HYMANS ROBERTSON

A better future for the LGPS

The charity experience

What is the employer experience in the LGPS? This is the second in a series of briefing notes where we consider some of these experiences, how they affect the employers concerned, and what solutions might be available for funds to secure better outcomes for everyone. This month we consider charities...

As mentioned in our previous note, Hymans Robertson has carried out a unique analysis across nearly half the Local Government Pension Scheme in England & Wales, considering different employer experiences in the LGPS. This showed a multitude of individual stories affecting employers and their staff. In this series of briefing notes we consider a few of these: our previous note looked at the position of a Multi Academy Trust, and now we turn to:

Case Study 1: Charity

History: When the Charity began working in partnership with the Council many years ago, it seemed fair and relatively inexpensive to offer its staff LGPS membership. Now however, the FD rues the day his predecessors made that pension decision. The Charity has evolved in a very different way from the Council, with a larger proportion of ex-employees and typically a very negative cashflow position. Reduced or removal of contracts and revenues from the Council to the Charity means the Charity has a greater legacy to be funded with less cash.

He also wishes that successive FDs had done something to tackle the problem instead of hoping it would somehow just disappear. Their one action had been to stop offering the LGPS to new joiners around the start of this century, but at that time no-one seemed to consider the size of the cessation debt this would inevitably lead to. Now that the active membership has fallen to single figures, that debt is looming.

Current issues: The Charity's finances do not look likely to improve materially any time soon, but its pension obligation is worsening. This is mainly because the dwindling number of active members mean the Charity will be facing a huge cessation debt which will be payable when the last member leaves. The ongoing deficit is difficult enough to handle, but the cessation debt is a multiple of that: the Fund's offer to pay it off over a few years does not really help, as it remains frankly unaffordable. And don't think that potential supporters of the Charity haven't noticed its large and growing FRS102 balance sheet provision either…

The FD also harbours distinctly un-charitable thoughts about those responsible for QE, the banking crisis, the EU Referendum result … all of which have driven interest rates to unprecedentedly low levels and the Charity's cessation debt unbelievably high. If only he could buy more time till markets helped him out, allowed the Charity to carry on its good work, but didn't require an artificial re-opening of the Fund to new entrants?

Solution: Firstly, the FD needs to avoid becoming another predecessor who didn't tackle the problem: action is needed as soon as possible to stop the problem potentially getting worse. This might be as simple as speaking with the Fund to make that connection. Early discussion with the Fund could help avoid the Charity being wound-up (which the Fund doesn't want to see, either), whilst addressing the key issues as follows:

- cease the Fund to future accrual by the current actives: some difficult conversations and careful legal analysis may be needed, but this means the Charity does not need to pay Primary contributions and the diversion of Primary (ongoing) contributions to Secondary (deficit repair) could be very valuable;
- the Charity would in effect "buy time" if they could provide suitable security to the Fund in place of paying the cessation debt. This could take the form of the Charity's office building, for instance;
- contributions maintained on a monetary basis (not a percentage of pay) to meet the legacy obligations, with increases as and when the Charity's finances allow;
- provide evidence of strength of covenant to reassure the Fund and allow more flexibility in contributions;
- monitor the funding level to identify as and when markets are helping to meet the cessation debt through equity gains and/or interest rate rises. These are by no means certain within a given timeframe, but modelling work could help identify the likelihoods of different outcomes, for the benefit of both parties; and
- monitoring also swiftly identifies any de-risking opportunities (in investment strategy) which could crystallise gains and improvements in the funding positon of the Charity.

Conclusion

There are over 13,000 employer stories in the LGPS, and counting: the number grows with every academy conversion, outsourcing contract, and service delivery re-design. To date, these stories have emerged in occasional newspaper articles, employer accounts, or even insolvency details. However, we think it is time to take a step back and tell these stories before they finish, while there is still time to change the ending. The Government can play its part, through financing arrangements, backing of charities, etc. We know that SAB are looking at options around "Tier 3" employers such as charities and admission bodies. This is to be welcomed, provided this doesn't simply move the LGPS problem elsewhere (as the colleges insolvency regime consultation did in effect).

We think it is increasingly untenable for LGPS funds to have a "one size fits all" approach to investment strategy. Whilst different funds may take different approaches, it is clear that re-considering investment and funding strategies in tandem, on an employer-focussed basis, will lead to better outcomes. We look forward to discussions with funds on what can be done.

Next month, we look at the experience of Borough and District Councils within the LGPS

"*The Borough Council looks enviously at the County. Over the years it has seen significant staff reductions, and its greater maturity puts it in a very different position from the County…*"

If you would like to discuss this further, please contact us or your usual Hymans Robertson consultant.