

Non-Executive Report of the: PENSIONS BOARD 25 November 2019	 TOWER HAMLET
Report of: Neville Murton, Corporate Director, Resources	Classification: unrestricted
LGPS Update - Investment Consultancy and Fiduciary Market Investigation Order 2019, The Pensions Regulator Publication of the LGPS Cohort Report, Updated UK Stewardship Code, Good Governance Report and TPR Governance Survey	

Originating Officer(s)	Miriam Adams, Pensions & Investments Manager
Wards affected	All

REASONS FOR URGENCY

The report was not published five clear days in advance of the meeting. This is due to the additional time required to review the report in order to provide the necessary clearances. Also as it is important that there should not be an extended period without member oversight of this matter this report cannot be deferred.

Introduction

This report provides the Board with a summary of the recent changes in the LGPS.

Recommendations:

Members are asked to

- note the contents of this report;

1. REASONS FOR THE DECISIONS

1.1 To keep the Board updated on recent and key developments in the LGPS.

2. ALTERNATIVE OPTIONS

2.1 There are no alternative options to this report.

3. DETAILS OF REPORT

The Pensions Regulator - Publication of LGPS Cohort Report

3.1 The Pensions Regulator published its report on the governance and administration risks in public service pension schemes, including the 10 UK local government funds who were engaged between October 2018 and July 2019.

3.2 The report summarises the key findings against the Regulator's Code of Practice 14 in terms of exceeding and falling short of required standards. The key improvement areas are summarised as key person risk, Pension Boards, fraud/scams and employers.

The report also outlined some areas of good practice and areas of improvements. Overall the TPR noted:

- Not all funds are the same and there is a variety of equally valid approaches to mitigating risk used across funds in the LGPS.
- It is important that scheme managers recognise, and maintain, a separation between the fund and Local Authority to avoid an over-reliance on the Local Authority's policies and procedures. When establishing its own policies and procedures a scheme manager should be able to seek assistance from the pension board, meaning steps should also be taken to ensure the pension board is able to fulfil its role. Where this is not possible, scheme managers should feed into creating Local Authority policies to make sure they are fit for purpose.
- There are clear benefits to the operation of the fund where there is an engaged s.151 officer who is directly involved.
- Good quality data and record-keeping standards underpin all aspects of successfully running a fund and these areas should be treated as a priority in order to drive good outcomes.
- Scheme managers that have developed and implemented a robust pension administration strategy have found them useful. While not a legal requirement, scheme managers should consider whether this type of document will be useful and look to introduce them where this is the case.
- A common risk is the unexpected departure of key members of the scheme manager's staff. Succession planning and clearly recorded processes help mitigate this risk.
- Measuring governance and administration is challenging and requires more than just an analysis of raw figures. Scheme managers should therefore put in place appropriate reporting measures that they believe capture both quantitative and qualitative assessments. This approach should be tailored to the specific circumstances of their fund.
- Scheme managers should take a holistic approach when considering the governance and administration risks to their fund. Most risks are connected to each other and a scheme manager should understand how a risk materialising will impact on other areas of governance and administration.
- Risks to funds are constantly changing and evolving. For example, the methods used by scammers change over time. Scheme managers should be alert to the changing nature of risks and adapt their approaches accordingly.
- Many scheme managers have a clear understanding of how their funds operate and want to provide the best experience for savers. Exchange of good practice amongst scheme managers is encouraged.

4. The Pensions Regulator – Publication of LGPS Cohort Report

- 4.1 The Pensions Regulator (TPR) announced on Wednesday 2 October that it will be asking the Trustee Boards of 400 schemes to conduct a data review within 6 months. Not all of those asked will be within the public sector, but some will. And for LGPS funds that may be on this list, it will mean another large task to add to a very long list of priorities. The move comes as TPR tightens its regulatory grip to drive up standards of governance and administration.

5. Update on MHCLG recent consultation on local valuations and McCloud

- 5.1 MHCLG recent consultations confirmed that the next round of local valuations for English and Welsh LGPS funds will be 31 March 2022. However what happens to the valuation cycle after 2022 remains subject to consultation. MHCLG confirmed that it expects each LGPS fund to explicitly state in its valuation report and/or Funding Strategy Statement how it has allowed for the McCloud ruling. In particular, where contributions rates are being reduced, funds should be clear about how they have taken the McCloud ruling into account before making the decision to reduce rates.

6. Competition and Markets Authority (“CMA”) and setting of Investment Consultant Objectives

- 6.1 The requirement for LGPS funds to establish objectives for their investment consultants comes into effect from 10 December 2019. At the end of 2018, the Competition and Markets Authority (“CMA”) published its report following a review of the investment consulting and fiduciary management markets. Earlier this year following on from this review, the CMA issued an Order, setting out requirements for the appointment and governance of fiduciary managers for Pension Scheme Trustees to set objectives for their investment consultants. Pension Scheme Trustees in this context means the trustees or managers of Occupational Pension Schemes that have their main administration in the United Kingdom. The CMA requirements extend to both Trustee-based schemes and Local Government Pension Schemes (i.e. Pensions Committees).
- 6.2 Funds must establish ‘measureable’ objectives for their investment consultant(s) which are aligned with their own strategic objectives. The Scheme Advisory Board has provided guidance setting out how the Order applies to the LGPS.

These objectives should be:

- Closely linked to the pension scheme’s strategic objectives;
- Reviewed at least every three years, and after a significant change to the investment strategy or objectives
- Include a clear definition of the outcomes expected and timescales for achieving this
- Should be measurable; and
- Established no later than 10 December 2019

- 6.3 The Pensions Regulator is also consulting on draft guidance, focussing mainly on how trustees should assess the performance of their investment consultants relative to objectives.

The SAB's briefing note issued on 15 October suggests that the Order will be implemented by MHCLG as an amendment to the Investment Strategy Statement statutory guidance and the CMA have confirmed that such provisions within the ISS guidance will meet the requirements of Part 1.4 of the Order. Detailed SAB briefing note is included as Appendix 3 to this report. The Pensions Committee will consider its investment consultants objectives in line with the CMA Order at its November meeting.

7. Good Governance Report Update

- 7.1 The SAB commissioned a report to examine the effectiveness of current LGPS governance models and to consider alternatives or enhancements to existing models which can strengthen LGPS governance in the future. The detailed report is attached as appendix 1 to this report.
- 7.2 Hymans Robertson project team delivered the report to the SAB in July. The process undertaken enabled identification of best practices within current governance arrangements as well as identification of additional ideas to strengthen governance within the current regulatory framework.
- 7.3 Results found that there was a majority preference in adopting a governance model which combined improved practice with greater ring fencing of the LGPS within existing structures. This involved the introduction of guidance or amendments to LGPS Regulations to enhance existing arrangements by increasing the independence of the management of the Fund and clarifying the standards expected in key areas. In addition to this, results found there was a preference for clearer ring-fencing of pension Fund management from the host authority, including budgets, resourcing and pay policies.
- 7.4 Following analysis of the results, Hymans Robertson proposed that an outcome based approach to LGPS governance, with minimum standards, should be adopted rather a prescriptive governance model. In addition to this, updating of relevant guidance and training requirements was proposed.
- 7.5 Following the approval of the good governance report, the Scheme Advisory Board (SAB) asked Hymans Robertson to assist with next stage of this project which involved the defining of good governance outcomes and options for assessment of these outcomes.
- 7.6 On 6 November, the Scheme Advisory Board ("SAB") received the report from the Good Governance Phase 2 working groups which Hymans Robertson facilitated. The purpose is to make a number of proposals designed to provide a framework for good governance outcomes in the LGPS. A link to the copy of the report is currently awaited.

8. Stewardship Code

8.1 The FRC published an updated Stewardship Code which takes effect from 1 January 2020. The Code represents a new best practice standard for both asset owners and asset managers alike.

8.2 Funds who want to remain or become signatories must publish a Stewardship Report demonstrating compliance with the 12 principles of the Code by 31 March 2021. Detailed report is included as Appendix 2 to this report. Further guidance on the Code is expected from the SAB.

8.3 Key changes in the Code include:

- An extended focus that includes asset owners such as pension funds, and service providers including investment consultants and asset managers.
- Annual reporting on stewardship activity and outcomes.
- Take ESG factors, including climate change into account and to ensure Scheme decisions are aligned with the needs of members
- Explain how stewardship has been exercised across asset classes beyond listed equity such as fixed income, private equity and infrastructure, and in investments outside the UK
- Explain Scheme purpose, investment beliefs, strategy and culture, and how these enable them to practice stewardship and how this is demonstrated commitment through appropriate governance, resourcing and staff incentives.
- Work in a collaborative fashion with regulators and industry bodies to identify and respond to the risk of market and systemic failure. As well as show how the scheme has worked with other stakeholders to promote continued improvement of the functioning of financial markets and the role played in any relevant industry initiatives in which they participated.
- Escalate stewardship activities where necessary

9. The Pensions Regulator Public Service Governance Survey

9.1 The Regulator issued the Public Service Governance survey on 6 November to be completed by the scheme manager, or by another party on behalf of the scheme manager in conjunction with the Pension Board Chair.

9.2 The survey covers governance, managing risks, administration and record-keeping processes, cyber security, data review, annual benefits statements, resolving issues, reporting breaches, governance and administration, perception of TRP and attribution.

10. FINANCIAL IMPLICATIONS

- 10.1 This report is for noting, so there are no direct financial implications. However, the outcomes could have financial implications for the Fund.

11. LEGAL COMMENTS

- 11.1 The Competition and Markets Authority have made the investment Consultancy and Fiduciary Management Market investigation Order 2019 implementing a range of requirements in relation to the investment consultants and fiduciary management market. The order comes into effect for LGPS funds on the 10th December 2019.
- 11.2 Part 7 section 12 of the Order prohibits Pension Schemes from entering into a contract with an Investment Consultancy Provider or to continue to obtain investment consultancy services unless the Pension Scheme trustees have set Strategic objectives for the Investment Consultancy provider.
- 11.3 This report provides the Board with an overall update on a range of matters affecting the LGPS. This update will assist the Board in fulfilling its statutory duty of oversight of the functions of the Administering Authority.

12. ONE TOWER HAMLETS CONSIDERATIONS

- 12.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in costs management will reduce the contribution and increase the funds available for other corporate priorities.

13. BEST VALUE (BV) IMPLICATIONS

- 13.1 The effective and efficient management of scheme costs is key to the achievement of the funding strategy objectives and this is considered to be a good decision which can result in greater cost savings to the fund.

14. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

- 14.1 There is no direct Sustainable Action for A Greener Environment implication arising from this report.

15. RISK MANAGEMENT IMPLICATIONS

- 15.1 The rigorous robust management of LBTH Pension Fund results in better quicker and more effective decision making which can lead to better Fund performance and reduction in the contribution required from the Council towards the Fund.
- 15.2 Ensuring good corporate governance and the adoption of sustainable business models at the companies in which the Fund invests should over the longer term ensure that they are able to deliver superior returns to the Fund.

16. CRIME AND DISORDER REDUCTION IMPLICATIONS

16.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

There are no linked reports to this agenda item

Appendices

- Appendix 1 – Hyman Robertson Good governance in the LGPS report
- Appendix 2 – The UK Stewardship Code 2020
- Appendix 3 – SAB briefing note on CMA Order

Local Government Act, 1972 Section 100D (As amended)

List of “Background Papers” used in the preparation of this report

<https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/governance-and-administration-risks-in-public-service-pension-schemes-an-engagement-report#0beb0d2047954672b2a73de451ef7eab>

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