

<b>Subject</b>	<b>Regulatory and Policy Update</b>	<b>Status</b>	For Publication
<b>Report to</b>	Local Pension Board	<b>Date</b>	10 August 2023
<b>Report of</b>	Director		
<b>Equality Impact Assessment</b>	Not Required	Attached	Na
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## 1 **Purpose of the Report**

- 1.1 To update the Board on developments in the policy and regulatory arena.
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## 2 **Recommendations**

- 2.1 Members are recommended to:

- a. Note the report and identify any comments or issues which they would like to be considered in the Authority's response to the issues raised.**
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## 3 **Link to Corporate Objectives**

- 3.1 This report links to the delivery of the following corporate objectives:

### **Effective and Transparent Governance**

To uphold effective governance showing prudence and propriety at all times.

Maintaining a clear line of sight on the policy agenda and developing considered responses to changes and developments is a key element of good governance.

## 4 **Implications for the Corporate Risk Register**

- 4.1 The actions outlined in this report touch on the risks related to data and regulatory compliance identified in the Corporate Risk Register. This is particularly true of the McCloud related issues. The developments in relation to the Divestment Boycotts and Sanctions legislation and pooling may well create new compliance issues and hence risks that will need to be incorporated in the risk register in due course.

## 5 **Background and Options**

5.1 This report provides the Board with an update on three specific developments in the policy and regulatory arena:

- The publication of draft McCloud regulations and particular proposals in relation to aggregations on which further consultation is being undertaken.
- The publication of the Economic Activity of Public Bodies (Overseas Matters) Bill which seeks to enact the Government's proposals in relation to divestment, boycotts and sanctions (DBS).
- The publication of the long awaited consultation on the further development of investment pooling and associated investment issues.

### *McCloud*

5.2 The Government has now published draft regulations which it intends to lay before parliament at such time that they can become effective in time for the October deadline for putting the McCloud remedy into effect. Alongside this there is further consultation seeking general views on the following areas:

- Aggregation – Determining the rules applicable to decide whether a member with multiple LGPS memberships has underpin protection in some or all of these.
- Club transfers – Determining the rules applicable to decide whether a member with previous membership of another public service pension scheme has underpin protection in respect of their LGPS membership.
- Flexible retirement – How the underpin should work in respect of flexible retirement, particularly for cases of 'partial' flexible retirement, where a member does not take all their accrued career average benefits.
- Divorce – How the scheme's divorce and underpin calculations interact.
- Injury allowances – How a retrospective increase to a member's pension arising from McCloud remedy may impact any injury allowances payable.

5.3 The Government is also seeking technical comments and comments on implementation in the following further areas:

- Excess teacher service – The retrospective admission to the LGPS of certain teachers who have multiple employments.
- Compensation – The circumstances where a member may be paid compensation where they have suffered a loss relating to the age discrimination found in the McCloud case or the McCloud remedy.
- Interest – The interest terms that will apply where payments are made later than would have been the case, due to the McCloud discrimination.

5.4 Some of these are particularly technical issues (interaction with divorce) or areas where established practice is being followed (interest payments). Some, however, will by the Government's own admission increase the administrative complexity of the scheme and present greater challenges than expected for administrators. In part this flows from an understandable desire to ensure that the implementation of the remedy is as far as possible able to withstand further legal challenge. However, in the areas of

aggregations, club transfers and excess teacher service there is potentially very significant extra work and investigation involved in every case also involving securing information from other pension schemes which will add to the time taken to resolve cases. It should also be noted that the expectation is that fewer than 1% of cases in the LGPS will be affected and of those only a very small proportion will see a material change in their benefits.

- 5.5 Locally we have established a project team to work through these issues and are developing the policy statements that are required to be in place to establish how missing and incomplete data should be addressed as well as a communications strategy. We are also testing the various calculations required within the administration system as they are released and so far no significant issues have emerged.

#### *Divestment Boycotts and Sanctions*

- 5.6 The Government laid the Economic Activity of Public Bodies (Overseas Matters) Bill before parliament on 19<sup>th</sup> June and it is now in Committee in the House of Commons. The Bill seeks to enact their commitment to preventing public bodies either through procurement or investment decisions from “running their own foreign policy”. In simple terms the Bill prevents LGPS funds from making decisions to divest from companies operating in particular countries at the urging of campaign groups. There is an enforcement regime in relation to the LGPS which will be operated by the Pensions Regulator. This Bill addresses a range of complex and difficult issues and raises some challenges which it appears will be difficult to navigate. Writing in Local Government Chronicle Phil Triggs the Tri-Borough Director of Pensions and Treasury who runs three LGPS Funds in London asked what happens:

*“where an analyst has anticipated that a company’s value will decrease because of ESG decisions it has made... if that strategy falls within the new law’s definition of not being in line with UK foreign defence policy, and the law therefore states that the fund must remain invested, and the fund therefore loses value, who will pay for that?... The government’s current message is that ‘this is not designed to get in the way of ESG factors, excepting the very narrow area of UK foreign or defence policy’. But this is absolutely not a very narrow area. .... We could end up in a scenario with never ending arguments involving ESG factors versus foreign and defence policy.”*

- 5.7 The Bill is proceeding through Parliament and undoubtedly statutory guidance and amendments to the LGPS Investment Regulations will be required to ensure that LGPS Funds do not inadvertently fall foul of the law. The involvement of the Pensions Regulator establishes a new precedent and while in the context it appears preferable to the alternative of the Department being the enforcement agency beginning to involve the Regulator in LGPS investment matters does break new ground and it remains to be seen whether this presages wider moves to involve the regulator in these aspects of LGPS.
- 5.8 Locally while SYPA is regularly lobbied to divest particularly from companies operating in the Occupied Palestinian Territories the policy framework around issues of this sort and the fact that as investments are made through pooled vehicles would appear to make it difficult for us to step over the line drawn in the Bill. However, there is a significant amount of detail which will only become clear in regulations and guidance and once the law is tested in court.

### *Investment*

5.9 Following the Chancellor's Mansion House speech the Government published the long awaited consultation on pooling which will ultimately lead to the production of more detailed statutory guidance and potentially some amendments to the Investment Regulations. The key points are:

- A clear timeline for the holding of all listed assets in pool run collective vehicles by March 2025 and a clear intention to use existing powers to make sure this happens. SYPA has already met this target.
- Clearer plans and timelines for the overall transition and what appears to be a higher bar for holding assets outside of the pool.
- A clearer view from Government on what counts as pooling and also how strategic asset allocation (the responsibility of funds) should be defined. This includes a clear view that pools should be more involved in advising on strategy.
- A clear view that the number of pools should be reduced with a minimum scale of at least £50bn and preferably £75bn. This should though be achieved through voluntary mergers.
- While accepting that pools might invest in each other's products a clear intention that there should not be competition between pools. The intent here is to allow pools to specialise in specific areas.
- A requirement to publish a plan showing how each Fund will move to achieve investment of 5% of AUM in projects which support "levelling up" and to report on the impact of these projects using the metrics in the "levelling up" white paper. The work already done by SYPA in this area anticipates this.
- A requirement to consider investing up to 10% of AUM in Private Equity and growth capital and to report on this.
- Detailed technical proposals concerned with the use of investment consultants (incorporating elements of the regulation of private sector schemes) and the definition of investment.

5.10 There is a very considerable amount of information to digest and a great deal of detail as well as some remaining unanswered questions in this document and an online session has been arranged for Board and Authority members to be briefed on and provide a steer on the issues prior to a response being drafted for approval at the September Authority meeting. The process of producing the response will work alongside the process to produce a collective response for the Border to Coast Partnership which will be approved at the Joint Committee at the end of September.

5.11 It is quite clear that this process is now being driven by HM Treasury and that there will be considerable momentum behind it as a result. It also seems to be true that there is little if anything within the consultation that would be a matter of party political contention and therefore it is important to work on the basis that these proposals will happen even if there are changes of emphasis and different timelines in the event of a change of government following the General Election.

## 6 **Implications**

6.1 The proposals outlined in this report have the following implications:

Financial	None directly
Human Resources	None
ICT	None
Legal	Changes to the regulations and ne statutory guidance will need to go through a formal consultation process which will allow further debate on the detail.
Procurement	None

**George Graham**

**Director**

<b>Background Papers</b>	
<b>Document</b>	<b>Place of Inspection</b>
McCloud Supplementary Issues and Scheme Regulations	<a href="http://www.gov.uk">‘McCloud’ remedy in the LGPS – supplementary issues and scheme regulations - GOV.UK (www.gov.uk)</a>
Economic Activity of Public Bodies (Overseas Matters) Bill	<a href="#">Economic Activity of Public Bodies (Overseas Matters) Bill - Parliamentary Bills - UK Parliament</a>
LGPS Investment Consultation	<a href="http://www.gov.uk">Local Government Pension Scheme (England and Wales): Next steps on investments - GOV.UK (www.gov.uk)</a>