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THE LGPS: UNSUSTAINABLE

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SUMMARY

- This paper considers the Local Government Pension Scheme's (LGPS) financial health, following publication of its 2014-15 results.
- Cashflow is considered in detail. Had (taxpayer-funded) employer contributions not risen substantially during the year (by £833 million), cashflow would have continued its long-term deterioration, which unambiguously signals that the LGPS is unsustainable. Over the next decade the LGPS faces a perfect storm, due to a combination of past under-funding (hence today's deficits); the end of contracting out rebates (April 2016; some £700 million per year); potentially sclerotic investment returns in a post-QE world; employers opting out of the scheme; destructive demographics (the membership is both living longer and ageing); mis-aligned cost and income drivers; a crippling accrual rate (increased by 63% since 2008); and ten year grandfathering from 2014, which effectively renders Lord Hutton's (cost-saving) proposals impotent for a decade. And while 2013's £47 billion deficit is expected to increase at the next triennial valuation (March 2016), it is negative cashflow that is likely to be the LGPS's undoing.
- Last year's 51% increase in fund management costs, to £748 million, is less alarming than at first sight. After decades of incurring £ billions in unreported costs, to the delight of the fund management industry, some (not all) of the LGPS funds have started to improve the quality of their reporting. But the cost disparity between individual funds is extraordinary. On a per member basis, Cheshire, for example, paid 44 times more than West Yorkshire for fund management, and 19 times more in total costs. Some Pensions Committees should be asking themselves some very tough questions. And what were the real costs, given that none of the funds report the performance fees and carried interest paid to external managers?
- The LGPS is unable to evidence adherence to the old adage of what gets measured gets managed. Cultural change is required, but that could take another decade to materialise.
- Another paper will follow shortly, discussing the Chancellor's recent proposal to reconfigure the 89 LGPS funds as up to six British Wealth Funds, with an infrastructure bias. This will not head off the looming cashflow crisis. The paper will include specific proposals to make the LGPS sustainable for the long term.

INTRODUCTION

Historically, the Local Government Pension Scheme's (LGPS) reporting of costs has been an expensive work of fiction. However, after decades of massive under-reporting, it has finally started to understand its costs, and transition to reporting data that is closer to reality.

In a recent Statistical Release from the Department for Communities and Local Government (DCLG), sponsor of the LGPS, some of the 89 individual funds responded positively to guidance issued by CIPFA,[1] requesting that they improve the transparency of their reporting.[2] Other funds, however (number: undisclosed), ignored CIPFA to continue their tradition of opacity, fuelling the lack of trust that surrounds them.

Heightened transparency should challenge the wilful blindness ("in denial") of a few of those involved in governance but, ironically, it could also accelerate the LGPS's demise. Meanwhile, we should expect further substantial increases in reported costs.

1. OVERVIEW

The LGPS is huge: it matters. At end-March 2015, it had assets of £214 billion and 5.17 million members (active, deferred and pensioners: more than 10% of *all* adults in the UK).[3] There are also 13,000 participating employers, 75% of whom are publicly funded. At the time of the last triennial valuation (March 2013), the average funding level across the LGPS was 79%; i.e. a 21% deficit, equivalent to £47 billion in cash terms. The next triennial valuation is at the end of March 2016: deficits are expected to be higher than previously.

If the LGPS were presented as a single fund, it would rank sixth by size, globally, enjoy considerable economies of scale, and global clout (i.e. soft power). As it is, the largest individual fund (Greater Manchester / Tameside) ranks a lowly 172nd.[4] Consequently the LGPS does not register on the world stage, a missed opportunity to exert influence on both the financial services industry, and also within the geo-political arena.

2. TOTAL COSTS

2.1 A 40% increase, year-on-year

Costs are controllable, whereas asset performance across a diversified fund, beyond asset class allocation, is fundamentally driven by the global economy, not individual fund selection.[5] In the year to April 2015, the 89 LGPS funds reported that costs charged to them had

[1] CIPFA, the Chartered Institute of Public Finance and Accountancy, the professional body for people in public finance.

[2] DCLG; *Local Government Pension Scheme Funds England 2014-15; Local Government Finance Statistical Release*, 28 October 2015. The underlying SF3 data pertains to England *and* Wales.

[3] As 1,893,802 contributing members, 1,775,356 deferred members and 1,489,175 pensioners and dependents; SF3 data returns.

[4] *P&I / TW300 analysis for year-end 2014*; Towers Watson, September 2015.

[5] Numerous studies evidence that, on average, active fund managers do not outperform the market.

Table 1: LGPS costs per scheme member, as reported

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	6 year change
Administration	£28.3	£30.2	£28.0	£27.2	£26.8	£25.2	-11.0%
Fund management	£68.4	£76.9	£84.1	£87.2	£99.9	£144.6	111.4%
Total costs, psm	**£96.3**	**£107.1**	**£112.1**	**£114.4**	**£126.7**	**£169.8**	**76.3%**

Source: DCLG; SF3 data returns for England and Wales increased by a staggering 40%, to £878 million. Third party fund management costs accounted for 85% of this, £748 million, the other £130 million being administration costs.[6] Table 1 shows the development of reported costs per scheme member, over the last six years.

2.2 Individual fund comparisons

The lack of standardisation (actuarial valuations, governance and reporting) across the LGPS affords each individual fund an immense amount of wriggle room. Consequently, comparing one fund with any other is a questionable exercise, which partly explains why no fund is ever held to account.

That said, the raw data underlying DCLG's 2014-15 Statistical Release still provides for some extraordinary comparisons between individual funds. There is, for example, an incredible range in reported total costs per member: *in extremis*, Cheshire's are nearly 19 times those of West Yorkshire's (Table 2). One would like to think that Cheshire's s101 Pensions Committee, and its Pension Board charged with "assisting" the Administering Authority, are asking themselves the question: *how did West Yorkshire do that?* Considerable curiosity is required, informed by a good understanding of the industry (which some s101 Pensions Committees lack).

Appendix 1 expands Table 2 to include all 89 funds. As a general rule, the larger the fund, the lower the costs per member, evidencing that there are opportunities for the LGPS to realise economies of scale. Consider a simple illustration. Table 3 compares the 81 English funds

6 DCLG; SF3 data returns for England and Wales.

Table 2: Total reported costs per member, in ascending order

Rank	Local Authority	Total costs per member 2014-15	% change on 2013-14	Fund market value 31 March 2015 £000's
1	West Yorkshire Superannuation	£28.3	1.8%	£11,319,225
2	South Yorkshire Pensions Fund	£41.3	-1.2%	£6,277,138
3	East Riding of Yorkshire UA	£47.6	-7.0%	£3,677,391
4	Nottinghamshire	£52.8	-3.3%	£4,078,600
5	Tameside	£53.5	-12.4%	£17,591,201
85	Tyne and Wear Superannuation	£462.7	364.4%	£6,378,063
86	London Pensions Fund Auth	£487.2	3.7%	£4,617,208
87	Hammersmith & Fulham	£504.5	29.5%	£868,475
88	Flintshire UA	£511.4	140.9%	£1,394,549
89	Cheshire	£530.3	71.5%	£4,097,211
	Average	**£197.7**	**28.0%**	**£2,404,812**

Table 3: Costs: scale matters

	Average fund size, £000	Total costs per member	Admin costs bp	Fund mgt costs, bp	Total costs, bp
England LGPS funds (81)	£2,479,612	£167.3	6.0	34.3	40.3
Wales LGPS funds (8)	£1,647,465	£208.5	6.9	44.1	51.0
All funds (89)	£2,404,812	£169.8	6.1	34.9	41.0

As basis points measured against assets with the 8 Welsh funds; the latter are, on average, 50% smaller than the average English fund, and their total costs are 25% higher, on both a per member and total assets basis.

Table 4 (and Appendix 2 for the full list) looks at how 2014-15's reported costs per member changed from the previous year. Seven of the 89 funds reported more than a doubling of total costs per member: the bottom five in Table 4, plus Buckinghamshire (103%) and Lancashire (121%).

How did Merton cut its costs per member by 41% while West Midlands increased theirs by 426%? One explanation is that the funds at the bottom of the table are now "catching up", by embracing CIPFA's more transparent reporting agenda, whereas those at the top either ignored it or did indeed achieve some miraculous *genuine* savings. We simply do not know. But what is clear is that many of the funds have long been under-reporting their costs, which raises major questions as to the quality of past cost-related decision-making by their Pension Committees.

3. FUND MANAGEMENT COSTS

The 89 funds, in aggregate, reported a staggering 111% increase in fund management costs per member over the last six years (Table 1), including a 51% increase in the last year alone.[7] However, these figures are misleading; part of the rise is due to better quality reporting, rather than actual cost increases, but we have no idea how much. And so the cloud thickens, albeit that CIPFA is, to its credit, attempting to lift it.

CIPFA is not being helped by the fund management industry, which revels in opacity. Earlier this year the Investment Association (formerly the IMA) issued a 10-point statement of principles for fund manager behaviour. These include requirements to "always put their clients' interests first and ahead of their own", and "take care of clients' money as diligently as they would their own". To date, the significant majority of the membership have refused to sign up to what most people would consider to be a very basic code of ethics. The FCA's recently announced probe into asset managers' and investment consultants' value for money, and conflicts of interest, are no coincidence.

7 Admin costs fell by 2% in the last year.

Table 4: Total reported costs per member; % year-on-year change

	Local Authority	Total costs per member 2013-14	2014-15	% change on 2013-14
1	Merton	£137.8	£81.1	-41.2%
2	Swansea UA	£348.3	£228.9	-34.3%
3	Harrow	£86.9	£70.4	-19.0%
4	Kent	£160.4	£130.5	-18.6%
5	Leicestershire	£103.5	£84.4	-18.5%
85	Newham	£169.0	£382.3	126.2%
86	Brent	£165.2	£387.1	134.3%
87	Flintshire UA	£212.3	£511.4	140.9%
88	Tyne and Wear Super. Fund	£99.7	£462.7	364.4%
89	West Midlands Pension Fund	£59.1	£311.0	426.0%
	Average	**£161.5**	**£197.7**	**28.0%**

Table 5 (Appendix 3 for the full list) focuses specifically on the LGPS's fund management costs.

Ignoring Harrow (which received various rebates), some funds report encouragingly low costs when expressed in terms of basis points measured against fund market value. But why are Flintshire's costs 48 times higher than what West Yorkshire paid (measured as basis points of year-end assets), and Cheshire's 44 times higher on a per member basis? And what was the *real* cost, given that none of the funds report the performance fees and carried interest paid to external managers? If the opportunity cost of this value leakage to third parties were properly understood (£ hundreds of millions each year[8], across the LGPS), one would hope that DCLG would not hesitate to take *all* asset management in-house. In particular, today's reliance on external management to invest over £9 billion in private equity is an extraordinary exhibition of profligacy and missed opportunity.

The LGPS should aspire to become an "expert client" of the market, capable of extracting best value from the financial services industry, and enjoying the many other benefits of scaling up.

4. COST UNDER-REPORTING: A FAILURE OF GOVERNANCE

Quantifying the cumulative impact of decades of cost under-reporting by the LGPS funds would be a depressing exercise; certainly £ billions. But more important is to understand the underlying causes. It has been facilitated by a dangerous cocktail of dismally lax, ineffective (amateur) governance and a culture of non-accountability, opacity, incompetence and indifference. This has accommodated decades of unchecked behaviour by a rapacious fund management industry (now surfacing: the Investment Association's internal ructions are no coincidence).

The Pensions Regulator (TPR) assumed responsibility for regulating public sector schemes in April 2015. Depressingly, after surveying half of public sector schemes over the summer, covering 85% of scheme members, it concluded that there is *a concerning picture of*

[8] For detail, see *The Local Government Pension Scheme: opportunity knocks*; Johnson, CPS, 2013.

Table 5: Reported fund management costs per member, 2014-15.

Rank	Local Authority	Fund mgt costs per member	Fund market value 31 March 2015 £000's	Fund mgt costs as bp
1	Harrow	-£0.3	£674,845	-0.1
2	West Yorkshire Super	£11.5	£11,319,225	2.6
3	South Yorkshire P Fund	£14.7	£6,277,138	3.3
4	Merton	£31.2	£541,572	6.1
5	East Riding of Yorkshire	£32.2	£3,677,391	8.8
85	London Pensions F Auth	£400.1	£4,617,208	67.4
86	Tyne and Wear Super	£444.3	£6,378,063	87.5
87	Hammersmith & Fulham	£457.8	£868,475	75.4
88	Flintshire UA	£483.4	£1,394,549	124.0
89	Cheshire	£506.2	£4,097,211	102.8
	Average	**£163.9**	**£2,404,812**	**37.1**

some public service schemes failing to engage fully with the requirements on governance and administration. Only 28% of schemes had a plan to comply with recent reforms, and less than half had reviewed arrangements against TPR's code of practice, published in January 2015.

This reality is in stark contrast with the declared intent of the LGPS's legislative cornerstone, the Local Government Act 1972. Section 151 of the Act requires that every local authority in England and Wales should *make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs*.

To-date, no Section 151 officer (often the Chief Financial Officer / Treasurer) has ever been held to account, notwithstanding their fiduciary responsibility to local taxpayers.[9] For a nation that is supposedly a leading provider of financial services, and given the scale of the LGPS, it is a national embarrassment. Culture change is required, but this could take another decade to materialise. Meanwhile, the LGPS is still years away from being able to evidence adherence to the old adage of *what gets measured gets managed…..*and decades too late.

5. CASHFLOW

5.1 Positive….for now

In the last financial year, fund income of £16 billion exceeded total fund expenditure by £3.1 billion; see Table 6. The improvement in cashflow in 2014-15 temporarily reversed a long term decline; it is a direct result of the implementation of Lord Hutton's reforms which, for the LGPS, came into effect in April 2014. But note that without that year's (taxpayer-funded) £833 million increase in employer contributions, the core net cashflow would have been *negative* £301 million. And while employee contributions increased by £108 million, every year they form a smaller proportion of total expenditure on benefits (34% in 2008-09, 23% in 2014-15), putting more pressure on taxpayers (and the need for investment income).

Note that this aggregated data masks serious cashflow problems within an increasing number of the individual funds: perhaps a third are already cashflow negative.

5.2 A cashflow crisis beckons

Crises tend to arise when, simultaneously, more than one independent component goes awry. Over the next decade, the LGPS faces a perfect storm.

[9] See *The role of the Chief Financial Officer in local government*; CIPFA, 2010.

Table 6: LGPS cashflow (aggregated for England and Wales)

£ million	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Total expenditure on benefits	-£5,981	-£6,733	-£7,190	-£8,026	-£8,005	-£8,388	-£8,856
Employee contributions	£2,054	£2,106	£2,099	£1,970	£1,917	£1,962	£2,070
Employer contributions	£5,809	£6,180	£6,378	£6,349	£6,181	£6,485	£7,318
Core net cashflow	**£1,882**	**£1,553**	**£1,287**	**£293**	**£93**	**£59**	**£532**
Investment income (gross)	£2,999	£2,690	£2,827	£3,191	£3,142	£3,338	£3,507
Net transfers and other	-£288	-£412	-£404	-£309	-£444	-£463	-£377
Total net cashflow	**£4,593**	**£3,831**	**£3,710**	**£3,175**	**£2,791**	**£2,934**	**£3,130**
Market value of funds, eoy	£103,418	£140,502	£152,012	£157,340	£178,193	£189,409	£214,028
Total net cashflow / market value	4.4%	2.7%	2.4%	2.0%	1.6%	1.5%	1.5%

Source: DCLG; SF3 data returns for England and Wales.

(a) Past under-funding

Today's large funding deficits are the result of decades of under-funding relative to the growth in the pension promise, aided and abetted by a history of actuarial underestimation of true costs (notably life expectancy) and excessively optimistic investment returns. Pension promises have historically been worth roughly 35% of salary, yet contributions have been only around 21%: pure Madoff economics.

Even with deficit recovery plans that are far more (timeframe) forgiving than would be permitted in the private sector, the weakest funds' deficits are now beyond repair. They are now consuming (i.e. selling) assets simply to meet pensions in payment. With no realistic prospect of recovery, they are probably in a death spiral, heading towards unfunded status.

Meanwhile, most funds are actively pursuing deficit recovery programmes, but perhaps the weakest of them should stop pretending that the objective is achievable? They are relying on some future investment performance miracle based upon "sophisticated" asset selection, concocted by expensive consultants: modern-day alchemy.

(b) Benign returns

A decade ago, the modelling team behind (Lord) Adair Turner's Pensions Commission assumed an annual real rate of return of 4% on a diversified asset pool.[10] This is dreamland in today's post-QE world of sclerotic returns. Indeed, to be prudent, we should assume a new norm of low real returns: even 2% should now be considered "aspirational".

Meanwhile, many funds are banking on higher fixed income yields to bail them out. Some are assuming that bond yields will mean revert to higher rates than implied by forward curves, utterly unrealistic given the collapse in long-term yields (including real yields). The prospects for investment income cashflow are not good.

(c) Squeezed employers

Employers participating in the LGPS are contributing, on average, roughly 14% of payroll to meet their share of on-going costs, plus some 7% to make up for past deficits. And although employer contributions rose by £833 million last year (i.e. up 13%), employers are under pressure to raise them further, not least because the deficits are still getting larger.

Some employer contributions are now over 30% of payroll (the 89 separate funds have different deficit levels); it is understandable that some employers want to leave the scheme. They are no longer prepared to chase deficits that they know are irretrievable, particularly deficits for which they are not responsible (perhaps only having recently joined the LGPS). Fewer employers means less cash inflow.

[10] After implicit costs but before explicit costs. See *A New Pension Settlement for the Twenty-First Century*; The Second Report of the Pensions Commission, 2005.

Table 7: LGPS membership and dependency ratio (England only)

Members ('000s)	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Contributing employees	1,617	1,638	1,656	1,685	1,684	1,633	1,567	1,586	1,668	1,758
Dependents: pensioners	973	1,019	1,049	1,088	1,131	1,187	1,253	1,288	1,344	1,401
deferred, other	851	942	1,056	1,151	1,249	1,335	1,429	1,518	1,618	1,687
Total	3,441	3,600	3,761	3,924	4,065	4,155	4,248	4,391	4,630	4,845
Dependents per contributor	1.13	1.20	1.27	1.33	1.41	1.54	1.71	1.77	1.78	1.76

(d) Destructive demographics

Consistent with the UK's general population, the LGPS membership is both living longer *and* ageing (Table 7), i.e. the dependency ratio is deteriorating: the LGPS is "mature".[11]

Cashflow inevitably deteriorates as the number of scheme dependents rises relative to the number of contributing members. In addition, ironically, the LGPS's cashflow is exacerbated by cost-cutting redundancies because they reduce the number of contributing workers (*and* some take early retirement).

(e) The end of contracting out

In April 2016, with the introduction of the single-tier State Pension, LGPS contributors will lose their National Insurance contributions (NICs) rebates, contracting out having ended with the demise of the second state pension (S2P). Employers' and employees' Class 1 NICs will increase by 3.4% and 1.4%, respectively [12], resulting in additional cost pressures for the former (by up to £1,264 per employee), and a reduction in take-home pay for the latter.

Private sector employers have been given a statutory override to amend scheme rules, to offset the increased costs of running DB schemes, without the consent of trustees. But the public sector is specifically excluded from this accommodation, so the additional cash cost to employers will be about £700 million per year.[13]

(f) Mis-aligned cost and income drivers

Following implementation of Lord Hutton's reforms (April 2014), the drivers of the LGPS's costs and income remain fundamentally misaligned. Pensions in payment, for example, continue to be indexed to CPI even if pay (and therefore contributions) are frozen, inevitably squeezing cashflow.

(g) A crippling accrual rate

One of the consequences of recent reforms is that the LGPS's accrual rate has been dramatically accelerated, from 1/80 to 1/60 (in 2008), and then to 1/49 (2014's Hutton reforms). Overall, this is a 63% increase, albeit with the loss of the 3/80 lump sum (in 2008). And while the calculation basis changed from final to career average salary (in 2014), the overall effect will manifest itself as additional cashflow strain.

(h) Grandfathering

In 2011, when negotiating Lord Hutton's proposals to reform public service pensions, the Government made a late concession to the unions, by offering ten year grandfathering.[14] This effectively rendered Lord Hutton's (cost-saving)

11 The number of contributing workers per scheme dependent (deferreds and pensioners) is falling, squeezing cashflow.

12 i.e. rising to 13.8% for employers and 12% for employees, for those earning between the Lower and Upper Earnings Limits (£5,824 to £43,004 p.a. for 2016-17).

13 Local Government Association; written evidence on the Pensions Bill, 2 July 2013.

14 Lord Hutton's reforms moved pensions from a final salary to a career average basis, effective from April 2014. "Grandfathering": transitional protection given to anyone within ten years of retirement.

Table 8: Unfunded public service pension schemes: the cashflow deficit

£ billion	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Outturn	£0.2	£1.1	£2.2	£3.1	£4.7	£5.6	£8.0	£10.2	£10.9

	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
OBR forecast	£12.5	£11.1	£11.2	£11.9	£12.7	£13.8

Source: OBR, Economic and Fiscal Outlook, Table 4.20: Total managed expenditure, March 2015 proposal's impotent for at least a decade, because it meant that no material cashflow savings will materialise until after 2024. It could ultimately be the LGPS's undoing.

It is worth noting that Lord Hutton quickly developed reservations about his own proposals: *"what we've seen is how very quickly the assumptions which underpinned my assessments of the long-term sustainability of public service pensions have been shown to be too optimistic. That is going to affect the sustainability of public sector pensions in a negative way."* [15]

5.3 Additional evidence of DB's demise

(a) Unfunded public sector schemes: the cashflow canary

Table 8 provides a hint as to the LGPS's cashflow future. It shows the net aggregated cashflow of all of the unfunded public service pension schemes (covering roughly 85% of employees). Ten years ago, pensions in payment were almost entirely met by contributions (from employers and employees), but a £11.1 billion shortfall is expected this year, rising to nearly £14 billion in four years' time. This cashflow gap has to be plugged by the Treasury, i.e. taxpayers. Unfunded (pay-as-you-go) schemes mask a classic case of kicking the can down the road.

(b) Private sector DB

The pending DB scheme cashflow crisis is not just a public sector phenomenon. Some 50% of FTSE 350 schemes are described as already being materially cashflow negative, or soon to become so.[16] Across the DB sector, schemes paid out £20 billion more in cash than they receive in contributions, an annual figure that is projected to increase to £100 billion by 2030 care of:

- reducing numbers of active members;
- increased closures resulting from rises in cost due to low long-term returns;
- national insurance costs increasing in line with the abolition of contracting-out;
- sponsor reluctance to inject cash into the scheme; and
- higher numbers of members transferring out under pension freedoms.[17]

Of the 86 FTSE 100 companies that have DB schemes (Table 9), only three now provide *any* form of DB pension provision as standard to new recruits: Diageo, Johnson Matthey and Morrisons.[18] None are final salary-based; they offer cash balance schemes. Tesco is in the process of closing its career average revalued earnings

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15 Interview with BBC Radio 4's World This Weekend, broadcast on 4 December 2011.

16 *The road to a resilient pension scheme; Hymans Robertson's Trustee Barometer 2015*, Nov. 2015.

17 Ibid.

18 *Accounting for pensions 2015; LCP's 22nd annual survey of FTSE 100 companies' pension disclosures*, 2015.

Table 9: Status of FTSE 100 company DB pension schemes

Not offering a DB scheme in the UK			14
Of the 86 DB schemes:	Closed to new entrants	83	
	Closed to all future accruals		23
	Cap on final salary increases		14
	No cap on final salary increases		36
	Open but not final salary-based		13
			100

("CARE") scheme, to both new entrants and to future accrual, and Royal Mail Group has just reported that it cannot afford to keep its DB scheme open beyond 2018.

In the universe of the UK's 6,000 DB schemes, only 13% are now open to new members (43% in 2006). Measured by current membership, only 22% remain open, with 62% now closed to new members and 16% closed to future accrual.[19]

De-risking continues apace, evidence of shortening investment horizons commensurate with scheme closure. In the last decade, the equity share of total assets fell from 61% to 33%, the gilt and fixed interest share rising from 28% to 48%. The "other investments" share of total assets is up from 11% to 19%.

The private sector's retreat from DB provision is fundamentally an issue of competitiveness, particularly in sectors where margins are tight and competitors do not provide DB schemes. Costing as much as one-third of salary, DB schemes are an expensive benefit that also introduce unwelcome volatility into companies' financial statements.

(c) Council tax

The overwhelming evidence from private sector DB schemes tells us that the LGPS is unsustainable. Evidence from a different perspective is equally unequivocal. In 2014-15, England's local authorities collected £24.1 billion in council tax; employers then contributed £6.8 billion to the LGPS, equivalent to 28% of collections. The Scottish data is £1.98 billion, some £900 million, and 45%, respectively. In all likelihood, contributions will have to go up, with adverse implications for local taxation or local services, or a combination thereof.

6. POLITICS AND THE MEDIA

Rising employer contributions will force already hard-pressed councils to make tougher choices in respect of their discretionary spending, with adverse implications for public services. Taxpayers, assisted by the media, will soon, if they have not done so already, connect deteriorating local services with a pensions-derived cashflow squeeze. Without substantial change, the LGPS risks ceding management control to the media. To be clear, this observation is based upon cashflow, not nebulous concepts such as point-in-time funding ratios, which do not manifest themselves in day-to-day life…..and therefore exert very little political pressure for change.

In addition, without a substantial restructuring, the evolving inequality between the LGPS and private sector pensions will continue unabated and, with it, the risk of societal division. Urgent action is needed but, in the meantime, the LGPS (and its sponsor, DCLG) increasingly risks ceding management control to the media.

A politically challenging U-turn is required. When the Government announced the Hutton-inspired reforms to public service pensions, Danny Alexander told the House of Commons that *"I believe that we will have a deal that can endure for at least 25 years, and hopefully longer."*[20] Fortunately this foolishness is not set in law.

7. WHERE TO NEXT FOR THE LGPS?

In his speech at October's Conservative Party conference, the Chancellor proposed the creation of up to six British Wealth Funds, perhaps to *replace* today's 89 LGPS funds (it was not clear). Allied to this were hints as to investing more into infrastructure ("get Britain building"). Further details were provided in November's Autumn Statement, when the Government

[19] *Figure 3.5, Purple Book 2015*; the Pension Protection Fund (PPF) and The Pensions Regulator.

[20] Danny Alexander, when Chief Secretary to the Treasury; House of Commons, 2 November 2011.

published some criteria for the pooling of investments.

Underlying the initiative are some laudable objectives, including generating some economies of scale and increasing the amount invested in infrastructure. The latter would socialise the benefit of the LGPS's huge assets across the whole of society; we all use airports, railways, roads and utilities.

But reconfiguring the LGPS as a few British Wealth Funds with an infrastructure bias will not address the fundamental issue that it is unsustainable. It will not ameliorate the pending cashflow crisis, nor repair the deficits. The author's next paper confronts this problem and proposes how to make the LGPS sustainable for the long term.

A note concerning data

The Local Government Pension Scheme (LGPS) is a single occupational pension scheme comprising 101 separate geographic funds (81 for England, eight for Wales, 11 for Scotland, and one for Northern Ireland). There is no aggregated scheme data, not least because the triennial valuations of the Scottish funds are conducted on a different annual cycle. In addition, the Northern Ireland fund reports separately. Consequently, this report pertains to the 89 funds in England and Wales. Were it based on all 101 funds, the conclusions and proposals would be no different.

APPENDIX 1: LGPS funds, England and Wales

Total reported costs per member for 2014-15, in ascending order

Rank	Local Authority	Total costs per member 2014-15	% change on 2013-14	Fund market value 31 March 2015 £000's
1	West Yorkshire Superannuation	£28.3	1.8%	£11,319,225
2	South Yorkshire Pensions Fund	£41.3	-1.2%	£6,277,138
3	East Riding of Yorkshire UA	£47.6	-7.0%	£3,677,391
4	Nottinghamshire	£52.8	-3.3%	£4,078,600
5	Tameside	£53.5	-12.4%	£17,591,201
6	Middlesbrough UA	£67.7	58.2%	£3,243,794
7	Harrow	£70.4	-19.0%	£674,845
8	Derbyshire	£70.5	-11.3%	£3,694,389
9	Lincolnshire	£72.7	2.2%	£1,750,942
10	Dorset	£73.4	6.0%	£2,301,132
11	Merton	£81.1	-41.2%	£541,572
12	North Yorkshire	£83.8	-13.4%	£2,399,869
13	Leicestershire	£84.4	-18.5%	£3,128,170
14	Cumbria	£85.8	-10.6%	£2,027,316
15	Windsor & Maidenhead UA	£91.8	15.8%	£1,649,769
16	Hertfordshire	£98.8	-13.4%	£1,963,058
17	Oxfordshire	£99.4	1.2%	£1,845,479
18	Lewisham	£102.5	-2.0%	£1,048,149
19	Carmarthenshire UA	£109.9	55.5%	£1,906,719
20	Greenwich	£116.5	1.4%	£1,056,702
21	Wiltshire	£119.3	47.0%	£1,852,603
22	Bedfordshire	£119.9	13.8%	£1,709,956
23	Merseyside Pension Fund	£121.8	-7.2%	£6,862,704
24	Northumberland	£123.4	0.3%	£1,067,121
25	Somerset	£124.6	36.4%	£1,595,212
26	Rhondda Cynon Taff UA	£126.6	7.1%	£2,410,321
27	Devon	£127.2	19.6%	£3,374,426
28	Islington	£129.0	15.6%	£1,087,055
29	Kent	£130.5	-18.6%	£4,539,037
30	Northamptonshire	£132.9	29.6%	£1,849,740
31	Gloucestershire	£141.2	0.9%	£1,709,074
32	Hampshire	£141.7	45.5%	£5,137,088
33	Enfield	£141.7	16.6%	£888,155
34	Durham	£142.0	5.2%	£2,334,975
35	Cambridgeshire	£142.7	29.7%	£2,264,187
36	Staffordshire	£143.0	15.4%	£3,768,709
37	Hounslow	£145.9	-11.4%	£803,014
38	Haringey	£149.0	27.6%	£1,045,355
39	East Sussex	£152.9	1.6%	£2,746,549
40	Richmond upon Thames	£154.8	1.5%	£607,280
41	Cornwall	£158.9	89.4%	£1,522,243
42	Cardiff UA	£158.9	9.7%	£1,653,151
43	Redbridge	£161.7	4.1%	£636,282
44	West Midlands PTA	£168.3	26.8%	£474,886
45	Warwickshire	£170.4	-3.4%	£1,638,059
46	Tower Hamlets	£171.1	-7.4%	£1,091,327
47	Worcestershire	£176.2	9.8%	£3,581,039
48	Torfaen UA	£176.6	19.2%	£2,276,999
49	West Sussex	£177.4	19.2%	£2,972,669
50	Barking & Dagenham	£178.0	-9.3%	£757,822
51	Ealing	£185.8	6.9%	£967,496
52	Lambeth	£186.5	16.2%	£1,136,522
53	Norfolk	£190.6	-7.2%	£2,948,870
54	Havering	£190.7	58.7%	£574,669
55	Barnet	£193.9	60.3%	£911,724
56	Surrey	£194.6	24.2%	£3,193,520
57	Croydon	£194.9	13.3%	£858,779
58	Bexley	£198.3	7.4%	£671,951
59	Bromley	£201.3	24.8%	£741,975
60	Powys UA	£201.8	2.3%	£502,898
61	Hackney	£204.2	9.6%	£1,146,793
62	Bath & North East Somerset	£211.8	4.5%	£3,839,316
63	Essex	£213.2	19.8%	£4,932,623
64	Wandsworth	£222.8	17.1%	£1,205,812
65	Isle of Wight UA	£224.0	17.9%	£482,669
66	Southwark	£227.5	-0.8%	£1,247,731
67	Swansea UA	£228.9	-34.3%	£1,537,706
68	Suffolk	£229.1	32.4%	£2,198,441
69	Lancashire	£231.2	120.9%	£5,830,674
70	Gwynedd	£247.8	-1.0%	£1,497,373
71	Buckinghamshire	£248.1	102.8%	£2,188,549
72	Sutton	£274.4	94.9%	£506,786
73	Kingston upon Thames	£287.4	27.5%	£646,311
74	West Midlands Pension Fund	£311.0	426.0%	£11,464,000
75	Shropshire	£319.9	4.3%	£1,512,735
76	Hillingdon	£335.4	51.9%	£802,300
77	Kensington & Chelsea	£359.5	-6.5%	£825,896
78	South Yorkshire PTA	£379.4	-0.7%	£212,424
79	Newham	£382.3	126.2%	£1,068,417
80	Brent	£387.1	134.3%	£657,050
81	City of London	£393.4	20.6%	£823,744
82	Camden	£422.3	12.2%	£1,265,449
83	Waltham Forest	£437.2	-9.5%	£742,177
84	Westminster	£439.3	80.3%	£1,096,916
85	Tyne and Wear Superannuation	£462.7	364.4%	£6,378,063
86	London Pensions Fund Auth	£487.2	3.7%	£4,617,208
87	Hammersmith & Fulham	£504.5	29.5%	£868,475
88	Flintshire UA	£511.4	140.9%	£1,394,549
89	Cheshire	£530.3	71.5%	£4,097,211
	Average	**£197.7**	**28.0%**	**£2,404,812**

APPENDIX 2: LGPS funds, England and Wales

Total reported costs per member, ranked by % change on 2013-14

	Local Authority	Total costs per member 2013-14	2014-15	% change on 2013-14
1	Merton	£137.8	£81.1	-41.2%
2	Swansea UA	£348.3	£228.9	-34.3%
3	Harrow	£86.9	£70.4	-19.0%
4	Kent	£160.4	£130.5	-18.6%
5	Leicestershire	£103.5	£84.4	-18.5%
6	Hertfordshire	£114.2	£98.8	-13.4%
7	North Yorkshire	£96.8	£83.8	-13.4%
8	Tameside	£61.1	£53.5	-12.4%
9	Hounslow	£164.6	£145.9	-11.4%
10	Derbyshire	£79.4	£70.5	-11.3%
11	Cumbria	£96.0	£85.8	-10.6%
12	Waltham Forest	£483.0	£437.2	-9.5%
13	Barking & Dagenham	£196.3	£178.0	-9.3%
14	Tower Hamlets	£184.8	£171.1	-7.4%
15	Norfolk	£205.4	£190.6	-7.2%
16	Merseyside Pension Fund	£131.3	£121.8	-7.2%
17	East Riding of Yorkshire UA	£51.2	£47.6	-7.0%
18	Kensington & Chelsea	£384.5	£359.5	-6.5%
19	Warwickshire	£176.4	£170.4	-3.4%
20	Nottinghamshire	£54.6	£52.8	-3.3%
21	Lewisham	£104.6	£102.5	-2.0%
22	South Yorkshire Pensions Fund	£41.8	£41.3	-1.2%
23	Gwynedd	£250.4	£247.8	-1.0%
24	Southwark	£229.3	£227.5	-0.8%
25	South Yorkshire PTA	£382.0	£379.4	-0.7%
26	Northumberland	£123.0	£123.4	0.3%
27	Gloucestershire	£139.9	£141.2	0.9%
28	Oxfordshire	£98.2	£99.4	1.2%
29	Greenwich	£114.9	£116.5	1.4%
30	Richmond upon Thames	£152.5	£154.8	1.5%
31	East Sussex	£150.5	£152.9	1.6%
32	West Yorkshire Super. Fund	£27.8	£28.3	1.8%
33	Lincolnshire	£71.1	£72.7	2.2%
34	Powys UA	£197.3	£201.8	2.3%
35	London Pensions Fund Auth	£469.9	£487.2	3.7%
36	Redbridge	£155.3	£161.7	4.1%
37	Shropshire	£306.7	£319.9	4.3%
38	Bath & North East Somerset	£202.6	£211.8	4.5%
39	Durham	£134.9	£142.0	5.2%
40	Dorset	£69.2	£73.4	6.0%
41	Ealing	£173.8	£185.8	6.9%
42	Rhondda Cynon Taff UA	£118.1	£126.6	7.1%
43	Bexley	£184.6	£198.3	7.4%
44	Hackney	£186.3	£204.2	9.6%
45	Cardiff UA	£144.9	£158.9	9.7%
46	Worcestershire	£160.4	£176.2	9.8%
47	Camden	£376.3	£422.3	12.2%
48	Croydon	£172.1	£194.9	13.3%
49	Bedfordshire	£105.4	£119.9	13.8%
50	Staffordshire	£123.9	£143.0	15.4%
51	Islington	£111.6	£129.0	15.6%
52	Windsor & Maidenhead UA	£79.3	£91.8	15.8%
53	Lambeth	£160.5	£186.5	16.2%
54	Enfield	£121.6	£141.7	16.6%
55	Wandsworth	£190.2	£222.8	17.1%
56	Isle of Wight UA	£189.9	£224.0	17.9%
57	West Sussex	£148.9	£177.4	19.2%
58	Torfaen UA	£148.2	£176.6	19.2%
59	Devon	£106.4	£127.2	19.6%
60	Essex	£178.0	£213.2	19.8%
61	City of London	£326.1	£393.4	20.6%
62	Surrey	£156.7	£194.6	24.2%
63	Bromley	£161.3	£201.3	24.8%
64	West Midlands PTA	£132.8	£168.3	26.8%
65	Kingston upon Thames	£225.5	£287.4	27.5%
66	Haringey	£116.8	£149.0	27.6%
67	Hammersmith & Fulham	£389.7	£504.5	29.5%
68	Northamptonshire	£102.5	£132.9	29.6%
69	Cambridgeshire	£110.0	£142.7	29.7%
70	Suffolk	£173.1	£229.1	32.4%
71	Somerset	£91.4	£124.6	36.4%
72	Hampshire	£97.4	£141.7	45.5%
73	Wiltshire	£81.2	£119.3	47.0%
74	Hillingdon	£220.7	£335.4	51.9%
75	Carmarthenshire UA	£70.7	£109.9	55.5%
76	Middlesbrough UA	£42.8	£67.7	58.2%
77	Havering	£120.1	£190.7	58.7%
78	Barnet	£120.9	£193.9	60.3%
79	Cheshire	£309.2	£530.3	71.5%
80	Westminster	£243.6	£439.3	80.3%
81	Cornwall	£83.9	£158.9	89.4%
82	Sutton	£140.8	£274.4	94.9%
83	Buckinghamshire	£122.4	£248.1	102.8%
84	Lancashire	£104.7	£231.2	120.9%
85	Newham	£169.0	£382.3	126.2%
86	Brent	£165.2	£387.1	134.3%
87	Flintshire UA	£212.3	£511.4	140.9%
88	Tyne and Wear Super. Fund	£99.7	£462.7	364.4%
89	West Midlands Pension Fund	£59.1	£311.0	426.0%
	Average	**£161.5**	**£197.7**	**28.0%**

APPENDIX 3: LGPS funds, England and Wales

Reported fund management costs per member for 2014-15, in ascending order

Rank	Local Authority	Fund mgt costs per member	Fund market value 31 March 2015 £000's	Fund mgt costs as bp
1	Harrow	-£0.3	£674,845	-0.1
2	West Yorkshire Super	£11.5	£11,319,225	2.6
3	South Yorkshire P Fund	£14.7	£6,277,138	3.3
4	Merton	£31.2	£541,572	6.1
5	East Riding of Yorkshire	£32.2	£3,677,391	8.8
6	Nottinghamshire	£32.8	£4,078,600	9.4
7	Tameside	£39.0	£17,591,201	7.5
8	Dorset	£42.5	£2,301,132	12.0
9	Middlesbrough UA	£44.2	£3,243,794	9.3
10	Derbyshire	£52.4	£3,694,389	12.8
11	Lincolnshire	£53.2	£1,750,942	20.1
12	Lewisham	£62.1	£1,048,149	13.8
13	Cumbria	£63.0	£2,027,316	16.4
14	North Yorkshire	£65.8	£2,399,869	23.1
15	Islington	£66.3	£1,087,055	12.0
16	Leicestershire	£68.1	£3,128,170	18.2
17	Oxfordshire	£69.3	£1,845,479	20.5
18	Windsor & Maidenhead U	£75.9	£1,649,769	27.3
19	Hertfordshire	£79.4	£1,963,058	22.6
20	Greenwich	£81.2	£1,056,702	15.3
21	Northumberland	£83.1	£1,067,121	19.1
22	Carmarthenshire UA	£88.2	£1,906,719	20.1
23	Wiltshire	£93.0	£1,852,603	29.9
24	Northamptonshire	£93.3	£1,849,740	28.8
25	Somerset	£94.8	£1,595,212	31.7
26	Rhondda Cynon Taff UA	£99.1	£2,410,321	26.0
27	Bedfordshire	£101.8	£1,709,956	35.2
28	Cambridgeshire	£103.7	£2,264,187	31.8
29	Merseyside P Fund	£105.4	£6,862,704	19.7
30	Kent	£106.8	£4,539,037	29.7
31	Enfield	£108.8	£888,155	20.5
32	Haringey	£111.1	£1,045,355	23.1
33	Hounslow	£111.8	£803,014	27.5
34	Barnet	£112.7	£911,724	28.8
35	Devon	£113.3	£3,374,426	32.9
36	Staffordshire	£117.0	£3,768,709	32.1
37	Durham	£117.8	£2,334,975	24.4
38	Ealing	£118.0	£967,496	25.7
39	Gloucestershire	£118.5	£1,709,074	34.0
40	Richmond upon Thames	£119.0	£607,280	22.9
41	Redbridge	£122.5	£636,282	29.2
42	Croydon	£122.8	£858,779	32.8
43	Hampshire	£125.5	£5,137,088	35.3
44	East Sussex	£127.6	£2,746,549	30.5
45	Tower Hamlets	£128.9	£1,091,327	22.4
46	West Midlands PTA	£130.9	£474,886	14.3
47	Lambeth	£135.4	£1,136,522	23.7
48	Cardiff UA	£137.2	£1,653,151	30.1
49	Warwickshire	£141.5	£1,638,059	37.4
50	Cornwall	£144.8	£1,522,243	45.4
51	Bexley	£145.5	£671,951	28.6
52	Torfaen UA	£145.6	£2,276,999	34.0
53	Powys UA	£148.2	£502,898	47.6
54	Barking & Dagenham	£149.4	£757,822	32.8
55	Worcestershire	£152.5	£3,581,039	39.1
56	Havering	£157.8	£574,669	48.0
57	Bromley	£158.0	£741,975	33.6
58	West Sussex	£158.4	£2,972,669	35.5
59	Norfolk	£164.7	£2,948,870	43.6
60	Hackney	£174.6	£1,146,793	32.9
61	Surrey	£177.3	£3,193,520	49.7
62	Bath & NE Somerset	£182.7	£3,839,316	45.8
63	Southwark	£185.0	£1,247,731	29.3
64	Essex	£194.1	£4,932,623	53.1
65	Isle of Wight UA	£194.7	£482,669	51.7
66	Wandsworth	£197.8	£1,205,812	28.4
67	Swansea UA	£202.4	£1,537,706	49.2
68	Lancashire	£208.1	£5,830,674	54.7
69	Suffolk	£210.1	£2,198,441	50.3
70	Sutton	£211.6	£506,786	49.2
71	Gwynedd	£216.9	£1,497,373	54.1
72	Kingston upon Thames	£217.5	£646,311	43.7
73	Buckinghamshire	£224.6	£2,188,549	64.6
74	South Yorkshire PTA	£292.0	£212,424	29.2
75	Hillingdon	£294.2	£802,300	74.7
76	West Midlands P Fund	£295.5	£11,464,000	71.6
77	Shropshire	£301.0	£1,512,735	82.3
78	Kensington & Chelsea	£315.6	£825,896	39.7
79	City of London	£337.8	£823,744	49.7
80	Newham	£348.3	£1,068,417	78.6
81	Brent	£350.8	£657,050	105.0
82	Camden	£385.9	£1,265,449	56.0
83	Waltham Forest	£386.7	£742,177	93.9
84	Westminster	£391.6	£1,096,916	57.3
85	London Pensions F Auth	£400.1	£4,617,208	67.4
86	Tyne and Wear Super	£444.3	£6,378,063	87.5
87	Hammersmith & Fulham	£457.8	£868,475	75.4
88	Flintshire UA	£483.4	£1,394,549	124.0
89	Cheshire	£506.2	£4,097,211	102.8
	Average	**£163.9**	**£2,404,812**	**37.1**

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