

Government response to Shadow Scheme Advisory Board analysis and recommendations in response to the Call for Evidence into the future structure of the Local Government Pension Scheme

I would like to thank the Shadow Scheme Advisory Board for your significant contribution thus far towards the work on structural reform of the Local Government Pension Scheme. I am sure my officials have found your final report, which identifies the key themes in the call for evidence and draws out your recommendations, highly useful in informing the development of principles for reform. I have sought to respond to each of your recommendations in turn, and would be happy to discuss these further in a meeting if you would find this helpful.

1. The Government should consult on options for reform as soon as possible.

My officials have finalised the drafting of the consultation and we are currently in the process of obtaining agreement across Government. Once this has taken place, I intend to share it with the Shadow Board in advance of its publication. I would be happy to meet with you once the consultation is public to discuss further its content and your continuing areas of work.

2. The Government and the Board should agree a realistic timescale for implementing reform by the end of summer 2014.

We will shortly be consulting on structural reform and publishing the Hymans Robertson report alongside it, giving interested parties the opportunity to feed in to the development of the policy and ensuring a realistic timetable for reform that allows for robust scrutiny and feedback.

It is in light of the responses to this consultation that I intend to consider the timetable for reform and the more detailed proposals that will emerge from it. Whilst being keen to progress at pace, I am mindful that making sure the right proposals are implemented effectively is of the highest importance.

3. The Board should complete the work on setting an agreed baseline of data and measurements via the Scheme Annual Report process by the end of 2014.

Your report recognised the popular view in the call for evidence that the current Scheme data is not comparable or sufficient to guide appropriate decision making. I am grateful for the work you have already undertaken towards developing a single Annual Report for the Scheme and welcome your proposal to set an agreed baseline of data and measurements by the end of 2014.

Whilst the Hymans Robertson report has provided comparable data on performance and fees to support decision making, I recognise that there is more to be done to establish a fully comparable set of fund data. I see a significant role for the Shadow Board in carrying out this function and would encourage you to work closely with my officials as they review the data collected by the Department, in order to ensure that Scheme data is more transparent, comparable and easily understood in the future.

4. The government should introduce proportionate and appropriate legislation to provide a statutory underpin for both the objectives of reform and the timetable for implementation.

The legislative changes required to deliver reform will largely be dependent upon the detailed proposals that develop following the consultation. I therefore do not propose to introduce legislation to underpin the objectives and timetable for reform, but remain prepared to consider secondary legislation where necessary as our proposals take shape.

5. In formulating its consultation on high level options for reform the government should consider (a) alternative methods for managing deficits and (b) analyse the costs/benefits and barriers to greater passive management, collective investment vehicles and in-house investment strategies.

As your report highlights, although the call for evidence was developed around the primary objectives of reducing fund deficits and improving investment returns, very few responses set out ideas for managing deficits in a different way. I agree with your recommendation that there is a clear role for the Shadow Board in supporting the Government by developing a shortlist of feasible options for managing deficits, and am keen to have sight of this analysis before the end of the summer recess.

With regard to part (b) of this recommendation, Hymans Robertson's analysis, which will be published alongside the consultation, has gone a considerable way towards addressing this issue. It provides a thorough analysis of the costs, benefits and barriers of greater passive management and common investment vehicles; setting out how they might be implemented and when savings might be realised. Their work has also made use of detailed, standardised data to explore investment costs more fully and take a comprehensive view of the Scheme's performance in aggregate. The evidence available indicates the potential to reduce costs significantly through passive management and collective investment vehicles, and I will seek views on their greater use in the consultation.

Although you recommend that in-house management is explored further, you also note in your report that it is more effective when used by larger funds. In light of the cost-benefit analysis undertaken by Hymans Robertson and the strong feeling in the responses to the call for evidence that funds should not be merged, the Government has decided not to pursue fund mergers at this time. As a result, we do not intend to investigate the option of in-house management further at present.

6. The Board will support the Government by (a) developing a shortlist of feasible options for managing deficits and (b) conducting further research on the costs and benefits of the key options for reform.

As set out above, I remain committed to considering alternative options for tackling deficits, and see great merit in the Shadow Board looking at the costs and benefits of the key options you identify around deficit management. I would be grateful to receive any innovative proposals on this subject, ideally before the summer recess.

7. That Government should ensure that any work being undertaken as part of the call for evidence is consistent with other strands of LGPS policy work, for example the LGPS 2014 governance regulations and any reform of the investment regulations.

I recognise that the investment regulations are in need of review and have asked my officials to consider whether they remain fit for purpose as we move forward with wider Scheme reforms. My officials will ensure that the emerging proposals for governance and investment regulation reform are taken into account as all three policies develop.

I appreciate that the work you will carry out around deficits and improving data transparency will sit alongside the consultation. However, I believe it is right that you continue to look at these important issues which you have helped identify, as the wider package of reforms develop.