Agenda Item

Subject	The Government's Pensions Review	Status	For Publication
Report to	Authority	Date	12th December 2024
Report of	Director		
Equality Impact Assessment	Not Required	Attached	No
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1 Purpose of the Report

1.1 To inform members of the Authority about the initial conclusions of and next stages in the Government's Pensions Review and gain approval for the approach to be taken in framing a response to the consultation exercises launched following the Mansion House Speech.

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2 Recommendations

2.1 Members are recommended to:

a. **Note the Government's proposals in relation to reform of the Local Government Pension Scheme.**

b. **Endorse the headline response set out in Appendix A and the body of this report as the basis for a formal response to the consultation and further discussion with Border to Coast partners.**

c. **Agree the process for finalising the formal consultation response set out in para 5.11.**

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3 Link to Corporate Objectives

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

Customer Focus

To design our services around the needs of our customers (whether scheme members or employers).

Listening to our stakeholders

To ensure that stakeholders' views are heard within our decision making processes.

Investment Returns

To maintain an investment strategy which delivers the best financial return, commensurate with appropriate levels of risk, to ensure that the Fund can meet both its immediate and long-term liabilities.

Responsible Investment

To develop our investment options within the context of a sustainable and responsible investment strategy.

Scheme Funding

To maintain a position of full funding (for the fund as a whole) combined with stable and affordable employer contributions on an ongoing basis.

Effective and Transparent Governance

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

Valuing and engaging our Employees

To ensure that all our employees are able to develop a career with SYPA and are actively engaged in improving our services.

The government's proposals potentially impact all the corporate objectives, in particular those associated with the delivery of the investment strategy.

4 Implications for the Corporate Risk Register

4.1 The Government's proposals outlined in this report will have implications both for the risk associated with the delivery of the Border to Coast Strategic Plan and the new risk associated with the Pensions Review. Some of these are outlined in the body of this report, however until more detail is available the full implications will not be fully apparent.

5 Background and Options

The Chancellor of the Exchequer made her Mansion House Speech on 14th November in which she set out the initial conclusions of the Government's Pensions Review and the next steps that the Government propose to take. Among the headlines from the speech were:

- Increased investment to spur innovation and growth.
- Launch of a Transition Finance Council (focussed on the climate transition).
- Plans for consolidation of Defined Contribution Master trusts.
- A more proactive approach to working with investors to ensure that capital and projects are matched.
- A British Growth Partnership to crowd investment into venture capital funds and innovative businesses.
- Outline of reforms to financial services regulation to move from "regulating for risk" to "regulating for growth".

5.1 Specifically relating to the Local Government Pension Scheme (LGPS) following the speech a consultation was launched on the following areas, with responses required by 19th January 2025:

Pooling Structure

- Definition on the model of pooling – FCA regulated investment manager with (or the ability to develop) in-house investment capabilities.
- Mandate full delegation of investment implementation to the pools; consistent definition of Strategic Asset Allocation to be agreed.
- Principal investment advice for Funds to come from the Pool.
- Pools to submit plans on how they will deliver policy by 28 Feb 2025.
- Target to pool all listed assets by March 2025 remains.
- Requirement to deliver on pooling model & transition of all assets by March 2026

Investments

- They recognise the "brilliant work" already carried out by the LGPS as a significant investor in the UK supporting 'local' investments. It seeks to provide a new framework to build on this:
    - Funds to set out approach & allocation for local investments.
    - Funds to provide annual reporting on local investments.
    - Pool to implement Funds' local investment strategies, including due diligence on local investments.
    - Funds to consider Mayoral / Combined Authority growth strategies in developing strategy and 'work with them' through pools on local investments.

Good Governance

- Implementation of Good Governance report (including knowledge & skills of Committee members); they expect this will drive collaboration & consolidation of Funds over time.
- Recognise the importance of Independent Advice to Funds.
- Consideration of Fund and Scheme Member Representatives in Funds/ Pools.

5.2 The Consultation sets out 30 specific questions on the 18 proposals set out in the consultation. These questions and an initial SYPA response are set out in Appendix A.

5.3 Broadly the consultation contains no surprises. It simply confirms and amplifies what was set out in the previous consultation exercise undertaken by the previous government.

5.4 The most significant proposals are those around the structure of pools, the requirement to pool 100% of assets and the timescales for delivery of these. From an SYPA point of view these do not raise major challenges, although significant work, particularly around the transition of legacy portfolios will be required. This reflects the fact that the Border to Coast Partnership already meets the Government's key requirements and already has plans to develop new advisory capabilities as required. As indicated in the consultation document other pools are not in this position and coupled with the timescale this may result in some consolidation of pools. Again, this is, should it occur, something that will likely require considerable work from officers and engagement with elected members.

5.5 The consultation sets out a much clearer divide between the roles of the pool and the individual fund, at the same time providing a definition of what is meant by Strategic Asset Allocation (a gap in the current framework previously highlighted by SYPA). This will require some changes for SYPA such as using the statement of investment beliefs to better define the appetite for both risk and volatility as well as issues of balance between different types of market (emerging and developed). The timing of this is fortuitous given that the process of reviewing the investment strategy is about to start.

5.6 While there will be a much clearer divide between the roles of the pool and the fund there will be a need to think much more about how to act when things go wrong (for example if an investment proposition significantly under-performs). In the pre-pooling world, the action generally would be to replace the fund manager. This is much more difficult in the pool relationship given that these decisions are not for the fund to take. The way to force action is through the shareholder route. However, the tools involved (in effect removing the Board) seem disproportionate in relation to the issues being dealt with. Therefore, work is going to need to be done which develops ways of addressing these issues while respecting the different roles of the different parties to the relationship.

5.7 The process of transitioning legacy assets is likely to be in several stages. In the first instance Border to Coast and SYPA will enter into an agreement for the pool to manage the relevant assets. Over time some of these may transition into new pooled vehicles as seed investments (as has been the case with other assets previously), others may stay as they are until maturity while others may be reviewed and disposed of, if it makes both financial and strategic sense to do so. Some “evergreen” investments in the legacy portfolios may justify the creation of a specific Border to Coast wrapper but the benefits of this type of solution which has been used by another pool would need further consideration regarding the costs involved weighed against the perceived benefits. These are matters of detail, delivering this proposal will allow the Authority’s team to work with greater focus on the oversight of the pool and the understanding and analysis of performance.

5.8 The focus on local (now defined as the area served by the fund) investment very much reflects the approach already taken by SYPA with a plan reflecting local growth priority identified by the Mayoral Combined Authority reflected within the Investment Strategy and the Strategic Asset Allocation. Give the move to 100% of assets being pooled there is a requirement that local investments be managed by the pool. This will require Border to Coast to develop and resource some additional capabilities to support investments of this nature.

5.9 The proposals in relation to governance are very much as expected and finally deliver the Scheme Advisory Board’s (SAB) Good Governance proposals. There are, though, a couple of areas of difference. Firstly, the regular Independent Governance Reviews are intended to have more teeth than was perhaps originally envisaged, potentially ultimately leading to the use of the existing intervention powers. The proposal to deliver these reviews through a peer led approach overseen by the SAB is welcome and works with the grain of the scheme and builds on the existing degree of collaboration and sharing across the “LGPS family”. The second area of difference is a proposed requirement to appoint one or two independent advisers (or members) with a somewhat broader remit than SYPA’s current independent advisers. This proposal is, at this stage, not well-defined buy given the nature of qualifications talked about in the consultation it seems to be a move to introduce professional trustees into the LGPS, which is something that needs to be treated with caution given the peculiarities of the mix of local government and pensions which are at the heart of the LGPS.

5.10 Broadly from an SYPA point of view there is little to criticise in the proposals being put forward at headline level, although there are several issues of detail. Equally there is much to welcome such as the commitment to both FCA regulated entities and the principle of internal management in the model of pooling and the commitment to local investment. The initial responses set out in Appendix A are therefore broadly positive, reflecting the degree to which both Border to Coast and SYPA were already progressing on the path now clearly set out by the Government.

5.11 Officers are working with colleagues across the Border to Coast partnership to develop a comprehensive partnership response, and the initial answers set out in Appendix A will need to be re-examined considering the results of that work, before being submitted as a formal response. Given that a response must be provided by 16th January 2025 there is no formal Authority meeting which could approve a response. Given the significance of this consultation, it is proposed to hold an informal meeting of Authority members in early January to endorse (or otherwise) a more comprehensive draft response with formal sign off under the urgency procedure by the s41 members following this. In addition, work will have to be undertaken between the operating company and the partner funds to develop the plan for meeting the Governments pooling model requirement which must be submitted by the end of February 2025. While approval of this plan is a matter for the Company's Board it is into currently clear how formal endorsement by partner funds will be built into the process although given the degree of co-production necessary to arrive at the plan it seems unlikely that there would be any significant level of disagreement.

6 Implications

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

Financial	At this stage there are no direct financial implications. However, should proposals to merge / restructure existing pools come to fruition the Authority would be required to make a contribution towards the legal and other costs associated with such a move which could be in the hundred of thousands. Moving legacy portfolios under pool management will have costs which will vary depending upon the route chosen. Such costs will erode performance (if marginally) on an ongoing basis. In addition the process likely to be started as a result of the proposals set out in the Mansion House speech is likely to consume a significant amount of officer time over the next 12-18 months which may divert senior management resource from addressing the Authority's key customer focussed priorities.
Human Resources	None identified at this stage
ICT	None
Legal	None identified at this stage

Procurement	None identified at this stage. However, changes to the structure and composition of pools could raise significant procurement issues.

George Graham

Director

Background Papers	
Document	**Place of Inspection**
Mansion House Speech	Mansion House 2024 speech - GOV.UK
LGPS Consultation	Local Government Pension Scheme (England and Wales): Fit for the future - GOV.UK

Appendix A

Consultation Questions and Initial Response

LGPS Pooling

Question 1:

Do you agree that all pools should be required to meet the minimum standards of pooling set out above?

Yes, the arrangements set out broadly mirror those already in place within the Border to Coast pool which have proved successful.

Question 2:

Do you agree that the investment strategy set by the administering authority should include high-level investment objectives, and optionally, a high-level strategic asset allocation, with all implementation activity delegated to the pool?

Yes, while SYPA would take up the option of setting the high-level strategic asset allocation we can see that for some funds a move to something much close to fiduciary management may be appropriate and we welcome the choice on this remaining with funds.

Question 3:

Do you agree that an investment strategy on this basis would be sufficient to meet the administering authority's fiduciary duty?

Yes. Clearly response to this question will vary depending upon how the strategy setting element of fulfilling fiduciary duty is viewed and on the understanding of what the new style investment strategy will look like.

In terms of fiduciary duty our view is that the strategy should be designed to give a significant probability of successfully delivering the funding objective in the long term. By significant probability we have always adopted a figure of 70% (2/3rds rounded). This approach frames the fiduciary duty in the context of the fact that any investment strategy runs the risk of not delivering the intended outcomes.

In terms of the content of the investment strategy it is likely that statements of investment beliefs (the high-level objectives referred to) may need to become somewhat clearer to enable them to be implementable. This will also include the need for the AA to specify much more clearly their appetites for risk and volatility. These are developments that would be broadly beneficial.

Question 4:

What are your views on the proposed template for strategic asset allocation in the investment strategy statement?

This seems generally acceptable and should all AA's to appropriately allocate between and within the growth, protection, and income asset categories. Allocating at a lower level than suggested could amount to tactical calls or stock selection which are better left to the pools. There may be a desire to define regional allocations (for example over or under weighting emerging markets relative to the broader world economy), however, this is essentially a judgement on risk and/or volatility which should be dealt with through the AA's investment beliefs.

There is one area where this template is problematic, which is the definition of cash. While there is cash held within various pooled products it is not separately identified. AAs hold cash to ensure the payment of benefits and the flows of cash into and out of various investment vehicles (for example drawdowns into alternative funds). The way in which cash is viewed in the template creates an artificial distinction between investment cash and operational cash which seems likely to result in higher levels of cash holding in order to ensure that cash is always available to pay pensions which is undesirable in terms of investment outcomes.

Question 5:

Do you agree that the pool should provide investment advice on the investment strategies of its partner AAs? Do you see that further advice or input would be necessary to be able to consider advice provided by the pool – if so, what form do you envisage this taking?

We have no objection to this and Border to Coast's 2030 Strategy includes the development of these capabilities, which we would intend to use when available. This is the logical result of the Government's move towards a more fiduciary management model for LGPS. There are, however, several potential conflicts of interest created by the development of advisory capabilities by pools and the plans to be provided to government by the end of February 2025 should identify these and set out at a high level the arrangements for managing them. Such mitigations would also be an FCA requirement.

We would want to continue to utilise independent advisers as part of the process of challenges and debate around the development of strategy, together with using them to assist in framing the questions which any strategy review should address. This is like the arrangement in place at present where we only use an investment consultant for the strategy review because of their modelling capabilities which will in future be delivered by the Pool.

Question 6:

Do you agree that all pools should be established as investment management companies authorised by the FCA, and authorised to provide relevant advice?

Yes, the presence of the FCA regulated entity in the operating model was a significant factor in the Authority's original decision to join the Border to Coast partnership.

Question 7:

Do you agree that administering authorities should be required to transfer all listed assets into pooled vehicles managed by their pool company?

Yes, and SYPA has already done so.

Question 8:

Do you agree that administering authorities should be required to transfer legacy illiquid investments to the management of the pool?

SYPA is currently working towards a position where only local (South Yorkshire) elements of its place-based impact strategy and natural capital (because there is no pool vehicle) are held outside the pool. Because of the timescale for running off the existing significant alternatives portfolio for reinvestment we were already beginning to think about whether there might be alternative options for management of the legacy illiquid investments, although initially the costs of providing some sort of pool wrapper (such as transfer taxes and legal fees for novation) looked prohibitive. In the short term a simple mandate to the pool to manage these assets will allow a more considered look at the plans for each asset.

If the Pool can meet SYPA's strategic objectives in managing these investments (in particular local impact and carbon offsetting as well as return) then there is no objection to transferring management provided the costs associated with doing so, do not significantly impact performance.

Question 9:

What capacity and expertise would the pools need to develop to take on management of legacy assets of the partner funds and when could this be delivered?

Border to Coast already has significant expertise in managing the type of assets that make up the bulk of the legacy portfolio, so rather than additional capabilities it is likely that additional capacity would be required which could, subject to budgetary approval etc., be delivered over the course of 2025/26. Other pools may not be in such a fortunate position and will need to consider whether to build capabilities from scratch which could be challenging in the required timescale or collaborate with others.

Border to Coast (and most of the other pools) would need to build new capabilities in relation to supporting local investment and to a lesser degree in relation to natural capital, but these are likely to amount to the extension and broadening out of existing teams and would be relatively easy to accomplish in the required timescale.

The timescale may be an issue if there is a need to develop some form of "wrapper" for legacy assets but this might become a staged process of developing "degrees" of transfer of management from managing assets on the fund balance sheet through to a "wrapper" or transfer into a fully pooled vehicle over a longer timescale.

Question 10:

Do you have views on the indicative timeline for implementation, with pools adopting the proposed characteristics and pooling being complete by March 2026?

This timescale is undoubtedly challenging and will be more so for those pools which do not have the initial building blocks in place already. However, the Government's frustration at the overall pace of pooling is understandable and setting an ambitious timescale is perhaps one way of concentrating minds to achieve the overall objective. But it will be important that the deadline does not result in the making of short sighted sub-optimal and potentially costly decisions about the transfer of assets to the Pool, although this will be something that will need to be dealt with at the individual asset level.

Other developments

Question 11:

What scope is there to increase collaboration between pools, including the sharing of specialisms or specific local expertise? Are there any barriers to such collaboration?

There is certainly scope for collaboration between the pools, for example the development of another direct infrastructure vehicle to compete with GLIL seems to be an entirely counter-productive course of action, and similar arguments might be made about limiting the number of direct real estate products across the pools. Equally though there is good reason why to avoid "lot sizes" becoming too large each pool should continue to deliver a core alternatives programme.

The Pools are commercial entities so there are logically some constraints to the ability to collaborate with potential commercial competitors. Equally the Teckal rules limit the amount of revenue that can be generated from outside the group of shareholders, and this may be a more significant constraint than the commercial one, and might be an area where the Government would like to consider providing some regulatory relief.

Question 12:

What potential is there for collaboration between partner funds in the same pool on issues such as administration and training? Are there other areas where greater collaboration could be beneficial?

Broadly we are supportive of increased collaboration between funds as this will result in the spreading of good practice, potentially at a faster rate than is currently the case.

Within Border to Coast we are already developing collaboration across a range of areas including governance, accounting and aspects of administratin, beyond investment, and this is beginning to generate some encouraging results. In the area of administration, the voluntary creation of genuine shared services (whether within or outside of a pool) seems likely to be more beneficial approach than more forced models and the mixing of regulated (investment) and unregulated (administration) activity within the same entity can be difficult.

Local investment

Question 13:

What are your views on the appropriate definition of ‘local investment’ for reporting purposes?

Our preference would be to define local as South Yorkshire and we already report on this basis also highlighting investment across the UK and the wider Yorkshire and the Humber region.

Question 14:

Do you agree that administering authorities should work with their Combined Authority, Mayoral Combined Authority, Combined County Authority, Corporate Joint Committee or with local authorities in areas where these do not exist, to identify suitable local investment opportunities, and to have regard to local growth plans and local growth priorities in setting their investment strategy? How would you envisage your pool would seek to achieve this?

Yes, and we have already done this. We would envisage that the Pool would become party to our existing Memorandum of Understanding with the South Yorkshire Mayoral Combined Authority (SYMCA) and participate alongside us in the regular dialogue that is maintained with SYMCA.

Question 15:

Do you agree that administering authorities should set out their objectives on local investment, including a target range in their investment strategy statement?

Yes, and we have already done so, setting a 5% target allocation for a place-based impact strategy although we will need to refine the target setting and trajectory as part of the next strategy review, in particular setting a specific target for South Yorkshire.

Question 16:

Do you agree that pools should be required to develop the capability to carry out due diligence on local investment opportunities and to manage such investments?

We see the logic of the position taken by the Government on this. However, there would need to be some arrangement which ensured that sufficient resource was being allocated to achieve partner funds specific local objectives, rather than simply folding investments into some form of UK structure. These types of investment are also relatively management intensive, even where external fund managers are used, and pools will need to ensure that they put enough resource in place to ensure that managing these types of investment does not negatively impact on the resources devoted to core investment offerings.

Question 17:

Do you agree that administering authorities should report on their local investments and their impact in their annual reports? What should be included in this reporting?

Yes, SYPA already does this. We believe reporting should follow the Place Based Impact Investing Framework developed on behalf of the Impact Investing Institute. This would ensure consistency in both outputs and the demands placed on fund managers and does not preclude individual funds prioritising the particular forms of impact which they are seeking to achieve in addition to financial return.

Governance of funds and pools

Fund governance

Question 18:

Do you agree with the overall approach to governance, which builds on the SAB's Good Governance recommendations?

We welcome the significantly overdue steps to finally implement the Good Governance proposals,

Question 19:

Do you agree that administering authorities should be required to prepare and publish a governance and training strategy, including a conflict-of-interest policy?

We agree that Funds should maintain both governance and training strategies and a conflicts of interest policy. Whether these should be contained in the same document is a moot point, particularly as the training strategy is likely to require more frequent updates. Guidance should emphasise that the training strategy should cover both Board and Committee (in SYPA's case Authority) members equally.

Question 20:

Do you agree with the proposals regarding the appointment of a senior LGPS officer?

Yes, and SYPA's unique status means that it already meets this requirement. We also believe that the requirement for the Senior Officer to manage all aspects of the Fund is crucial and should be fully reflected in regulation rather than guidance.

Question 21:

Do you agree that administering authorities should be required to prepare and publish an administration strategy?

Yes, and SYPA already does so.

Question 22:

Do you agree with the proposal to change the way in which strategies on governance and training, funding, administration and investments are published?

Yes, this is a long overdue change.

Question 23:

Do you agree with the proposals regarding biennial independent governance reviews? What are your views on the format and assessment criteria?

Yes, and SYPA has already undertaken two such reviews since the formulation of the Good Governance proposals.

We believe that delivering these reviews through a peer led mechanism is in line with the way in which LGPS has historically developed and shared good practice and works with the grain of the scheme, and the broad process set out in the consultation seems appropriate. This will also reduce the cost of such reviews to the scheme and further reduce dependency on external consultants.

In terms of the assessment criteria, we believe that assessment against aspects of the following four dimensions will give a comprehensive view of whether a fund is meeting the relevant requirements.

- People – Are the right people (both officers and members) in place and with the right knowledge and experience and access to the right advice to effectively run the Fund.
- Process – Are the right processes in place to ensure that decisions are taken at the appropriate level and are based on the right information and with the right degree of transparency.
- Performance- Are the combination of people and process is delivering the performance sought.
- Partnership- How well does the Fund work with others (particularly the Pool) to deliver its objectives.

A framework of this sort would allow a comprehensive assessment to be made of how effectively the AA is discharging its responsibilities towards the Fund. Importantly this cannot be a pass/fail assessment. All these reviews will identify some areas for improvement as no fund will be perfect. However, where significant weaknesses are identified there also needs to be a view taken on whether there is the willingness and capacity to address the weaknesses. This goes to the degree of self-awareness among the members and officers exercising stewardship over the Fund, which will be important in assessing whether identified weaknesses will be addressed.

Question 24:

Do you agree with the proposal to require pension committee members to have appropriate knowledge and understanding?

Yes, members of the Authority effectively commit to this through approving the Learning and Development Strategy each year, but this is currently effectively voluntary so removing the long-standing anomaly of differing requirements between Board and Committee members is welcomed.

Question 25:

Do you agree with the proposal to require AAs to set out in their governance and training strategy how they will ensure that the new requirements on knowledge and understanding are met?

Yes, this is the logical content of such a strategy and managing the inevitable turnover in membership. Such consideration should also include the reflection of the level of commitment to developing knowledge and understanding within AAs members allowance schemes.

Question 26:

What are your views on whether to require administering authorities to appoint an independent person as adviser or member of the pension committee, or other ways to achieve the aim?

We are supportive of this as a concept and the Authority already has two independent investment advisers whose role could be broadened in line with the requirements suggested. These current arrangements work well and are strongly supported by members of the Authority. However, we are wary of the suggestion that such roles would be members of the Committee / Authority and of the suggested qualification requirements. This seems to imply a desire to move to more of a professional trustee model. The democratic accountability of the LGPS is an extremely important aspect of the scheme and while change is undoubtedly necessary and accepted (as indicated in our previous answers) we need to be careful not to undermine this. We would welcome the opportunity to discuss the proposed arrangements and the thinking behind them in this area further with officials.

Pool governance

Question 27:

Do you agree that pool company boards should include one or two shareholder representatives?

Yes, and Border to Coast already has this in place. However, it is important to recognise that all Non-Executive Directors owe their duty to the interests of the company and not to those who nominated them. This could in certain circumstances be challenging. Different pools have taken different approaches to this matter but given the commitment of time required which amounts to at least 30 days per annum and the requirements for FCA approval there are an increasing range of hurdles which may make filling these roles more difficult.

Question 28:

What are your views on the best way to ensure that members' views and interests are taken into account by the pools?

The Border to Coast Joint Committee includes two Scheme Member Representatives elected through the employee side members of the 11 Partner Fund Local Pension Boards who can effectively contribute to the oversight of the pool company. Similarly, the pool company is represented at meetings of individual pension committees through which it is exposed to the views of scheme members. It is, however, accepted that this does not necessarily provide a comprehensive or representative picture of scheme member views. This is best achieved by funds effectively consulting during the development of key strategies such as the investment strategy taking the views expressed into account as appropriate and ensuring that the pool delivers as appropriate.

It would be possible to appoint a scheme member Non-Executive Director of the pool company. However, there is the potential for them to feel the role compromises their ability to represent scheme member views and the nature of the role in an FCA regulated entity means that the time commitment (30 days per year) may make such a role impossible for many scheme members.

Question 29:

Do you agree that pools should report consistently and with greater transparency including on performance and costs? What metrics do you think would be beneficial to include in this reporting?

Yes

Equality impacts

Question 30:

Do you consider that there are any particular groups with protected characteristics who would either benefit or be disadvantaged by any of the proposals? If so please provide relevant data or evidence.

No