



intergenerational foundation

Fairness for Future Generations

A response to the call for evidence on the future structure of the local government pension scheme

Who we are...

The Intergenerational Foundation (IF) (www.if.org.uk) is a think tank which researches fairness between the generations in the UK, in order to protect the interests of younger and future generations, who are at risk of being ignored by current policy-makers.

Our response...

Our responses to the individual questions set out in the call for evidence document are as follows:

Question 1 – How can the Local Government Pension Scheme best achieve a high level of accountability to local taxpayers and other interested parties – including through the availability of transparent and comparable data on costs and income - while adapting to become more efficient and to promote stronger investment performance.

IF believes that one of the key objectives of reforms to the Local Government Pension Scheme (LGPS) in England and Wales should be minimising the financial liabilities which are being passed onto future generations of taxpayers. Towards this end, we need to achieve both complete recognition of what the liabilities of each individual scheme are worth in today's terms – published as regularly as possible using a range of different discount rates and life expectancy projections to take account of different future scenarios – and what the financial position of each of the schemes is in terms of assets and liabilities. This is the only means by which individual schemes can remain transparent and accountable to local taxpayers.

Each scheme within the LGPS currently has to publish annual accounts, but these are highly technical documents which are difficult for ordinary members of the public – or indeed the majority of scheme members – to read and understand. Therefore, it would improve accountability and transparency if the key information about each scheme could be made available in a more accessible format which had been designed to be accessible to ordinary members of the public and scheme members, such as an online web portal designed on a similar basis to the one which already exists for the National Employment Savings Trust (NEST).

Question 2 – Are the high level objectives listed above those we should be focussing on and why? If not, what objectives should be the focus of reform and why? How should success against these objectives be measured?

IF agrees that the two objectives of the reforms which have been designated “high level” are both extremely important. Addressing the substantial deficits which exist within many of the individual schemes within the LGPS should reduce the burden which is placed upon future taxpayers, although we would urge that increasing the employee contributions paid by individual members should play a significant role in achieving this. Increasing investment returns will also be another important part of the achieving the same goal.

IF believes in focussing on long-term policy objectives, so we would argue that the objective of increasing the amount of money which schemes within the LGPS invest in infrastructure projects should also have been classed as a “high level” rather than a “secondary” objective. As a report from the National Association of Pension Funds¹ has observed, member schemes within the LGPS are increasingly looking to diversify their investment portfolios away from equities and put a larger share of their money into alternative types of investment, but their ability to invest in infrastructure projects has so far been under-exploited because of restrictions on the types of corporate structure in which they are allowed to invest. Given that the LGPS manages over £150 billion in total and tends to be searching for investments which can deliver returns over the long-term, it seems that much more could be done to unlock the LGPS as a potential source of funding for addressing Britain’s vital infrastructure needs. Achieving this goal should be one of the main objectives of the reforms.

It is a key belief of IF’s that long-term investors such as pension funds should seek to promote intergenerational fairness, a goal which encompasses taxpayers, scheme members and the wider general public. Therefore, improving intergenerational fairness should also be given the status of a “high level” objective. Funding long-term infrastructure projects is one means of promoting intergenerational fairness, while lowering the burden the scheme places on future taxpayers is another. The LGPS should also attempt to promote fairness between different generations of scheme members, a goal which appears to have been neglected during the formulation of the Hutton reforms as these will enable older scheme members to retain their previously accrued final-salary pension rights and retire at 65, while younger scheme members will be moved to a career average basis and have a retirement age which is adjusted in line with changes in the state pension age. We do not see why older scheme members should have received this preferential treatment compared to their younger colleagues, and it means that one outcome of the Hutton reforms will be to spread intergenerational unfairness between different generations of scheme members.

¹ NAPF (2013) *Local Governemnt Pension Scheme 2013: Investing in a Changing World* London: NAPF

Question 3 – What options for reform would best meet the high level objectives and why?

As explained in our answer to the previous question, allowing schemes within the LGPS to invest more aggressively in long-term infrastructure projects should have a positive impact both on deficits and improving investment returns. There are also clearly arguments in favour of merging some of the individual schemes within the LGPS in order to take advantage of economies of scale over administration costs and management fees, as well as to give them greater financial weight as investors. Although merging all of the individual schemes currently within the LGPS into one individual fund could prove unwieldy, there is obvious scope for merging smaller schemes within neighbouring geographical areas. For example, it would be perfectly logical to create a single LGPS scheme combining every single local authority in Greater London.

Question 4 – To what extent would the options you have proposed under question 3 meet any or all of the secondary objectives? Are there any other secondary objectives that should be included and why?

Our response to question 3 should help to satisfy the first four of the secondary objectives, as these refer to making larger investments in infrastructure and achieving greater economies of scale.

Question 5 – What data is required in order to better assess the current position of the Local Government Pension Scheme, the individual Scheme fund authorities and the options proposed under this call for evidence? How could such data be best produced, collated and analysed?

As mentioned in our response to question 1, we would argue that more data needs to be produced which can provide a clearer picture of the liabilities which are accumulating within the LGPS for future generations of taxpayers. This would include producing estimates of the schemes' future liabilities using a range of different discount rates and life expectancy scenarios. These should be independently audited, perhaps by the Office of Budget Responsibility (OBR) or the National Audit Office, to ensure they provide a realistic appraisal of likely future outcomes (the NAPF report referred to above showed that the average scheme uses a 6% discount rate, which has proved to be over-optimistic in relation to the returns achieved by the scheme between 2007 and 2010). Producing this data would facilitate a clearer, fairer debate about the liabilities which the LGPS is leaving to future generations of taxpayers.

Conclusion...

In order to help promote the interests of future taxpayers as stakeholders within the LGPS, IF would be willing to discuss any of these ideas further with DCLG.

For more information about the Intergenerational Foundation and its work, please visit www.if.org.uk or contact Liz Emerson, Co-Founder at liz@intergenerational.org.uk.

Author:

David Kingman