worcestershire countycouncil

AGENDA ITEM 14

PENSIONS COMMITTEE
16 OCTOBER 2019

GOVERNANCE AND PENSION BOARD

Recommendations

1. **The Chief Financial Officer recommends that:**

   (a) a further report is brought back to the December Pensions Committee benchmarking the Fund and administration of the Fund against the Scheme Advisory Board and Pension Regulator's governance reviews, with recommendations to further strengthen the Fund;

   (b) objectives for the Fund's Advisor be brought back to the next Pensions Committee for review and approval;

   (c) the proposed changes to the Pension Board be considered for recommendation to Full Council in November for approval; and

   (d) the Chief Financial Officer be authorised to finalise and submit such a report to full Council, in consultation with the Head of Legal and Democratic Services.

Background

2. Strong governance of the Pension Fund has always been paramount, and with the collapse of several private sector funds, alongside the set up of the pension pools and pressures to maintain balanced funds the need to maintain the strong governance of LGPSs has never been more important.

3. As a result of this level of inspection there have been two reviews by the Scheme Advisory Board (SAB) and the Pension Regulator looking at how to strengthen governance. This paper highlights the findings from those reviews, and sets out proposals to strengthen the Pension Board as a first step.

Scheme Advisory Board Guidance

4. Earlier this year, Hymans Robertson were appointed by the Scheme Advisory Board (SAB) to facilitate a review of governance structures for the LGPS. The SAB commissioned this report to examine the effectiveness of current LGPS governance models and to consider alternatives or enhancements to existing models which can strengthen LGPS governance.

5. A number of stakeholder groups contributed their time and expertise to the review either via the online survey, one-to-one interviews, or through attendance at seminars and webinars.

6. The Hymans project team delivered the report to the SAB on 8 July. The report sets out the results of the survey, recognising strengths and weaknesses in all governance models and proposes 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 funds to continue doing what currently works well while still ensuring the highest governance standards across the scheme.

7. The report recommends introducing key benchmarks which will be used to assess each fund, these include: evidencing robust conflict management, providing sufficient administration capabilities and resource, having a clear and inclusive policy on employer and scheme member engagement and holding regular, independent governance reviews.

8. The SAB agreed to take forward the findings and conclusions to improve governance in the LGPS, and released the report for publication in July. download the full report here. The main conclusion and headline proposals were:

- governance structure is not the only determinant of good governance. Funds with similar governance models deliver different results and good examples exist across a range of different set ups

- Survey respondents were also clear that establishment of new bodies is not required, although this should be facilitated for funds who wish to pursue other arrangements voluntarily. instead, the focus should be on greater specification of required governance outcomes from within the existing structures, and a process to hold funds to account for this

- Respondents favour developing a set of standards that all funds are required to achieve, drawing on current best practice and not imposing disproportionate burden on administering authorities or disrupting current practices that deliver good outcomes already

- Respondents emphasised that independent review is needed to ensure consistency in application of standards.

9. The key proposals were:

- **An 'Outcomes- based approach** to LGPS governance with minimum standards rather than a prescribed governance model. Critical features of the 'outcomes based' model should include:

  a) robust conflict management including clarity on roles and responsibilities for decision-making
  b) assurance on sufficiency of administration and other resources (quantity and competency) and appropriate budget;
  c) explanation of policy on employer and scheme member engagement and representation in governance; and
  d) regular independent review of governance - this should be based on an enhanced governance compliance statement which should explain how the required outcomes are delivered.

- **Enhanced training requirements** for s151s and s101 committee members (requirements for s101should be on a par with LPB members)

- **Update relevant guidance and better sign- posting**. This should include2014 CIPFA guidance for s151s on LGPS 2014 CIPFA guidance for s151s on LGPS responsibilities and 2008 statutory guidance on governance compliance statements. This guidance pre-dates both TPR involvement in LGPS oversight, local pension boards and LGPS investment pooling.

10. SAB agreed that following publication of the report, the Secretariat should commence work, in conjunction with scheme stakeholders, to outline the practical steps necessary to implement the main options set out in the report for consideration by the Board in November. Once approved, scheme stakeholders will be given the opportunity to comment on the Board's recommendations before any formal approach is made to MHCLG Ministers for changes to the scheme's regulations or guidance. It is proposed to bring a report back to the December Committee on the outcomes from that review and to benchmark how our Fund compares to the practices recommended by SAB.

The Pensions Regulator

11. In addition to the work being undertaken by the SAB, the Pensions Regulator also published its report in September 2019 into the governance and administration risks in public service pension schemes, including the 10 UK local government funds who were engaged with between October 2018 and July 2019. The report summarises the key findings against the Regulator's Code of Practice 14 both in terms of exceeding and falling short of required standards and will be discussed in detail when the SAB next meets on the 6 November 2019.

12. In commenting on the report, Chair of the Board, Councillor Roger Phillips said "This key area of work ties in closely in with the Board's own Good Governance project. In identifying examples of best practice as well as areas for further improvement the report will undoubtedly be of great assistance to LGPS funds in seeking to enhance their own governance and administration arrangements." The full report can be found here Governance & Admin Risk report and the Executive Summary and conclusions are as follows:-

13. Overall, TPR found a number of common areas, some requiring improvement but others demonstrating good practice relating to the various risk areas we investigated. The key improvement areas are summarised below. These findings align with the findings from TPR annual public service governance and administration survey.

- **Key person risk**: While most scheme managers demonstrated a good knowledge of what we expect, many funds have a lack of comprehensive documented policies and procedures. We also found an over-reliance on controls put in place by the Local Authority with little interaction between the scheme manager and Local Authority. This was particularly prevalent in relation to cyber security but this theme overlays several of the risk areas we explored.

- **Pension boards**: Engagement levels varied, with concerns being raised about the frequency some pension boards meet and their appetite to build their knowledge and understanding. We saw evidence of some pension boards not wanting to review full documents, instead relying on much reduced summaries and leading us to question how they could fulfil their function. Others were well run and engaged.

- **Fraud / scams**: TPR saw evidence of scheme managers learning from wider events and taking steps to secure scheme assets. However, not all were as vigilant when it came to protecting members from potential scams.

- **Employers**: TPR saw considerable variance in the approaches taken to dealing with the risks surrounding employers, such as receiving contributions and employer insolvency. Generally, this was connected to fund resourcing but also related to different philosophies related to taking security over assets.

14. The key areas of focus that were covered with the findings and recommendations, together with case studies were as follows:

- Record keeping
- Internal Controls
- Administrators
- Member Communication
- Internal Dispute Resolution Procedure
- Pension Boards
- Employers and contributions
- Cyber Security
- Internal Fraud and false claims

15. Overall, 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 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. Where scheme managers liaise with each other to discuss common challenges and solutions to them, whether at formal events or through ad hoc engagement, often leads to improved governance standards. TPR encourage such action.

CMA order on Fiduciary management and Investment consultants

16. On the 10 June the Competition and Markets authority (CMA) published the Investment Consultancy and Fiduciary Management Market Investigation order 2019. In summary, the Order defines the Fiduciary Management (FM) services and obliges pension schemes to formally tender for such services. It also obliges pensions schemes to set objectives for their Investment consultancy (IC) providers as well as placing a variety of new obligations on FM and IC service providers

17. It potentially had consequences for LGPS pools, however on the 29th July the DWP published a consultation on regulations to enact the provisions of the CMA order which explicitly rules out the LGPS as falling under the scope of the obligations in relation to FM service providers. The requirement to set objectives for IC providers remains with a deadline for doing so of 10 December 2019.

18. On the 31 July 2019 The Pension Regulator (TPR) published guidance on the implementation of the CMA order which similarly reflects the position that the LGPS is within the scope only of the IC strategic objectives requirements. Administering authorities should take note of the DWP consultation and the TPR's guide "Setting Objectives for the Provider of Investment Consultant Services. IC Objectives Guide. This may result in WPF setting up formal objectives for its Investment consultancy advisor. Part of the TPR's guidance states the following:

- Setting objectives for advisers is an important part of an effective system of governance. We expect that by putting objectives in place, trustees will be better positioned to assess the quality of the service they receive and to deliver better outcomes for their members
- In setting objectives for your investment adviser, you will want to receive their input to ensure that the objectives being set are consistent with the service

being offered and are realistic. In obtaining your adviser's input, you should be aware of the potential for their input to be subject to conflicts of interest and you should be prepared to challenge their input. You should also consider whether to involve a third party to help you set those objectives

- Once objectives have been agreed, we would expect these to be signed off in accordance with your existing governance framework, ensuring that all members of the trustee board have sight of and, if relevant, agree with the adviser objectives that have been set and the ongoing monitoring process of these.

19. Further information and the consideration of formal objectives being set will come back to the December Committee for formal approval.

Pension Board

20. Members will recall that there is a legal obligation to have a Pension Board. That Board is responsible for assisting the Council to comply with legal obligations relating to the Scheme and any requirements imposed by the Pensions Regulator, and for assisting the Council to ensure the effective and efficient governance and administration of the scheme. This is an oversight role and the local Pension Board is ***not*** responsible for decision-making in relation to the management of the Scheme or the discharge of the Council's functions – that is a matter for the Pensions Committee and sub-committee.

21. At the September meeting of the Pension Board, the Independent Chair stood down after four years as Chair. This allows the Fund to review the working arrangements and to assess the performance of the Board and consider, in light of the reviews mentioned above and the Business Plan of the Fund, potential next steps to further strengthen the governance and administration of the Fund as well as the advice to the Committee.

22. A review of practices across the various LGPS Funds across the region and country have identified a real mix of practices. Firstly, not all Boards are chaired by independent members. The Regulations that set up Pension Boards allowed for two models: one chaired by an independent and one model chaired by a member selected from the Board members. There is no legal requirement to have an independent chair.

23. Whilst there are benefits of an independent chair, in terms of knowledge and advice there is also a cost and risk that there is a concentration of skills and responsibility in one individual. The independent chair was also a non-voting role. It is proposed that in the current position that the nature of the Board is changed and that going forward there is not an independent non-voting Chair but that a Chair is selected by the Board from the membership of the Board.

24. The second area of review is the membership itself. The Regulations are very clear that the membership must be 50:50 Employer and Member representatives. Currently the Pension Board consists of five members (the independent chair, two councillors representing employers and two trade union representatives for members). With only 4 voting members, this has often led to issues of quorum but also and importantly excludes representation from wider stakeholders. Therefore it is proposed to increase the membership to eight as follows:

Employer representatives	Member Representatives
• Three Councillors – Two for Worcestershire County Council and one from Herefordshire Council • One senior officer from an employer Employer representatives must not be involved in the administration of the Fund and are to be nominated by the relevant body, and the Senior Officer appointed by the CFO	• Two Trade Union representatives • One active member • One retired member

25. It is suggested that the two Fund member representatives outside of the unions (i.e. one active and one retired Fund member) are recruited by the CFO through head-hunting / open invite and interview, and appointment by the CFO. It is also recommended that members serve for four years subject to the terms attached in the Terms of Reference attached as an Appendix.

26. It is proposed that the quorum for the Board be four with a 50:50 attendance being maintained so that is two Employer and two member representatives being quorate.

27. The third area of review proposed is the timing of the Board. Presently the Board meets after Committee to consider the minutes of the Committee, this does not meet good practice and the original objective of the Board to advise the Committee. It is proposed that the Board meets ahead of Committee to consider matters that the Committee will be or need to consider and make decisions, that way the Committee can seek and hear the advice of the Board.

28. Finally, there are a number of changes proposed to the Terms of Reference of the Board outside of those necessitated by the above proposals. The changes proposed are more to tidy up the current ways of working to tie them in line with actual practice. So for example it is proposed the Board reviews the IDRP process and performance rather than assist. The current and industry standard is that this is an officer process and members of the Committee would be engaged in rare occasions, as such advice is limited to review rather than assist. The proposed terms of reference changes are set out in the Appendix and this Committee's views are sought on this.

29. If Committee are minded to support the proposals set out above a report will be presented to the November meeting of Worcestershire County Council as the Administering Authority for approval.

Contact Points

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Supporting Information

- Appendix – Proposed Pension Board updated Terms of Reference

Background Papers

In the opinion of the proper officer (in this case the Chief Financial Officer) the following are the background papers relating to the subject matter of this report:

10 June 2015 – Pension Committee paper on the establishment of the Pension Board.