## 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. |
| Fife Council | Employer and Administering Authority |
| **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. |
| Elaine Muir, Head of Finance, Fife Council  Laura Robertson, Finance Operations Manager, Fife Council | Confirm |
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| **Date** Please date the response. | 12.12.18 |

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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. |
| Fife Pension Fund recently entered into a collaboration arrangement with Lothian Pension Fund for Investment related activities , this means that;-   * Delegation of investment strategy implementation to the Head of Finance taking advice from professional Investment Strategy Panel of internal and external advisers. * Draw on experience of LPF internal investment team |

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?   Fife Pension Fund comply with the accounting arrangements set out in CIPFA’s guidance on Accounting for Local Government Pension schemes. However, there remain concern around any “hidden” or “embedded costs” that are not disclosed as part of that process.  Aware that fund managers have signed up to the LGPS fee transparency code and welcome this.  Can see the benefit of this and it’s an area that should be further explored.   * How well does the current system manage investment costs?   Fee levels are of importance to all pension funds however, particularly for smaller funds there are limited resources and experience to manage and challenge investment costs or to analyse in depth. Larger funds may be better equipped to actively manage costs.  Consideration also needs to be given to the level of performance achieved for those costs.   * How would you improve the measurement and management of investment costs in the current system?   The introduction of the Transparency code has increased awareness and interest in understanding investment costs. Fund managers should be required to comply with the code and disclose fee structures as appropriate. Further exploration and explanation is required to understand the dependencies and resultant fee costs from asset out performance. Funds should understand what they are agreeing to and the results.   1. Governance:  * How well informed do you feel about the governance of your fund? What information do you rely on to measure this?   The Committee makes decision around the investment strategy for the fund, relying significantly on external investment advisers. There are questions around whether pension fund management is a core function of the Council?  Committee also seeks advice and clarity on issues of Corporate and Social Responsibility from external partners.   * How well is the current system governed?   LGPS Pension Funds are subject to statutory external audit on an annual basis and the subsequent audit reports are positive and evidence that there are sound governance arrangements in place.  In recent years there has been significant improvement in the External Audit reports and the most recent report was a very positive report with a few achievable recommendations and actions  The introduction of Pension Fund Boards is fairly new and will take time to settle down.  Fund comply with MFID 2   * How would you improve governance of the current system?   Pension Boards provide an added level of scrutiny with representation from employee and employers. Experience is shared across the 11 Funds through the Investment Governance Group and Scottish Local Government Pension Scheme group.   * How important is it to maintain a local connection with respect to oversight and strategy?   Unsure how appropriate a local connection is. There is little correlation between decision making and local Council. The more important connection is that decision making around strategy is made by well informed, well trained and experienced independent group of individuals – which should be the make-up of the decision making body, with the best interest of the pension fund members at heart.  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?   Reliant in investment advisers and Council Staff and Committee/Board members to assess overall operating risks. Not all funds have the same available internal resource to identify and mitigate and manage risk. Key person risk in smaller funds exacerbates this.  Funds have opted up to professional status via MiiFID2 which means funds should have access to the appropriately qualified advice to ensure risks are managed.  Pension Funds have risk management arrangements in place.   * How well are operating risks managed in the current system?   As above, this will differ across the range of sizes of funds. Smaller funds rely more heavily on external advisers.   * How would you improve the measurement and management of operating risks in the current system?   By looking at what other funds are doing in terms of risk mitigation and learning and assessing best practice in this area.   1. Infrastructure:  * How well informed do you feel about your fund’s investments in infrastructure? What information do you rely on?   Fairly well informed through meetings with fund managers and from performance information from them.   * How do you rate the current system’s ability to invest in infrastructure?   The current system does support investment in infrastructure whilst taking into account the fiduciary duty. Examples of local and other investment across Scotland. More about ensuring appropriate returns.   * How would you increase investment in infrastructure in the current system?   Increasing investment in infrastructure would be dependent on the investment strategies across each of the funds since investment in assets flows from this. There would be a question for each fund as to whether increasing investment in infrastructure was the right thing to do for the fund. It would depend as to whether this was an objective linked with the investment strategy as to whether this would be a desired outcome. Fiduciary duty would also be a consideration.   1. Do you have any additional comments about this option?   Current system works, with good funding levels across SLGPS, with contribution rates remaining stable. Positive investment returns in recent years. |

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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?   Has the potential to increase opportunities to exploit economies of scale and reduce investment but is not inevitable   * What would be the positive impacts?   Greater opportunity to look at opportunities for joint investment, and potentially more direct investment in e.g. infrastructure, where collaborative partners have shared beliefs and objectives and common asset types.  Has the potential to improve investment returns through scale, if adopted.   * What would be the negative impacts?   Over reliance on others in other organisations.  Move away from undertaking effective due diligence at a local level.  Loss of input at a local level maybe a concern   1. Governance:  * What impact do you think promoting agreements between funds would have on governance?   Would help encourage best practice in relation to governance and learning from each other beyond that which exists at present.  Known and established local governance agreements would remain in place allowing the Pension Board arrangement to evolve and strengthen   * What would be the positive impacts?   Smaller funds could benefit from the scale of larger partners and could ‘buy in; to their resource and expertise.  Probably a more cost effective change to governance than pooling or merging.  No sale and repurchase of assets as might be the case with other options.   * What would be the negative impacts?   Could slow down decision making and processes the more partners are involved in any one collaborative model. Logistically less manageable the more partners are involved.  Could take a long time to move funds forward to voluntarily work in this way. Resistance to change could slow things down even further.   1. Operating risks:  * What impact do you think promoting agreements between funds would have on operating risks?   Responsibility and accountability could become unclear and/or complex  Voluntary cooperation already exists with funds across Scotland therefore some of the risks are known and have been mitigated to a certain extent.   * What would be the positive impacts?   Funds would retain their own investment strategies relevant to their local fund requirements, funding levels, risk appetite.  Local expertise would be retained e.g. staff with knowledge and expertise in pensions, investment, and an understanding of pension benefits this is an asset within the Local Authorities. This would potentially be lost in a merger arrangement.  Economies of scale   * What would be the negative impacts?   May be slow or difficult to ensure operational consistency and to reach a point where collaborative partners are progressing operationally to similar timescales and in a consistent manner and using a similar ‘language’. Each partner will have competing priorities which might be different for each organization.  There is a limit to the size of a collaborative model e.g. the current collaboration between Lothian, Falkirk and Fife would be difficult to expand to add yet another partner.  Formal agreements are required to establish legal position.   1. Infrastructure:  * What impact do you think promoting agreements between funds would have on funds’ ability to invest in infrastructure?   Increasing investment in infrastructure would be dependent on the investment strategies across each of the funds since investment in assets flows from this. There would be a question for each fund as to whether increasing investment in infrastructure was the right thing to do for the fund. It would depend as to whether this was an objective linked with the investment strategy as to whether this would be a desired outcome.  Agreements between funds would impact on the fund’s ability to invest in infrastructure but it might open up opportunities previously not available in the case that investment in infrastructure was in line with the investment strategy.   * What would be the positive impacts?   Greater access to opportunities  Cost sharing  There is sufficient evidence and experience to support this approach   * What would be the negative impacts?   Potential time taken in decision making  Capacity of Funds to collaborate.   1. Do you have any additional comments about this option?   Fife has recently review into a collaboration arrangement with Lothian and Falkirk Pension Funds based on research, business case and evidence. It is believed that the collaboration promotes the interests of the pension fund members and the employers and is beneficial for the overall governance of the fund. |

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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?   There is evidence to suggest that scale in investments can bring down the cost of investing, however, there is also evidence to suggest that pooling investment can be extremely costly.   * What would be the positive impacts?   There may be a positive impact on fees   * What would be the negative impacts?   Costs of doing – including set up costs and any additional governance costs.  Loss of control  Decision making on investing and disinvesting  The time taken to recoup set up costs could be a consideration.   * If asset pooling were possible, under what circumstances should a fund consider joining an asset pool?   If pooling provided opportunities and advantages that are currently unavailable   * Under which circumstances should the SLGPS consider directing funds to pool?   Funds are underperformed and pooling would rectify this. This needs to be balanced against the risk of doing so.   1. Governance:  * What impact do you think pooling investments between funds would have on governance?   Known and established local governance agreements would remain in place allowing the Pension Board arrangement to evolve and strengthen. Any additional governance arrangements required could be costly.   * What would be the positive impacts?   Pooling would not eliminate the potential for collaborative working – this could still happen at a local level and sharing of knowledge, experience and expertise across funds would no doubt be beneficial in this scenario  Benefits in sharing administration would not be precluded under this option and could still be looked at as a further development.  There is no guarantee there would be a positive outcome.   * What would be the negative impacts?   Loss of experienced individuals at a local level to investment pools. Duplication of effort both within the pools and in Local Authorities  Responsibility and accountability could become unclear and/or complex  Authorities would be heavily reliant on external advisers in organising a change of this nature. This will be costly and there will be risk associated with that heavy reliance.   1. Operating risks:  * What impact do you think pooling investments between funds would have on operating risks?   There is likely to be market risk, and potentially substantial costs associated with divesting and then reinvesting into a pooled investment.   * What would be the positive impacts?   Funds would retain their own investment strategies relevant to their local fund requirements, funding levels, risk appetite  Local expertise would be retained e.g. staff with knowledge and expertise in pensions, investment, and an understanding of pension benefits this is an asset within the Local Authorities. This would potentially be lost in a merger arrangement.   * What would be the negative impacts?   Duplication of effort both within the pools and in Local Authorities increasing cost overall  Little evidence on which to develop the business case.  Responsibility and accountability could become unclear and/or complex  Loss of experienced individuals to investment pools. Duplication of effort both within the pools and in Local Authorities  The need for the fund to recoup the cost of change and the potential length of time this will take and the impact on the performance of the funds.   1. Infrastructure:  * What impact do you think pooling investments between funds would have on funds’ ability to invest in infrastructure?   Pooling could create a large investment vehicle with the capability of funding infrastructure project and savings through economies of scale.   * What would be the positive impacts?   Access to large projects and reduce costs   * What would be the negative impacts?   Need to consider any potential conflicts of interest.  Do you have any additional comments about this option?  Learning from the England & Wales experience will be of benefit – e.g. what benefits are being delivered when compared with original arrangements. |

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| Question 4: Merge the funds into one or more new funds The text can wrap onto additional pages. |
| 1. Cost of investing:  * What impact do you think mergers between funds would have on the cost of investing?   There is evidence to suggest that scale in investments can bring down the cost of investing, however, there is also evidence to suggest that merging pension funds can be extremely costly.   * What would be the positive impacts?   See Question 3   * What would be the negative impacts?   See Question 3   * If merging were possible, under what circumstances should a fund consider a merger?   See Question 3.   * Under what circumstances should the SLGPS consider directing funds to merge?   See Question 3   1. Governance:  * What impact do you think mergers between funds would have on governance?   Anticipated this would have a significant impact on local governance.   * What would be the positive impacts?   Takes away key person risk for smaller funds  Greater efficiency in terms of governance across Scotland of 1 or more funds – fewer people across the Country involved in governance e.g. committee members and pension boards as there would be fewer of them.  Enhanced skills of people dealing with governance   * What would be the negative impacts?   Loss of local involvement in governance and decision making   1. Operating risks:  * What impact do you think mergers between funds would have on operating risks?   Little evidence on which to develop the business case. Unknown costs v’s unknown benefits   * What would be the positive impacts?   Larger funds would retain the investment strategies.   * What would be the negative impacts?   Unclear how this would impact on funding levels across all funds. Some winners? Some losers? Associated investment strategy approach is also unclear.  Would there be an impact on Contribution Rates?  Loss of Pensions staff from Local Authorities to new Pension Fund would need to be understood – e.g. what impact this might have on Local Authorities whereby staff have parts of other functions as their business as usual.  Significant implementation costs  Impact on contribution rates will be unknown  Impact on membership levels will be unknown   1. Infrastructure:  * What impact do you think mergers between funds would have on funds’ ability to invest in infrastructure?   See Question 3   * What would be the positive impacts?   See Question 3   * What would be the negative impacts?   See Question 3   1. Do you have any additional comments about this option?   There could likely be efficiencies to be gained in relation to systems costs in relation to administration of 11 funds being brought together e.g. one contract for Altair. |

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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.   The Fife Pension Fund would prefer the option of further collaboration.  The reasons for this preference are as follows:  Fife Pension fund has recently entered into a collaborative partnership with both Lothian and Falkirk Pension Funds and this has been progressed based on a body of evidence collected over a substantial period of time and based on an evidence based business case.  This partnership has been agreed on the basis that those who govern the pension fund believe that it is in the interests of both the pension fund members and the employers and for the overall governance of the fund.  There is still some way to go to really maximise the benefits from this approach and the Pension Fund committee believes that these benefits should first be fully explored and exploited before further change is considered. It is still too early to have a proper understanding of the benefits that this way of working can deliver.  This has been a voluntary change in the model for managing the Fife fund and the Fife Committee believes that fiduciary duty would be compromised by moving to any enforced model.  The Fife Committee believes that performance of the fund is strong and does not want to compromise this position.   1. What other options should be considered for the future structure of the LGPS?   The Fife Pension Fund Committee remains open minded about possible changes in the future but believe that any future changes must be based on a significant body of evidence that leads the Committee to believe that the Fife pension fund members would be better served by any different model.  However, at this point in time the Committee believes that there is not enough detailed evidence to suggest that any other model would result in better performance or management of the Fife Pension Fund.  The Committee also believes that there is no place for imposed wholescale structural change in relation to management of the LGPS as this takes no cognisance of risks/benefits/stability of individual funds.   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?   It is not clear that any of the other proposed changes would alter the opportunities to be gained from working collaboratively. However, there may be a limit as to how many partners can collaborate before a partnership becomes too unwieldy, so there may be additional economies of scale from merging/pooling.   1. Are there any other comments you would like to make?   Fife considers the introduction of compulsory performance reporting and cost benchmarking across all funds as a positive step to aid transparency. |

The consultation questions end.