

Local Government Pensions
Ministry of Housing, Communities
and Local Government

By Email

Date 19 July 2024

Dear Teresa Clay and Michelle Warbis,

Efficiencies in local government and management of the Local Government Pension Scheme (LGPS)

We welcome the opportunity to respond to the Efficiencies in local government and management of the Local Government Pension Scheme (LGPS) funds letter of the 15 May 2024 and have provided commentary against all the questions on behalf of the East Sussex Pension Fund.

The LGPS is in a unique position to deliver excellent value for money for its members, and deliver outstanding performance with a diversified asset strategy. This has been furthered by the establishment of asset pools, which have acted with a high degree of professionalism in delivering additional benefits to Authorities.

We would welcome an opportunity to participate in a discussion with the Government about the good practice in the management, governance and administration of the LGPS and where there may be opportunities for this to be improved.

How your Fund will complete the process of pension asset pooling to deliver the benefits of scale.

What proportion of assets have been pooled in your chosen LGPS pool?

59.5 % of total assets were pooled as at 31 March 2024 (78.3% of the Funds listed assets).

Is your fund on track to pool all listed assets by March 2025 and if not what are the barriers to this?

No, there is a third-party operator procurement taking place in 2024 which has paused the development of any new listed assets to be added to the ACCESS platform until the outcome is known.

We anticipate that of the 21.7% liquid assets currently invested outside the pool, 15.8% invested in 3 separate mandates will not be pooled by the 31 March 2025. These mandates are all 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. The Fund will work with the pool to consider how these asset allocation decisions can be implemented at scale once the new third-party operator has been appointed.

The Fund is also working on transferring more illiquid assets to the pool and progress in this space is accelerating.

Is there scope for minimising waste and duplication by making use of your LGPS asset pool's services and expertise in reporting and development of the pensions investment strategy?

Reporting: We currently use our pools reporting and actively work with the pool to improve this where we can. There is still an opportunity for an LGPS asset pools to further support consistent, transparent reporting noting the increasing requirements being placed on the LGPS. The reporting from the asset pools will continue to evolve as they increase the investment options available, however some areas of reporting are subject to the release of long awaited statutory guidance such as on Climate reporting.

It is important for Funds to receive independent assessments of the Asset Pools performance to ensure we are getting the best service we can and to avoid potential conflicts of interest within pooling structures. Each Fund has a different context and range of considerations to take into account with its approach to investment including liquidity and cashflow requirements, risk appetite, maturity and covenant of employers, affordability and funding positions. These are unique to each Funds and not consistent within pools meaning there is little duplication and local oversight is required to ensure the ongoing sustainability of each Fund and affordable contribution rates for employers.

Development of investment Strategy: The Fund is required to seek proper advice on our Investment Strategy Statement the pool companies are not able to provide this as they do not have investments in all asset classes. They are not set up to provide advice around the

The Pools do not have all of the available information around the individual Funds liabilities or their Funding Strategy Statement nor do they have expertise in these aspects of a Fund, so are not able to advice how best to match the Fund's assets against liabilities or understand the covenant risk of employers.

What is your expenditure on pensions investment consultancy?

The Fund spent £116k or 0.002% of fund assets on proper advice from our investment consultants. We also spent £55k on specific ESG work to deal with the increasing challenge on Pension Funds to divest and £23k on an independent advisor to assist the Committee in challenging the assumptions from consultants.

Does your LGPS asset pool have an effective modern governance structure in place, which is able to deliver timely decisions and ensure proper oversight? If not, what steps are you taking to make your pools governance more effective?

The Governance structure allows for challenge at several levels from Joint committee, Section 151 officers and senior LGPS officers within the Funds. There are dedicated ACCESS officers which form the ACCESS support unit who are purely focused on the Pool. Along with this there is a third party operator who have a regulatory and depository oversight of their activities.

The ACCESS pool made the strategic choice to use an independent, third party FCA regulated ACS operator, third party Investment Manager for passive investments and a third party Implementation Adviser for non-listed assets. For all of these suppliers, ACCESS has the option to retest the market and re-procure at regular intervals.

In turn these strategic partners have delivered a full range of active listed sub-funds and passive mandates at a discount to market equating to 9bps along with the establishment of best in class offers across alternatives.

The ACCESS model avoids conflicts of concern to the FCA. For example, one role of the operator is due diligence and ongoing monitoring and oversight of investment managers appointed to the ACS sub-funds. Investment managers (in the private and public sectors) with in-house operator functions face conflicts in this regulatory function since the operator is responsible for the appointment and firing of investment managers for reasons of underperformance or other ongoing due diligence concerns. An independent operator using third party managers does not face these conflicts.

How you ensure your LGPS fund is efficiently run, including consideration of governance and the benefits of greater scale.

Does your LGPS fund have effective and skilled governance in place, which is able to hold officers, service providers and the pool to account on performance and efficiency?

Yes.

ESCC operates a Cabinet style decision-making structure. Under the 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.

The Fund governance focuses on:

- The effectiveness of the Pension Committee, the Local Pension Board (Pension Board) and Officers to which delegated function has been passed, including areas such as decision-making processes, knowledge and competencies.
- The establishment of policies and their implementation.
- Clarity of areas of responsibility between Officers and Pension Committee/Board members.
- The ability of the Pension Committee/Board and Officers to communicate clearly and regularly with all stakeholders.
- The ability of the Pension Committee/Board and Officers to ask for the appropriate information and advice and to interpret that information in their supervision and monitoring of the Scheme in all areas.
- The management of risks and internal controls to underpin the framework.

The Fund has implemented as far as it could the LGPS Scheme Advisory Board's 'Good Governance Project', however, we would reiterate previous requests that the Government puts into action the recommendations from the 'Good Governance Project' to develop a common standard on governance and evidence the effective relationships between pensions funds and asset pools with a focus on the type and quality of outcomes administering authorities should aim to achieve.

The Fund has proven its effective governance arrangements as reflected in winning the Governance Award at the LAPF investment awards in 2023 and also won the large LGPS fund of the year in 2021.

Would you be likely to achieve long-term savings and efficiencies if your LGPS fund became part of a larger fund through merger or creation of a larger pensions authority?

We do not consider that there are any material long-term savings that could be achieved from merging the East Sussex Pension Fund with another LGPS Fund or the creation of a larger pensions authority to include the Fund. There could be benefits around resilience for smaller Funds from merging as most LGPS Funds, however is unlikely to result in any cost savings and East Sussex is already substantial in size.

There would be complications around the governance and very high levels of risk involved with a merger. The maintaining of pensioner payrolls would be the main concern, particularly if the Funds merging were on different software suppliers. The challenge of moving hundreds of employers and their payroll providers over to the new Fund and the processes could be detrimental to the quality of member data. The administration costs of a merged Fund would not reduce as the volume of work to administer records and pay pensioners would remain, this would just move the staff resources from one location to another. The software costs will also remain as they are chargeable based on member numbers not a set cost to an organisation.

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).

Yours sincerely

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East Sussex Pension Fund
East Sussex County Council