Consultation on the future structure of Scottish LGPS

Joint response from the Scottish Council for Voluntary Organisations and the Robertson Trust

7 December 2018

SCVO Background

The Scottish Council for Voluntary Organisations is the national membership body for Scotland's charities, voluntary organisations and social enterprises. SCVO works to support people to take voluntary action to help themselves and others, and to bring about social change. It provides services and support to the third sector in Scotland to advance shared values and interests. SCVO has approximately 1,900 members, ranging from individuals and grassroots groups, to Scotland-wide organisations and intermediary bodies. The organisation employs approximately 100 staff.

The Robertson Trust Background

The Robertson Trust is the largest independent grant-making Trust in Scotland. We aim to improve life and realise potential of people & communities in Scotland. Robertson Trust is therefore integrally linked with the Charity Sector across Scotland and has a stake in ensuring that the value of grant funds to the Third Sector is fully maximised.

Introduction

We are jointly responding to the Scottish Local Government Pension Scheme Advisory Board ('SPSAB') consultation on the future structure of the Scottish LGPS issued in June 2018. This response specifically looks to focus on issues charities face through being part of the various LGPS funds in Scotland and builds on our engagement with Scottish Government directly and as part of the collective engagement headed by ICAS.

Charities and not for profit organisations are an integral part of Scottish LGPS. According to the data collection exercise undertaken by SPPA in March 2014 there were 530 employers with at least one active member in LGPS funds. Of these, 422 are admission bodies covering both transferee admission bodies (TABs) and community admission bodies (CABs). The remaining 108 are scheduled bodies, including local authorities.

So these admitted bodies account for about 83% of total employers and around 17% of the 218,669 active members so are material participants.

From 1 February 2013, all new admission bodies must provide some form of security – indemnity, bond or guarantor. Whilst given this we are more concerned with the bodies who entered the schemes prior to this date who may have liabilities which are unprotected. Equally we understand that 3rd sector organisation will continue to participate in LGPS for many years as transferee admission bodies performing outsourced services on behalf of public sector entities.

Consistent feedback from 3rd sector participants in LGPS highlights poor clarity in communication, a lack of focus on these organisations' specific circumstances, limited flexibility when considering exits from the Fund and an inequity in dealing with legacy liabilities, relating to public sector employers, accrued in the Funds. These findings are wholly consistent with those recently identified as part of the Tier 3 review commissioned by the Scheme Advisory Board in England & Wales.

Our organisations are wholly supportive of any steps taken within LGPS which would provide increased engagement, lower benefit costs, a greater level of consistency and above all greater fairness in how 3rd sector organisations are treated. We are also wholly supportive of the proposals made by ICAS in September 2017. In addition we recognise the steps taken by Scottish Government in updating LGPS Legislation in 2018 to increase flexibility however remain concerned by the limited level of traction the Regulations have achieved given a lack of commitment from the individual Funds. Our key concerns are that any review should also address the following:-

- The attitude of Funds to legacy liabilities which have been passed on to charities by Councils and other public sector bodies. It is very common when analysing charity liabilities that very significant proportions of these liabilities relate to staff who had service built up prior to working with the charity. These transfers of liability were not clearly communicated to the charities and while they may have been transferred at the time on a 'fully funded' basis, this calculation was on an 'on-going' basis and not on the 'cessation' (nil risk gilts basis) that charities are asked to pay on exit. This means that Councils are just expecting charities to absorb these liabilities and effectively pay for them on behalf of the public bodies. This seems wholly inequitable. We have seen numerous examples of organisations being left with these liabilities as Councils and/or Scottish Government refuse to accept responsibility for them even though it is clear that they were built up by them and indeed had agreements been written now they would have had to guarantee them.

This is also an area where there has been a huge divergence of approach between Funds. Lothian Pension Fund has amended its Funding Strategy Statement (FSS) to look to address the issue of legacy liabilities formally. While a small number of others will consider it informally, the vast majority due to not having any practice in place are rejecting any proposals.

This was an issue raised in the ICAS paper but was not dealt with in the new Regulations. This we feel has to be addressed and in our view further consolidation between the LGPS funds is likely to make consistent practice more likely.

- There is a huge lack of consistency and clarity in relation to pensions associated with public sector out-sourcing contracts. The charitable sector is very well placed to perform these duties in many cases, but are discouraged from doing so by the complexities associated with LGPS participation. This is not in the interests of the charities, public bodies or indeed the tax payer should these services not be being provided by those most suitable and most able to offer cost effective provision because of the complexity, inconsistency and risk of the associated pension provision. A single, consistent, risk managed approach would therefore be hugely valuable.

- The cessation position and process is not clearly understood by many third sector participants and we believe that greater transparency and better communication is required from the Funds. We would propose that admitted bodies are provided with an estimated cessation valuation annually with a clear description of what this means. Some Funds already provide this on request as part of FRS102 disclosures but it should be incorporated as practice.

Considering the proposed options

The SPSAB's consultation sets out four options for the future structure of pension fund in Scotland and we would like to comment on each in turn as we believe they relate to 3rd sector bodies.

1. Retain the existing structure

Retaining the status quo is likely to mean that inefficiencies will remain as most funds will not achieve the benefits of scale such as improved bargaining power, access to greater resources and reduced duplication of efforts in administration, governance, spending on advisers and fund management. Larger funds are also likely to be able to better access infrastructure investments. Maintaining the existing approach is therefore likely to mean that costs per member are likely to be higher than necessary.

A move away from the status quo might result in the loss of local input and oversight and regional diversification. From our experience however this regional input is more of a hindrance than a value as it results in a wide range of practice and additional cost in managing interactions. It is also usually the case that regional funds are not aware of valuable approaches undertaken in other areas and therefore feel unable to apply them in their area. Greater centralisation would allow for greater implementation of best practice and for a much greater consistency of approach. Also, the existing structure potentially creates a key person risk as there is less available resource to cover key roles as well as budgetary and staff risk due to other competing local priorities. Consolidation should result in access to greater specialist resource, even if some of that resource needs to be regionally located.

Clearly any savings made or improvements achieved would need to outweigh any initial transition costs but all research to date would tend to support a move away from the status quo.

2. Promote co-operation in investing and administration

There have already been some examples of collaboration particularly in the investment area and around procurement. This approach would allow the current governance structure to continue, allowing for continued local oversight, although requiring some sharing of control. There would also have to be some adaptation of governance.

Approaches to date seem to have been relatively informal which results in a degree of uncertainty over their future persistence so a more formal structure may be of value to assist with planning as well as the distribution of costs and returns. To date this sort of co-operation has been pretty limited despite its obvious benefits which would suggest that without strong vision and direction it will remain something of an outlier which would suggest that greater structure and compulsion is needed to really drive change.

3. Pool investments

This approach would mirror that currently being adopted in England and Wales.

A single pool would double the asset size to about £42Bn over the largest Fund which has assets in excess of £20Bn. At this size it would be of a similar size to 3 of the English pools and larger than the 3 others so it would not be excessively large but would have sufficient scale.

Fund assets and liabilities would still be allocated in the same way to ensure specific employer responsibility for liabilities.

A move of this type would be likely to result in lower cost investing, subject to some initial cost increases to manage a transition. It would also be likely to mean that the asset pool was of a significant enough size that more of the investment and administrative tasks could be undertaken in house.

From a governance perspective each Pension Committee would retain responsibility for asset allocation and managing the legislative structure however day to day investment management would be delegated to the pool.

As has been shown in England and Wales this approach is very achievable and it's hard to deny the value so this would seem to be a minimum required step. However other than the potential for reduced cost of pension provision such an approach is unlikely to meet the administrative demands of charitable employers participating in the Funds as outlined in Point 1.

4. Merge funds in to one or more funds

We envisage this as the creation of a Scottish 'superfund' which would manage all LGPS benefits in Scotland. Such a move would benefit from the asset pooling advantage in option 3 above but also allow for merging of the administrative and governance functions.

Such a move, whilst ultimately desirable from a cost and consistency perspective is not without its challenges. Each of the Schemes is funded at a different level and there would have to be a recognition of this and a mechanism to resolve it to ensure there was no cross subsidy between different regions and, as a result, between employers. There would also have to be clarity in terms of governance, priorities and costs. There are also political drivers as well as the need to ensure that the right level of resource is available to the new consolidated scheme.

None of these challenges, however, in our view, are insurmountable and really just need commitment to achieve the objective and a clear plan to do so over a reasonable timescale.

The LGPS funds all provide consistent benefits based upon a single regulatory framework. Consolidation would remove regional variations and inconsistency. Legacy arrangements would have to be clearly documented and honoured but future practice could be implemented on a wholly fair and consistent basis. Undoubtedly given the size distribution of schemes in Scotland a number of them would be likely to benefit from cost savings and improved governance very quickly. Market buying power in terms of services would be improved and greater investment possible in staff, technology and scheme communications.

Conclusion

We believe that any change to the future provision of pension benefits via LGPS in Scotland must meet some key principles:-

- Value for money

  Research carried out by Deloitte in 2011 suggested that costs per member in Scotland compared favourably with LGPS funds in England and Wales and that a single operating model and common administration system may have a greater benefit than formal administration mergers. However, research by APG concluded that administration costs decline with larger funds and certainly this seems to be the model being employed across UK defined contribution businesses. Future cost savings need to be considered against any transition costs.

  Any changes which mean that more of any contributions paid go in paying for pension benefits and not in scheme costs are to be welcomed.

- Independence

  The benefits of having a single scheme which is not accountable to a local authority and can operate in an autonomous way based on its agreed priorities should provide greater flexibility and consistency in staff terms and conditions, and therefore provide the opportunity to attract a much higher calibre of staff.

  Currently also there is a lot of local autonomy and national guidance can tend to be ignored in certain areas. A single scheme would make it much more likely that changes/ improvements to the Scheme could be more consistently applied.

- Expertise

  Consolidation would allow for much more specialist staff and teams of staff to be developed who were much more familiar in dealing with key issues in a consistent way. We would even hope that perhaps there would be a specialist department to deal with admission bodies/ charities which could be more engaged with the sector and it's needs as well as being party to solutions which could be applied on a more consistent basis.

- Flexibility

  More centralised support and specialism allows greater flexibility in resource, skills and approach. It also needs to be considered that the number of employers participating in LGPS in Scotland is falling so less resources are needed and greater consistency of practice can be achieved.

- Consistency/ Fairness

  There is the potential to better integrate best practice and provide greater consistency across the Scheme with less room for decisions based upon local interest to be taken. In addition with greater employer consolidation there will undoubtedly be increased demand for larger employers to have all benefits consolidated in a single fund rather than across multiple schemes.

There are clear benefits which can be achieved through investment pooling and even further benefits through a consolidated single scheme for Scotland – it just needs vision and commitment to achieve them.

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