

**Report to:** Governance Committee

**Date of meeting:** 24 January 2023

**By:** Chief Finance Officer

**Title:** East Sussex Pension Fund – Review of Pension Committee membership

**Purpose:** To consider whether changes should be made to the structure of Pension Committee to provide wider representation to Pension Fund decision making

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## **RECOMMENDATIONS**

**The Governance Committee is recommended**

- 1. maintain the current Pension Committee membership requirements after considering full legal advice in the exempt report**
  - 2. review the Pension Committee membership requirements following any change in the law**
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### **1. Background**

- 1.1 The Pension Board of the East Sussex Pension Fund (the Fund) received a report on 27 May 2022 regarding representation on the Pension Committee following a paper by one of the Employer Representatives requesting representation of Brighton & Hove City Council (BHCC) on the Pension Committee as the second largest employer in the Fund suggesting the addition of two BHCC Councillors. At the same time the Pension Board heard from a member of the public following a petition being presented to the Chairman before the Full Council meeting on 10 May 2022 with 450 signatures, calling for BHCC to have representation on the Pension Committee. The report to Pension Board is available at <https://democracy.eastsussex.gov.uk/ieListDocuments.aspx?CId=374&MId=5157&Ver=4>.
- 1.2 Following discussion and a vote of 2:1, with one abstaining and two members absent, the Pension Board requested that a report be taken to the Governance Committee for consideration as to whether a change to the Constitution should be implemented in relation to the membership structure of the Pension Committee for wider representation.
- 1.3 Having looked at the issues raised by BHCC, in particular the legal framework in which an LGPS Pension Fund must operate, it is recommended that there should not be a change the Pension Committee arrangements. In any event, notwithstanding the limitations presented by the current legal framework, it is considered that the current arrangements work well. Overall governance ensures that the views of the Scheme

Members and Scheme Employers are taken into account through the Pension Board, Annual Employers' Forum, Surveys and redesigned website.

- 1.4 Should the current statutory regime change then the effect of these changes and the implications on the Fund would be considered having regard to the advice and guidance provided by the Scheme Advisor Board and the Department of Levelling Up Housing and Communities. The paper sets out in detail the work undertaken to reach this conclusion.

## **2. ESCC as Administering Authority**

- 2.1 Regulation 2(2) of the Local Government Pension Scheme (LGPS) Regulations 2013 (2013 Regulations) provides: "The Scheme Manager responsible for the local administration of pensions and other benefits payable under these Regulations is referred to in these Regulations as the "administering authority"."
- 2.2 Regulation 53(1) of the 2013 Regulations provides that: "The bodies listed in Part 1 of Schedule 3, referred to in these Regulations as "administering authorities", must maintain a pension fund for the Scheme."
- 2.3 Part 1 of Schedule 3 provides "The following bodies are required to maintain a pension fund and are administering authorities for the purposes of these Regulations— (a) a county council in England;" among other specific bodies.
- 2.4 ESCC is explicitly stated in Part 2 of Schedule 3 as Administering Authority for LGPS administration for ESCC and BHCC.

## **3. Pension Committee membership and role**

- 3.1 Under the ESCC Constitution, the Pension Committee has delegated authority to exercise the powers of the County Council in respect of all powers and duties in relation to its functions as the Scheme Manager and Administering Authority for the Fund.
- 3.2 The County Council appoints five members to the Pension Committee in accordance with political balance provisions contained in s.15 Local Government and Housing Act (LGHA) 1989. These provisions require that the make-up of the Committee is in line with the political balance of the Local Authority.
- 3.3 The prime duty of the Pension Committee is to act in the best financial interest of the Fund's beneficiaries, i.e. Scheme Members. Scheme members make contributions to the Fund in the course of their employment, and as a result of this, it was found by the Supreme Court that members' pensions represent deferred pay, hence the assets invested by the Fund are those of the beneficiaries and not of any other stakeholder.
- 3.4 The views of other parties, whether scheme employers, taxpayers, or Scheme Members themselves cannot supersede the ultimate obligation of the Pension

Committee to decide strategic investment matters itself, with the aim to provide the best long term investment return for Scheme Members.

- 3.5 In the LGPS, the assets of the Fund are owned solely by the Administering Authority (as named by the LGPS Regulations 2013), not by the beneficiaries, employers or other stakeholders. This is confirmed in opinion by Nigel Giffin QC in October 2016 to the Local Government Association (LGA), who advises that the assets of the Fund legally and beneficially belong to the administering authority and do not 'belong to another person' despite the administering authority, through its Pension Committee, owing fiduciary duties to Scheme Members and indirectly to scheme employers.
- 3.6 Whilst ESCC is also a scheme employer, the appointment of the Pension Committee is under the capacity of ESCC as Administering Authority and, as such, the Committee members are not appointed as scheme employer representatives but representatives of the Administering Authority to act on behalf of all Scheme members and employers. This is made expressly clear in the Pension Committee Terms of Reference where it states "No matters relating to East Sussex County Council's responsibilities as an employer participating within the East Sussex Pension Fund are delegated to the Pension Committee". The members of the Pension Committee are required to consider "views expressed by employing organisations and staff representatives in relation to the operation of the East Sussex Pension Fund" but are not permitted to take decisions in order to benefit any particular employer ahead of the overall interests of the Fund".
- 3.7 Whilst all Committee Members bring with them their own knowledge and experience, political views should form no part of the consideration of issues or of the decision-making process.

#### **4. Representation**

- 4.1 Under the LGPS Regulations there are compliance standards against which LGPS administering authorities are to measure their governance arrangements which include the requirement that all key stakeholders are afforded the opportunity to be represented. within the main or secondary committee structure. These include: - i) employing authorities (including non-scheme employers, e.g., admitted bodies). ii) scheme members (including deferred and pensioner scheme members), iii) where appropriate, independent professional observers, and iv) expert advisors (on an ad-hoc basis). In addition it is required that where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision-making process, with or without voting rights. The wording of the compliance standards was prior to the statutory creation of the Pension Boards in 2015.
- 4.2 The Fund had 134 scheme employers and 81,291 scheme members as at 31 March 2022, scheme members live across the world.
- 4.3 One of the arguments raised as part of the Pension Board consideration was that residents of BHCC have no democratic oversight over the local government pension scheme in the same way that other residents in ESCC have. As noted above in 3.5,

the assets of the Fund are owned solely by the Administering Authority not by the beneficiaries, employers or other stakeholders (e.g. residents). The scheme is not open to residents of any locality, it is part of the remuneration package of those individuals whose work gives them entitlement of access to the LGPS. The Fund and the Administering Authority has no fiduciary duty to residents of any locality and, as such, there is no representation in any form of “residents” in either the Pension Committee or Pension Board structure. The fiduciary duty of the Fund is to the beneficiaries of the scheme. More than 20% of the scheme members live outside both ESCC and BHCC constituencies. As noted in 3.6 Pension Committee members are appointed to act on behalf of all Scheme members and employers and not represent the views of ESCC, while political views must not form part of decision making.

- 4.4 The Fund currently provide representation through the Pension Board which has three employer representatives, a Councillor representative from Brighton and Hove City Council, a Councillor to represent the Borough and District Councils and the third representative from the wider employer base. Scheme Member representatives include two union members, who are active members of the Fund, and a pensioner member. The Board also has an independent chair. All appointments are made by the ESCC Governance Committee under delegated authority.
- 4.5 The independent Chair of Pension Board is invited to attend all Pension Committee meetings and comment on all papers during the meeting; the independent Chair is invited to stay for the exempt section of Committee meetings also (this is at the agreement of the Pension Committee at each meeting rather than in the Terms of Reference). The Pension Board minutes are the first item of the Pension Committee agenda so feedback from the Pension Board can be taken into account by the Pension Committee on all items outside of investments. Other Pension Board members are welcome to attend as a member of the public to the Pension Committee.
- 4.6 The Chair of the Pension Committee attends Pension Board meetings on the request of the Pension Board; other Pension Committee members are also invited to attend, and they do often sit in.
- 4.7 In addition to the Pension Committee and Pension Board, the Fund has a number of working groups to help develop, progress and monitor specific areas of work such as administration, communications and the McCloud project. There is also an investment implementation working group to implement investment decisions made by the Pension Committee, and to carry out research to present to the Pension Committee for decision making; membership is open only to Fund Officers and advisers, with the Chair of the Pension Committee invited to sit in.
- 4.8 The Pension Committee discusses the same papers as the Pension Board, other than investment items, with the Pension Committee also approving the budget and accounts of the Fund. The Pension Board has the opportunity to comment on the budget in its meetings in advance of the Pension Committee prior to the decision making and is involved in discussions in advance of the approval of the Funding Strategy.

- 4.9 As laid out in the Communications Strategy, there are several routes for communication with the Fund for Scheme Members. In addition to the representation of the Scheme Members on the Pension Board, the Fund also carries out surveys with members to get feedback on the administration of the Fund; the results of the recent surveys are published on the Fund website and issues regular newsletters. The Pensions Administration team and Pensions Helpdesk also provide direct support and information to individual members. The Fund engage with scheme employers through an annual employer forum event, quarterly newsletters, an engagement team designated to support employers and direct communications and consultations. The Funds website has undergone substantial development to improve the communications with scheme members, employers and wider stakeholders including changes in response to their suggestions and provide additional information where needed as well as making information more accessible.

## **5. Regulations**

- 5.1 The Fund obtained legal advice from Eversheds on the regulations that are in place that set the rules under how a Local Authority Committee must be structured, alongside King's Council opinion that has been published on the Governance structures of the LGPS.
- 5.2 In the advice obtained, the lawyers advise there is no requirement for scheme employers or scheme members to be represented on a Pension Committee. The Administering Authority must however evidence that the Pension Committee is meeting its roles and functions as set out in the Terms of Reference, including seeking and considering views expressed by employing organisations and staff representatives in relation to the operation of the Fund.
- 5.3 There is a statutory obligation for membership of Local Authority Committee's to be allocated in accordance with the rules under s15 of LGHA 1989 and the Local Government (Committees and Political Groups) Regulations 1990 which provide for representation of different political groups on committees and to reflect the political balance of ESCC.
- 5.4 Key regulations to note are -
- 5.4.1 The Pension Committee is a committee of ESCC which has been appointed under local government legislation in order to discharge the functions of ESCC as Administering Authority for the Fund. As a local government committee, the membership of the Pension Committee is therefore subject to local government legislation. Section 101 of the Local Government Act 1972 (the "1972 Act") provides express powers for a local authority to arrange for the discharge of their functions by a committee, a sub-committee or an officer of the authority (or by any other local authority).
- 5.4.2 The functions of the Pension Committee (under Regulation 53 of the 2013 Regulations) are to maintain a pension fund in relation to the Scheme and to be responsible for managing and administering the Scheme.

- 5.4.3 Under the Local Authorities (Functions and Responsibilities) (England) Regulations 2000, statutory decisions taken under schemes made under sections 7, 12 or 24 of the Superannuation Act 1972, are not the responsibility of the Executive therefore the Pension Committee must be a non-executive committee.
- 5.4.4 Section 102(3) of the Local Government Act 1972 provides that membership of a committee may include persons who are not members of the local authority other than if the committee is appointed to regulate and control the finance of the local authority or of their area.
- 5.4.5 The LGA commissioned two pieces of advice firstly from James Goudie QC in December 2015 which states that “A committee concerned with LGPS investments may be regarded as regulating and controlling the finance of the local authority”; and secondly, that of Nigel Giffin QC in October 2016 in which Mr Giffin opines that the assets of the Fund legally and beneficially belong to the administering authority and do not ‘belong to another person’ despite the administering authority owing fiduciary duties to scheme employers and members.
- 5.4.6 The administering authority is required to comply with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 in performing its functions, which require it to take proper advice on investment matters.
- 5.5 Based on the regulations and published QC opinion, the Fund’s legal advisors suggest that in light of the Terms of Reference (TOR) and governance structure of the Pension Fund, the Pension Committee has been appointed to “regulate and control the finance of the local authority or area” and, as such, non-ESCC councillors would not be permitted to be allowed to be members of the Pension Committee under the current legislation. The advisers also suggested it may be impracticable to separate out the current TOR to identify those matters relating to regulating and controlling the Fund, however if this was deemed possible then a sub committee of the Pension Committee could be created, to allow for the activities of regulating and controlling the Fund to be separated between those activities under the control of ESCC councillors and items outside would have wider representation.
- 5.6 Further legal commentary and detailed analysis is included in the exempt appendix 1.

## **6. Wider Governance**

- 6.1 The Fund underwent a comprehensive Governance review in 2020 carried out by an independent governance consultant. The findings of this review were presented to Pension Board and Committee in June 2020. This review was a follow up to focus on governance and resource arrangements following a report in January 2019 which looked at the evolution of the Fund and interaction with the Fund’s management. The governance review focused on ensuring the Fund would be compliant with the Scheme

Advisory Board's Good Governance Project and making it a leader in the LGPS for governance arrangements.

- 6.2 As a result of this review the independent consultant made a number of recommendations aimed at improving the Fund's organisational and governance structure. Most of the recommendations were implemented immediately with a change to the constitution, the terms of reference to both the Pension Committee and Pension Board, change to delegations, creation of a new Pension Team structure and implementation of two new strategies, the remaining recommendations were implemented in the following quarters with the last item implemented in November 2020. These recommendations have led to major changes within the management and governance of the Fund.
- 6.3 The Fund won the Fund of the Year (over £2.5bn assets) at the 2021 LAPF investment awards. The LAPF Investments Awards were established in 2015 and have come to be recognised as a mark of excellence in the field of pensions provision in the LGPS. To win this award the Fund has to demonstrate excellence in: Implementing best practice; Leadership across pension fund operations; Investment performance; Governance; Administration; Collaboration and leadership within the LGPS.
- 6.4 Internal Audit reports in 2020 and 2021, both found substantial assurance on regulatory compliance, with no recommendations made in 2021.
- 6.5 The Fund publishes a governance and compliance statement annually. The Fund is fully compliant in all areas.
- 6.6 The LGPS Investment Regulations 2016 require the Fund to take and follow expert advice; the investment strategy is in line with all advice from the Investment Consultant, Independent Adviser and all government department and ministerial advice. Failure to follow investment advice could lead to intervention by the Secretary of State.
- 6.7 The Pension Committee must maintain an Investment Strategy Statement (ISS) which is maintained in line with statutory guidance from the Department of Levelling Up, Housing and Communities. The ISS provides an overall framework for the Fund to invest and express the Pension Committee's views on a range of factors to take into account when making investment decisions. The ISS includes a comprehensive Statement of Responsible Investment Principles, which addresses climate risk and energy transition risk. Climate risk including a number of mitigations are clearly presented in the Fund Risk Register. This Risk Register is considered at all Pension Board and Pension Committee meetings.
- 6.8 The Fund was highly commended on their Climate Strategy at the 2021 LAPF investment awards and has recently submitted a report on its stewardship activities to the Financial Reporting Council.

## **7. Approaches taken to the make-up of a Pension Committee**

- 7.1 Officers have reviewed the approaches taken in the wider landscape of the Local Government Pension Scheme (LGPS) and sought appropriate legal advice. In doing so it was noted that:-
- 7.1.1 Where different approaches are taken across the landscape, any supporting legal advice and analysis is not made available to help understand the approach taken.
  - 7.1.2 In some Pension Committees there are co-opted members from outside of the Administering Authority. However, the approaches taken as to whether they should be allowed to take part in discussions and vote are not consistent, with many examples of non-voting members.
  - 7.1.3 The documentation publicly available regarding decision making is unlikely to capture the nuances of how processes apply in reality. Terms of Reference, along with compliance statements, only provide limited information and often do not fully clarify the roles of working groups and whether they are decision makers for financial matters.
  - 7.1.4 A number of Funds have separate Investment Sub-committees outside of the Pension Committee.
- 7.2 It is understood that different LGPS funds have different interpretations of the law surrounding the establishment of Committees under the Local Government Act 1972 in order to carry out the delegated functions of an Administering Authority. Officers have obtained legal advice for the Fund on this topic, which is included as Appendix 1 to the exempt report later in this agenda. Officers have not had sight of any competing legal arguments and recommend that Governance Committee accept the views provided by the legal professionals engaged to provide this advice.
- 7.3 There is evidence that where other Administering Authorities have allowed people from outside the Authority to be part of the Pension Committee that concerns have been raised around balancing the desire to expand representation with the legal requirements of setting up a committee. An example of this is the Oxfordshire Pension Fund, which has allowed co-opted members into the Pension Committee as non-voting members in order to overcome this hurdle.
- 7.4 Other examples of the different approaches being taken across the LGPS landscape include the Merseyside and Avon Pension Funds, which have co-opted members on their Pension Committee but decides on investment matters through a working group that only consists of Councillors from the Administering Authority along with appropriate advisors.
- 7.5 There are also examples of Funds within the LGPS that have broadened their Pension Committee whilst not appearing to separate decisions around investments. The publicly available information is not clear what steps these Funds took to ensure they are compliant with the legislation discussed in Appendix 1 to the exempt report.



- 7.6 It is an increasing trend that co-opted members are joining Pension Committees in order to boost representation. The trend is connected to the work of the Scheme Advisory Board (SAB) as part of its good governance review. The SAB believes that committees in LGPS funds should have increased representation; but the suggestions by the SAB are only guidance at this stage and do not represent the legal requirements for establishment of committees. It is not known at this stage whether there will be a change in the Regulations and there has not been any consultation on this topic, however a consultation is anticipated in 2023 from DLUHC.
- 7.7 Should there be a change in legislation affecting the appointments of members of the Pension Committee, Officers will consider whether any alterations need to be made in practice and advise Governance Committee accordingly.

## **8. Conclusion**

- 8.1 Legal advice obtained by the Fund and reported throughout as relevant legislation, confirm that the Pension Committee is currently structured in line with the Local Government Act 1972; in that the Committee must be solely appointed from elected members of the Administering Authority (as defined in the Local Government Pension Scheme Regulations 2013 as East Sussex County Council), as the work of the Pension Committee include areas such as Investments which are deemed to regulate and control the finance of the Fund. In addition, the Pension Committee is politically balanced to represent the Administering Authority in line with rules under s15 of Local Government and Housing Act 1989, the Local Government (Committees and Political Groups) Regulations 1990.
- 8.2 Officers recommend that the Governance Committee maintain the current term of reference and membership requirements of the Pension Committee until such a time as the law is changed to require and allow for an increase in representation; noting a consultation on good governance which will include Pension Fund structure and representation is anticipated in 2023.

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