a comparison. However, strain costs are calculated using actuarial guidance and depend on individual membership data and are payable immediately when the member retires.

- 3) Cessation Basis for employers admitted to the Fund as a direct result of a staff transfer from another Fund employer: The group response is unclear on this proposal 'do not necessarily agree'. It is worth noting that three employers in the group would be favourably affected by this change. The Fund has received confirmation from the two councils who are directly affected by this change that they are comfortable with the change.

3.41 Committee is asked to approve the changes to the Funding Strategy Statement.

Measures of success

- 4.1 This report seeks to ensure the sustainability of the Lothian Pension Fund, recognising the affordability constraints faced by its employer membership.

Financial impact

- 5.1 None directly arising from this report, although the determination of any employer appeal against the funding strategy has obvious financial implications for Lothian Pension Fund. Similarly, any spreading of a deficit payment on cessation of an employer will also be of consequence. Both these aspects are directly addressed by the separate reports on the "B Agenda".

Risk, policy, compliance and governance impact

- 6.1 The risk that any individual employer is unable to fulfil its financial obligations to meet pension liabilities is addressed by the Fund's Funding Strategy Statement. This report proposes suitable amendments to the Funding Strategy Statement.

Equalities impact

- 7.1 There are no adverse equalities impacts arising from this report.

Sustainability impact

- 8.1 There are no adverse sustainability impacts arising from this report.

Consultation and engagement

- 9.1 The Fund has engaged in consultation and dialogue with its employers over the changes to its funding strategy during the actuarial valuation. Similarly, there has been engagement with employers regarding the implications of cessation of LGPS membership.
- 9.2 Changes to the Funding Strategy Statement have been subject to consultation with employers.

- 9.3 During consideration of the appeals, consultation has also been undertaken with the Convenor of the Pensions Committee, the Convenor of the Pensions Audit Sub Committee and the Independent Professional Observer.
- 9.4 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading/external references

Alastair D Maclean

Chief Operating Officer

Deputy Chief Executive

Clare Scott, Investment & Pensions Service Manager

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Links

Coalition pledges

Council outcomes CO26 - The Council engages with stakeholders and works in partnerships to improve services and deliver agreed

Single Outcome Agreement

Appendices

1. Letter from Scottish Government
2. Employer response to consultation on amendments to Funding Strategy Statement

Deputy First Minister
and Cabinet Secretary for Finance, Constitution and Economy
John Swinney MSP

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Local Government Pension Scheme (Scotland) Investment &
Governance Group
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FAO - Scottish Local Government Pension Fund Authorities



30 October 2015

To Scottish Local Government Pension Fund Authorities

I have previously asked the Scheme Advisory Board of the Local Government Pension Scheme (LGPS) to consider in some detail the impact on Community Admission Bodies and on the LGPS of fund authorities' approaches to cessation valuations.

Initial responses supported the introduction of amendments to scheme regulations which my officials were already bringing forward and on which consultation closed on 10 October. The amendments contained in The Local Government Pension Scheme (Scotland) (Amendment No. 2) Regulations 2015 augment flexibilities which already exist in those regulations. Taken together, stakeholders have told us that they can enable fund authorities to take a balanced approach - considering the impact on the fund, organisations in question and scheme members - when dealing with and considering their approach to cessation valuations.

The Scottish Government expects these regulations to be in force in December 2015. However, given the support these have received from the Scheme Advisory Board and other stakeholders I am sending you this letter to confirm that it is entirely appropriate for fund authorities to consider these sensitive matters as if those regulations were already in place, and act accordingly.

It has also become clear that there is limited and incomplete information available to the Scheme Advisory Board and amongst the local government community about the scale and impact of cessation funding issues on affected bodies and the pension scheme. Consequently, I have asked the Board to carry-out a detailed assessment of this issue in Scotland, around which further policy guidance may subsequently be considered.

Given the significance of this issue to affected bodies; the eleven LGPS funds; and members of the LGPS and the communities they serve; I would expect fund authorities to seek all means to carefully avoid precipitating the triggering of cessation liabilities until that assessment has concluded and has been considered by the Scheme Advisory Board and by the Scottish Government. This is particularly important where there has been limited prior discussion between a fund authority and an organisation about its liabilities and relative proximity to a cessation event.

JOHN SWINNEY

**Response to Consultation on Proposed Amendments to the Lothian Pension Fund Funding Strategy Statement by LPF Employers' Forum
September 28th 2015, updated October 22nd 2015**

1. Short Notice of Consultation Process

- a. Consulting on any amendments to the Funding Strategy Statement at such short notice puts most of the employers affected by the Funding Strategy Statement at a significant disadvantage as they do not have the capacity or resource to consider the implications of the amendments and to respond appropriately.
- b. At the LPF Employers Forum Meeting with Clare Scott in April 2015 the issue of communications was specifically raised. It was widely believed that had changes been considered over a more reasonable timescale and better communicated to employers that many of the difficulties faced by employers could have been better addressed. Employers were provided with reassurances that future communications would be provided in a more timely manner. This does not appear to be the case.

2. Scope of Appeals Process

- a. The opening paragraph of the consultation document states:
Following consideration of appeals by certain employers against the lower risk investment and contribution strategy, submitted in accordance with the decision of the Pensions Committee in March 2015, Lothian Pension Fund is now consulting with all its employers on proposed amendments to its Funding Strategy Statement.
- b. The appeal process was explicitly not about the lower risk investment and contribution strategy. The appeal process was only about the affordability of the lower risk investment and contribution strategy on individual employers.

3. Employer Contributions in respect of Past Service Deficit

- a. According to this consultation, the Past Service Deficit is a 'fixed monetary sum', rather than a variable amount based on a percentage of payroll. Therefore it is irrelevant when this 'fixed monetary sum' is paid within the financial year.
- b. Existing precedent of payments of pension strain costs, where single annual payments are made rather than 12 monthly payments, suggests that this is an acceptable approach to payments of 'fixed monetary sums' to LPF.
- c. At the meeting of the LPF Employers' Forum with Clare Scott in April 2015, it was explicitly stated that given the nature of the past service deficit payments (i.e. a 'fixed monetary sum'), payments could be paid within the financial year, rather than at the same time as the future service contribution.
- d. However, the valuation of the Past Service Deficit is not a 'fixed monetary sum'. Simply put, the level of this valuation varies depending on the financial assumptions made at a particular moment in time, the financial market conditions at that particular moment in time, the mortality of the individual members and their beneficiaries, and whether members transfer their benefits out of the scheme.
- e. All of these mean that the Past Service Deficit is not a 'fixed monetary sum'.

4. Cessation Basis and Admission Agreements

The employers note the terms of the Consultation document. The employers do not necessarily agree with the proposed changes in respect of employer contributions for past service as it relates to their individual circumstances with specific reference to the terms and provisions of their own admission agreements. As such the employers reserve all rights under the terms of their admission agreements and in terms of the Regulations.

The following organisations are members of the LPF Employers' Forum and support this joint response:

Centre for the Moving Image
Dean Orphanage & Cauvins Trust
Edinburgh International Festival
Edinburgh World Heritage Trust
Festival City Theatres Trust
Freespace
Health in Mind
Homeless Action Scotland
Impact Generation
Into Work
Link in Craigmillar
National Mining Museum Scotland Trust
Penumbra
Pilton Youth and Children's Project
Queensferry Churches Care in the Community
Scottish Legal Complaints Commission
Streetwork UK Ltd
Victim Support Scotland