## Review of the Structure of the Scottish Local Government Pension Scheme

**CONSULTATION RESPONSE FORM**

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| **Instructions** Responses in this form should be drafted in conjunction with the accompanying consultation report. To respond, please complete the **respondent details** and as many of the **consultation questions** your organisation wishes to complete and return the form via email to the Pensions Institute at [consultation@pensions-intitute.org](mailto:consultation@pensions-intitute.org) no later than **Friday, 7 December 2018**.  This consultation is being conducted in electronic form only, so **responses must be emailed**; hard copy posted or delivered responses cannot be received. Any queries about the consultation should be addressed to Matthew Roy, Fellow, Pensions Institute at matthew.roy@pensions-institute.org. |

**RESPONDENT DETAILS**

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| **Name of responding organisation(s)** Please list the full name of each organisation participating in this response. | **Organisation type** Is your organisation an administering authority, employer, or employee group? Please record for each responding organisation. |
| Argyll and Bute Council | Local Authority employer |
| **Authors** Please list any people that wish to be recorded as authors of this response, including name, job title and organisation. | **Consent** Please confirm each author consents to their information being retained for analysing the consultation responses by writing ‘confirm’ by their name. |
| Jane Fowler, Head of Improvement and HR | confirm |
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| **Date** Please date the response. | date |

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| **Covering information** If you wish to include covering information with your response, please include the text here. The text can wrap onto additional pages if needed. |
| This consultation response draws on views discussed by senior officers local government in SPDS and Directors of Finance.  It is our view that the current system is working well and has significant strengths. The importance of the scheme to its thousands of members is such that reform should only be undertaken with extreme care. Any changes must be based on the evaluation of statistically sound and compelling empirical evidence.  It is our view that the current arrangements for the LGPS are well established, having been in place with Administering Authorities since 1995. There is a track record of delivery, supported by long established relationships with a range of respected fund managers.  All 11 administering authorities demonstrate high levels of compliance with good governance standards. Information on the funds is transparent and available to all interested parties through these governance arrangements.  All funds have delivered positive net investment returns over time and the recent  valuation demonstrates that funding levels in all 11 funds were very high, with most funds exceeding, and all funds almost meeting, their primary objective i.e. to have a fund of assets that is sufficient to meet pension fund liabilities as they fall due. Currently the LGPS Scotland has over £44bn of assets under management.  The Funds have continued to improve and develop over time. Recent initiatives such as the LGPS transparency code, the advent of pension boards, with strong employee representation need time to bed in. There are already improving levels of collaboration between Councils and the sharing of benchmarking data. These need to be given time to bed in and be properly evaluated. Only if this evaluation provides evidence for change should any further changes be considered. Any further proposed change must be widely consulted upon.  Employee participation rates in the LGPS are high and stable. No fund has seen significant withdrawals of assets by members following the implementation of recent pension freedoms. The advent of auto enrolment has seen an increase in membership. This broadly stable membership position indicates members value their pension benefits and trust that they are being well managed.  The costs of administering the scheme in Scotland are relatively low and stable, with some variation in the level of administration cost between funds which may be a result of different level of fee disclosure and of relative size.  It is very important that any changes to the LGPS improve the current situation, deliver demonstrably lower costs, higher funding levels and better governance than are being delivered at present and that these can be evidenced.  There is a risk that implementing large scale reform may have a de-stabilising effect on the membership and this must be carefully considered before any changes are made.  There is a process of ongoing Pension Fund reform in England and Wales which has, as yet, provided no strong evidence on the effect of pooling.  There is no evidence to suggest that the merger of funds to create larger bodies or pools will deliver better investment returns simply by virtue of their enhanced scale.  Pension fund investment is a long term business and the only truly useful time period horizon over which to assess performance is over the long term. The LPGS in Scotland has performed well for its members over the 20 year period it has been operating in its current form.  In general terms, whilst economies of scale may be possible, there will be costs associated with re-organisation of the LGPS which will offset these benefits, at least during the transition phase. These costs are likely to be significant and cannot be ignored. The impact on capacity to support council functions in those councils which are currently managing pension funds should not be ignored if reform requiring TUPE transfer of finance staff is required.  Many of the benefits being sought by the reforms in England and Wales are already being delivered without the need for costly structural reform. The primary duty of the LGPS is to take decisions which are in the best interests of its members.  Investment in infrastructure features heavily in the consultation. The primary objective of a pension fund is to build up a fund of assets sufficient to meet future pension fund liabilities. It is not to fund public infrastructure projects. Decisions on investment in infrastructure must only be taken where the project delivers an investment return to the fund as part of a diversified portfolio. The purpose of the funds are not to deliver public investment in infrastructure at the lowest possible cost to the taxpayer.  It is our strongly held view that any changes to the structure of the LGPS in Scotland must place the interests of the scheme members at the forefront of decision making. In considering any change a balance needs to be struck between cost reductions, the need to deliver sound investment returns from scheme assets to meet scheme liabilities, the ongoing affordability of the scheme to employers and the aspiration to invest in public infrastructure through appropriate vehicles. |

The consultation questions follow.

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| **CONSULTATION QUESTIONS** Question 1: Retain the current structure with 11 fundsThe text can wrap onto additional pages. |
| 1. Cost of investing:  * How well informed do you feel about the investment costs in your fund? What information do you rely on to specify and measure these?   Detailed information is available on investment in all funds is accessible through the annual accounts, the AGM and other LGPF meetings. We are assured that the funds comply with accounting requirements as set out by CIPFA and that all fees are disclosed in the annual accounts as per the Fee transparency code.   * How well does the current system manage investment costs?   The costs of investment again are available and transparent to interested parties. Limiting the fee level is an important consideration, but is not a simplistic measure. Decisions may be taken to pay additional fees to secure higher performing investments.   * How would you improve the measurement and management of investment costs in the current system?   No further comment   1. Governance:  * How well informed do you feel about the governance of your fund? What information do you rely on to measure this?   Local governance of the fund is transparent and all documentation is available via the governance channels, Board meetings, AGM and annual accounts.   * How well is the current system governed?   The governance of the system was assessed in 2016 by KPMG following the 2015 changes. KPMG stated:  *These arrangements need to be given time to bed in although they have improved employee representation and would appear to be to be working effectively. It would seem too early to consider making further changes to the current arrangements without the necessary data to understand how effective still relatively new governance changes have been.*  Audits of the funds take place annually as set out in statute and no concerns have been highlighted.     * How would you improve governance of the current system?   We would recommend, in line with the Directors of Finance, that the accounts, statement of investment principles etc should be made publically available.  *How important is it to maintain a local connection with respect to oversight and strategy?*  The SLGPS is an important facet of local Council democratic governance. Local connection to local government and to employee representatives is important for oversight. There are thousands of current and former local government employees who depend on the secure and effective management of the funds for their financial wellbeing. It is very important that the finds are open and transparent. If there were to be a single, central fund, there would have to be an associated local governance structure established to ensure appropriate scrutiny.  The decisions taken by the fund have a significant impact on local authority budgets. Ownership at a local level keeps the responsibility for oversight of the funds at the forefront of decision making as it affects budgets through for example pay structure, early retirals etc.  How would you determine if the benefits of a local connection in governance outweigh the benefits of scale?   1. Operating risks:  * How well informed do feel about the operating risks of your fund? What information do you rely on to specify and measure these?   Pension funds hold regular meetings with fund managers to assess and understand the risks associated with their investments. The funds operate robust risk management on the basis of risk assessments and risk registers.   * How well are operating risks managed in the current system?   Reports and documentation as scrutinised by external audit indicate that these risks are being managed effectively.   * How would you improve the measurement and management of operating risks in the current system?   The funds should publish their risk registers.   1. Infrastructure:  * How well informed do you feel about your fund’s investments in infrastructure? What information do you rely on?   Investment in infrastructure is established as a part of the investment portfolio. The main issue is that the fund only considers investment in infrastructure when it is the best decision to maximise the return on investment for the fund. It is essential that the decision is not taken in order to provide low cost capital for investment in public infrastructure.   * How do you rate the current system’s ability to invest in infrastructure?   There are good examples of the LGPS investing in infrastructure as part of the Asset Allocation Strategy, which Strathclyde has invested £330m in.   * How would you increase investment in infrastructure in the current system?   The Scottish Futures trust has recently examined this issue and while there appears to be a political desire to see greater investment in public infrastructure, the structures to enable large scale investment in infrastructure and balance suitable returns within an optimised risk profile are not yet suitably developed. Development of such a model would help to facilitate infrastructure investment.   1. Do you have any additional comments about this option?   No |

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| Question 2: Promote cooperation in investing and administration between the 11 funds The text can wrap onto additional pages. |
| 1. Cost of investing:  * What impact do you think promoting agreements between funds would have on investment costs?   Joint agreements on collaborative investments could have a positive impact on fees.   * What would be the positive impacts?   This could deliver economies of scale to smaller funds and may give them greater confidence in investing in a wider range of diversified assets.   * What would be the negative impacts?   Any collaboration would require to be specifically set out and agreed through the appropriate governance structures.   1. Governance:  * What impact do you think promoting agreements between funds would have on governance?   Sharing best practice and knowledge could have a positive impact.   * What would be the positive impacts?   Collaboration would enable us to retain local expertise in Finance and HR functions, which would retain resilience across Scotland. This knowledge can provide wider benefits to individual councils and the local government community. This would be lost and diluted under a formal restructuring proposal, but could be retained through a collaborative model. Current governance arrangements would not be compromised.   * What would be the negative impacts?   There may be a perceived dilution of elected member involvement and influence in favour of officers.   1. Operating risks:  * What impact do you think promoting agreements between funds would have on operating risks?   Significant voluntary cooperation already exists between the funds that share best practice and access a range of services through national procurement framework.   * What would be the positive impacts?   There may be positive impacts on economies of scale.   * What would be the negative impacts?   Formal agreements would need to be documented, which would incur legal costs. There is the potential for disagreement on the proposed arrangements. It would be important to ensure that this did not result in the need for additional administration,   1. Infrastructure:  * What impact do you think promoting agreements between funds would have on funds’ ability to invest in infrastructure? * What would be the positive impacts?   Smaller funds would have access to a wider range of investment opportunities. Co investment provides the opportunity to share legal, technical and due diligence costs.   * What would be the negative impacts?   This may result in very complex administrative arrangements.   1. Do you have any additional comments about this option?   No |

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| Question 3: Pool investments between the 11 funds The text can wrap onto additional pages. |
| 1. Cost of investing:  * What impact do you think pooling investments between funds would have on the cost of investing?   This would require significant restructuring and significant cost. It has not been proven that a large fund always has lower costs.   * What would be the positive impacts?   Smaller funds may benefit from fee reductions but Strathclyde is unlikely to see any benefit due to its current scale.   * *What would be the negative impacts?*   May reduce the number of managers and thus lose knowledge to the sector, which may have a negative impact on fund performance.   * If asset pooling were possible, under what circumstances should a fund consider joining an asset pool?   Pooling should only be considered if it would bring significant advantages to the individual fund.   * Under which circumstances should the SLGPS consider directing funds to pool?   Only if there was evidence of failures at the local level.   1. Governance:  * What impact do you think pooling investments between funds would have on governance?   Pooling is likely to require additional governance and infrastructure.   * What would be the positive impacts?   Current governance structures would remain in place and this would avoid costly restructuring.   * What would be the negative impacts?   Added layer of bureaucracy would be needed under this option. Pooling would result in a reduction in expertise across local government.   1. Operating risks:  * What impact do you think pooling investments between funds would have on operating risks? * What would be the positive impacts? * What would be the negative impacts?   There is no evidence that the pooling arrangements in England and Wales have delivered any cost benefits or improvements in governance. Although there is no evidence yet, there are indications that the process has been problematic with concern over accountability and governance. The costs could be high and would require substantial professional advice from a range of sources.   1. Infrastructure:  * What impact do you think pooling investments between funds would have on funds’ ability to invest in infrastructure? * What would be the positive impacts?   What would be the negative impacts?  Local investment may be detrimentally impacted. If more investment in Scotland’s infrastructure is sought, then a robust business case for each demonstrating the benefit of investment must be developed and presented to the funds for consideration.  Do you have any additional comments about this option?  No |

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| Question 4: Merge the funds into one or more new funds The text can wrap onto additional pages. |
| Cost of investing:   * What impact do you think mergers between funds would have on the cost of investing?   This would require significant restructuring at significant cost to no apparent benefit with no evidential basis for doing it.   * What would be the positive impacts? * What would be the negative impacts?   The consultation document refers to significant cost savings as a potential advantage, but there is no evidence presented to show that this would be the outcome.  The proposal remains untried and the risks are not fully understood. It is not clear what impact this would have on funding levels, which could potentially change for employers. It is not clear how a merger would affect/assist investment in infrastructure.   * If merging were possible, under what circumstances should a fund consider a merger?   A merger should only be considered if there are demonstrable, evidence based benefits in doing so.   * Under what circumstances should the SLGPS consider directing funds to merge?   Only where there is evidence of governance failure or inability to meet future liabilities. This is not the case with the current LGPS.  Governance:   * What impact do you think mergers between funds would have on governance?   There would be a diminution in local involvement in fund governance.   * What would be the positive impacts?   There could be savings on back office functions, but this may also have a detrimental effect where there are shared roles between Councils and funds.   * What would be the negative impacts?   There is a risk that a new arrangement would fail to perform as well as the current arrangements and would introduce unnecessary risk into a highly important financial activity.  New arrangements would be costly in administration, advice, TUPE etc.  Operating risks:   * What impact do you think mergers between funds would have on operating risks? * What would be the positive impacts? * What would be the negative impacts?   Expertise would be lost across all councils. Restructuring would be expensive. There is no robust evidence basis for a change and risk would be increased. Transition may unsettle membership and result in people transferring their funds out, which would have a detrimental effect on the fund resource. New entrants may be discouraged from joining.  Infrastructure:   * What impact do you think mergers between funds would have on funds’ ability to invest in infrastructure?   A larger fund may have a greater appetite for infrastructure investment. But the proposal is untried and the risks are not understood. It is not clear what the impact would be on funding levels.   * What would be the positive impacts? * What would be the negative impacts?   New governance arrangements would be required and this would incur additional costs to transition to the new arrangements.  TUPE transfer would apply to staff who spend a significant element of their time on pensions matters. There are potential redundancy costs to be met by pension funds.  The move to formal restructure would sever links to local decision making with regard to investment strategy and asset allocation removing a key role for elected members in the governance of pension funds.  Do you have any additional comments about this option?  The merger option is not preferred for the following reasons:   * The current performance of the funds is healthy * It remains an untested model * Administration would suffer as evidenced by the transfer to SPPA of police and fire pension administration * Local involvement would cease * Potential risk of single point of failure * There would be job losses, impacting on the economy |

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| Question 5: Preferred and additional options The text can wrap onto additional pages. |
| 1. Which option does your organisation prefer? Please explain your preference.   Option 2  Collaboration already exists and extending this is likely to be beneficial if extended.  Promotion of co-operation should be carried out through a framework as opposed to legislation.  It provides some positive benefit opportunities without incurring significant additional cost.  It carries the least level of risk. The other options, particularly merging the funds, carry significant known and unknown risk and there is no evidence presented to justify this radical change and heightened risk.   1. What other options should be considered for the future structure of the LGPS?   No other options proposed   1. What would be the advantages and disadvantages of these other option for funds’ investment costs, governance, operating risks and ability to invest in infrastructure?   N/A   1. Are there any other comments you would like to make?   As set out in the introduction, the SLGPS in its current format of 11 funds is healthy and performing well. There has been no evidence base presented to depart from the current arrangements, although close collaboration on some areas of activity may improve efficiencies. |

The consultation questions end.