Report to:	**Pension Board**
Date of meeting:	**11 September 2024**
By:	**Chief Finance Officer**
Title:	**Governance Report**
Purpose:	**To provide an update on governance workstreams and changes effecting Local Government Pension Schemes and the East Sussex Pension Fund**

RECOMMENDATIONS

The Pension Board is recommended to note this report

1 Background

1.1 This report is brought to the Pension Board to provide an update on the steps being taken to adopt good practice and ensure compliance with regulatory requirements for the East Sussex Pension Fund (the Fund or ESPF).

2 Legal and regulatory changes

2.1 The Fund received a letter from the Minister for Local Government dated 15 May 2024 requesting a two-page submission covering how the Fund will complete the process of asset pooling to deliver benefits of scale and how the Fund will ensure it is effectively run including governance and benefits of greater scale. Despite the change in Government, the Fund responded to the questions in the letter submitting its response to the new Ministry of Housing Communities and Local Government following advice from the Scheme Advisory Board that the responses would be useful to any minister in this position. A response was submitted prior to the deadline of 19 July 2024. A copy of the response from the Fund is available at **Appendix 1.**

2.2 In July 2024, the new Chancellor of the Exchequer, Rachel Reeves, announced a pensions' review to boost investment and tackle waste in the pensions system stating that action will be taken to unleash the full investment might of the £360bn LGPS to make it an engine for growth and tackle the £2bn that is being spent on fees. The work announced focusing on investments was stated to be the first phase in reviewing the pensions landscape.

2.3 In a press release issued on 20 July 2024 by the Government, it states

> "The Local Government Pension Scheme (LGPS) in England and Wales is the seventh largest pension fund in the world, managing £360 billion worth of assets. Its value comes from the hard work and dedication of 6.6 million people in our public sector, mostly low-paid women, working to deliver our vital local services. Pooling this money would enable the funds to invest in a wider range of UK assets and the government will consider legislating to mandate pooling if insufficient progress is made by March 2025."

This is a clear statement of direction that the LGPS must invest through the LGPS pools and do so as quickly as possible.

2.4 59.5 % of the Fund's total assets were pooled as at 31 March 2024 (78.3% of the Fund's listed assets). It is anticipated that 15.8% of the Fund listed assets will not be pooled by 31 March 2025. These assets are held in three small boutique funds that specialise in climate change, either as an impact manager or as listed infrastructure. Impact equity and listed Infrastructure are Strategic Asset allocations by the Pension Committee and there is currently no solution available on the pool platform that would replace these investments.

2.5 The press release goes onto say

> "To cut down on fragmentation and waste in the LGPS, which spends around £2 billion each year on fees and costs and is split across 87 funds – an increase in fees of 70% since 2017, the Review will also consider the benefits of further consolidation."

This statement highlights the concern over investment fees paid in the LGPS by the Government and potential uncertainty for the future structure of the LGPS and administering authorities in their current forms.

2.6 The ACCESS pool has already demonstrated significant cost savings to the underlying LGPS funds with costs savings of £28.5m p.a. In analysis conducted by ClearGlass it was established that the total ongoing charges were 4bps compared to the Benchmark Median of 7bps which equates to annual fees totalling £4.2m compared to the Benchmark Median annual charge of £7.6m for a comparable portfolio; and the resultant savings total £3.4m (3bps). More illiquid assets such as those being considered for increased investment by pension funds such as productive infrastructure assets and UK private equity assets are significantly higher costs than liquid mandates.

2.7 On 16 August 2024 the Government published the terms of reference for the pensions review. The Chancellor has appointed the Minister for Pensions to lead the review. The review will focus on defined contribution workplace schemes and the Local Government Pension Scheme. The review will also work closely with the Minister of State at MHCLG Jim McMahon to look at how tackling fragmentation and inefficiency can unlock the investment potential of the £360 billion Local Government Pension Scheme in England and Wales, which manages the savings of those working to deliver our vital local services, including through further consolidation. The first phase of the review will focus on developing policy in four areas including "Tackling fragmentation and inefficiency in the Local Government Pension Scheme through consolidation and improved governance"

3 Pension Board membership

3.1 Since the last meeting of the Pension Board, the Governance Committee resolved to appoint Linda Hughes as a new employer representative on the Pension Board for the period 25 June 2024 to 24 June 2028 at their meeting on 24 June 2024.

4 Pension Fund Policies

4.1 The Fund's Conflict of Interest Policy is due for its three year review and is attached at **Appendix 2.** Changes to the Strategy include the addition of a reference to the potential conflict as Employer and Administering Authority and a new section on Investment conflicts. Where wording has been amended the text is highlighted in yellow.

5 Funding Update

5.1 The Fund Actuary has not yet produced the indicative quarterly funding update. A verbal update will be provided if this report is provided before the meeting date.

6 GAD Section 13

6.1 On 14 August 2024 the Government Actuary's Department (GAD) issued a report under section 13 (s.13) Public Service Pensions Act 2013. This report relates to the 2022 Triennial Valuation.

6.2 GAD's report is based on 4 objectives which are to determine:

- Compliance - If Fund Valuations are compliant with Scheme Regulations.
- Consistency - Whether Fund Valuations are inconsistent with those of other Funds.
- Solvency - If employer contributions are set at an appropriate level to ensure the solvency of the Pension Fund.

- Long term cost efficiency - Whether employer contributions are set at an appropriate level to ensure the long-term cost efficiency of the Scheme so far as it relates to the individual Fund.

6.3 In relation to Compliance GAD concluded that the aims of section 13 were achieved under the heading of Compliance in terms of valuation reporting. GAD were please to note improvements in the clarity of references to the assumptions on which Rates and Adjustment Certificates were based following the prior review.

6.4 In relation to Consistency GAD found that presentational consistency was evident in 2022 and dashboards aid understanding. The additional information provided following the 2019 review has helped with presentational consistency. However they found that there was no indication of significant improvement in evidential consistency since the 2019 review. They note that local variations may merit different approaches and assumptions but these lead to different outcomes such as ongoing contribution rates. GAD recognised significant improvement in the presentation of climate risk analysis as part of 2022 valuations and most Funds had followed the broad climate risk principles agreed between MHCLG, Fund Actuaries and GAD. GAD recommend the SAB engage with stakeholders to develop the principles and improve consistency across Funds for 2025.

6.5 In relation to Solvency GAD found funding levels have continued to improve on a local basis since 2019 with 106% funded LGPS in aggregate. This reduces current solvency concerns but future solvency risk is still an important consideration. GAD found that the growth of Fund assets relative to the size of the underlying local authorities mean that Funds in deficit will more likely trigger the GAD asset shock measure. No other solvency flags have been raised, however GAD recognise the competing pressures on employer budgets and sensitivity of funding levels to future experience including investment market conditions. GAD recommend Funds continue to review risks and respond to emerging issues and ensure they have appropriate governance arrangements in place.

6.6 In relation to long term cost efficiency GAD flagged two funds in relation to deficit recovery periods and were concerned with one fund that contribution rates were reducing while the deficit recover period was extended. GAD made a recommendation that the SAB consider the approach to surpluses in their review of the Funding Strategy Statement (FSS) guidance. GAD also carried out Asset Liability Modelling (ALM) to illustrate two different surplus sharing models which highlights the potential contribution volatility and funding risks even where a Fund may have a strong current funding position.

6.7 A summary report for ESPF is provided in the exempt section of this agenda. The report does not recognise any flags for concern. Under the SAB funding model GAD have calculated the funding position of the Fund to be 129.4% compared to the Fund's own actuarial funding level of 123%.

7 Conclusion

7.1 The Board is recommended to note this report.

IAN GUTSELL
Chief Finance Officer

Contact Officer: Sian Kunert Head of East Sussex Pension Fund
Email: sian.kunert@eastsussex.gov.uk