

Report to: Pension Board

Date: 9 September 2019

By: Chief Finance Officer

Title of report: Local Government Pension Scheme (LGPS) Regulatory Update

Purpose of report: To provide the Board with an update on the current regulatory environment, and consultations that could impact the Local Government Pension Scheme.

RECOMMENDATION

The Board is recommended to consider and comment on the report.

1. Background

1.1 There are a range of ongoing consultations and discussions concerning the Local Government Pension Scheme (LGPS) and any proposed regulatory matters that could affect scheme administration. This includes responses to consultations that have been made.

1.2 The appendices to this report sets out updates in relation to the topics below, which are currently underway or completed within the LGPS:

- Good Governance in the LGPS;
- The Pensions Regulator (TPR) Public service governance and administration survey 2018;
- Response to the Changes to the local valuation cycle consultation.

2. Good Governance Review

2.1 At the June meetings of both the Pension Board and Pension Committee, members considered various updates under the LGPS Regulatory Updates, including the Good Governance Review; and that the LGPS Scheme Advisory Board (SAB) in England and Wales has commissioned Hymans Robertson to facilitate a consultation with LGPS stakeholders on governance structures and to examine the effectiveness of current LGPS governance models, including considering alternatives or enhancements to existing models which can strengthen LGPS governance.

2.2 SAB has now published its report (attached as Appendix 1), which sets out the outcomes of the survey; recognising strengths and weaknesses in all governance models; and proposing that an outcomes-based approach would be the most effective method of improving governance, rather than mandating a single governance structure for all. This allows pension funds to continue doing what currently works well while still ensuring the highest governance standards across the scheme.

2.3 The summary of the proposals are as follows:

- Outcomes-based approach to LGPS governance with minimum standards rather than a prescribed governance structure;
- Critical features of the 'outcome-based' model to include –
 - Robust conflict management, including clarity on roles and responsibilities for decision making;
 - Assurance on sufficiency of administration and other resources (quantity and competency), and appropriate budget;
 - Explanation of policy on employer and scheme member engagement, and representation in governance

- Regular independent review of governance – this should be based on an enhanced governance compliance statement which should explain how the required outcomes and delivered.
- Enhanced training requirement for S151s and Pension Committee members (requirement of Pension Committee should be on a par with the Pension Board members).
- Update relevant guidance and better sign-posting.

2.4 The Scheme Advisory Board has now invited the Hymans Robertson project team to assist the Secretariat in taking forward the next stage of the good governance project. Two working groups will be established, one to focus on defining good governance outcomes and the guidance needed to clearly set them out; and the other to focus on options for the independent assessment of outcomes and mechanisms to improve the delivery of those outcomes. Both groups will comprise a wide range of scheme stakeholders to ensure a full range of views and options are considered. The aim is for an options report to be ready for the Board's consideration it meets in November. Any proposals agreed by the Board would be subject to a full stakeholder consultation before being put to Ministry of Housing, Communities and Local Government (MHCLG).

3. The Pensions Regulator Annual Governance and Administration Survey 2018

3.1 The 2018 Annual Governance and Administration Survey for public service pension schemes has been published (Appendix 2) by The Pensions Regulator (TPR). The key observations are:

- *Foundation blocks in place* - The report indicates that the vast majority of LGPS funds have now got, at the very least, the basic governance and administration foundations, such as Local Pension Boards, risk registers and data improvement plans, in place.
- *Administration matters* - Appreciation of the importance of scheme administration has increased, but there is still much more focus needed in this area from Pension Committees and Pension Boards, both of which have a big role to play. TPR commented that it is imperative that Pension Boards cover administration issues on every agenda, particularly those that are persistent or emerging.
- *It's all about data* - Not surprisingly the importance of member data runs throughout the report. TPR's expectation is for improvement plans to be in place and funds to continue the push towards full electronic data submissions from all employers.
- *Cyber security, keep vigilant!* - Cyber security has its own separate section within the report and TPR wants to ensure public service pension schemes give this issue due prominence in the running of the scheme.
- *TPR role now clearer and more relevant* - The role and perception of TPR is one that it is both visible and respected but falls down in the area of being tough and decisive. Nevertheless, TPR has been seen as a strong driver in increasing good governance and raising administration standards and performance across public service pension schemes.

3.2 The report is an important insight into the wider LGPS governance and administration landscape. Encouragingly they have seen year on year improvements across every category. But, as ever, TPR does not expect schemes to rest on their laurels – continuous improvement and development is still expected. TPR is quick to state that this is merely the start of the journey to improve governance and administration standards and has said it will use its 2018 survey results to inform future regulatory initiatives and schemes will continue to see greater engagement from TPR.

4. Response to the Consultation on changes to the local valuation cycle

4.1 The Board recently considered the MHCLG policy consultation called 'LGPS: Changes to the local valuation cycle and the management of employer risk policy'. The consultation contains proposals on a number of matters relating to the LGPS in England and Wales. Amongst these, it is proposed to amend the local fund valuation cycle of the LGPS from the current three year (triennial)

cycle to a four year (quadrennial). The Government consultation is intended to ensure that scheme and local valuations are aligned. *The closing date for responses was 31 July 2019.*

4.2 The East Sussex Pension Fund (ESPF or “the Fund”) response is attached as Appendix 3 focusing on the proposed number of changes. This includes the proposal to move the local valuation cycle (which sets employer contributions) from triennial to quadrennial, with the aim of aligning with the scheme valuations (carried out by the Government Actuary Department for cost management purposes). Although the rationale is weak when considered from a local, funding perspective, MHCLG does, however, appear to recognise this and has proposed a number of potential mitigations, including interim valuations.

4.3 ESPF’s response also addresses what has proved to be a material oversight in the introduction of the requirement to repay an exit credit to an outgoing employer, i.e. the failure to allow administering authorities to consider any risk sharing or other arrangements which are not consistent with any surplus being repaid on exit. Many administering authorities have put exit credits on hold, but clarity will be needed on what should happen where exit credits have already been paid but where risk sharing arrangements were in place – will steps need to be taken to reclaim these payments?

5. Competition and Markets Authority order

5.1 The Competition and Markets Authority (CMA) has established new requirements affecting LGPS funds. There is now a requirement for the Fund to establish investment consultant’s objectives that are linked to the Fund longer-term investment objectives. There may also be wider reaching implications of the Order, including how some of the new pooling arrangements might be viewed and what advice will be deemed as being regulated.

5.2 The changes follow an investigation by the CMA into the investment consultancy market which found weaknesses, including trustees entering into uncompetitive terms or failing to switch to potentially better providers because they struggled to compare fees and performance.

5.3 Following this new requirement, TPR has published a consultation (Appendix 4) on new guidance to support tougher rules on investment governance. This consultation appears to reflect a position of the LGPS only being in scope for CMA remedy 7 - the obligation to set strategic objectives for investment consultants. The consultation runs until midday on 11 September and involves guidance for a pension committee on how to choose an investment model, how to set objectives for those providing investment advice to the committee, and how to run competitive tenders before appointing investment consultancy services. SAB has also produced a briefing note (Appendix 5) on the CMA Order and its impact on the LGPS taking into account the currently understood position that only remedy 7 will apply to the LGPS.

5.4 The Pension Board and Pension Committee will need to establish objectives for consultants by no later than 10 December 2019. To support this, Hymans Robertson will be raising awareness of the new requirements and initiating discussions around potential objectives, after which a logical progression would be to consider setting objectives for all key service providers.

6. The LGPS Community

6.1 The Local Government Association (LGA) has published a new document called ‘the LGPS Community’ attached as Appendix 6. The document was produced in response to a request from the Local Government Pensions Committee (LGPC). The purpose of the document is to explain the relationship between the different bodies that make up the LGPS community. The document will be particularly helpful to Pension Committee and Pension Board members, as well as administration staff, in explaining how their role fits in to the wider LGPS community.

7. Conclusion and reasons for recommendation

7.1 The Board is recommended to consider and comment on the report.

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BACKGROUND DOCUMENTS

None