ASSOCIATION OF CONSULTING ACTUARIES

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16 January 2025

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Dear all

ACA response to Consultation on Local Government Pension Scheme (England and Wales): Fit for the future

I am writing on behalf of the **Association of Consulting Actuaries (ACA)** in response to your consultation above.

Members of the Association are all qualified actuaries and are subject to the Actuaries' Code of the Institute and Faculty of Actuaries. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering most members of private sector defined benefit pension schemes.

The ACA is effectively the "trade association" for consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

Members of the ACA provide advice to thousands of pension schemes, including most of the funded public service schemes – most notably the funds that make up the Local Government Pension Scheme or LGPS. Members however are also involved in advising some of the employers that participate in the LGPS.

Our responses to your specific questions are set out in the **appendix** below.

We hope that you find the contents of this letter of assistance. We would be happy to discuss them further if that is helpful. In that event, please contact me at Robert.Bilton@hymans.co.uk on **0141 566 7936**.

Yours faithfully

Robert Bilton
Chair, Pension in Public Services Committee
On behalf of the Association of Consulting Actuaries Limited

APPENDIX

ACA response to consultation on Local Government Pension Scheme (England and Wales): Fit for the future

Question 1: Do you agree that all pools should be required to meet the minimum standards of pooling set out above?

The minimum standards are a significant development of the pools' role in the LGPS. As such, we have concerns over the timescales set out in the proposal. The pools are being expected to perform new roles, whilst continuing to build out their current functions, in just over a year's time.

This increases the risk of poor investment outcomes for the LGPS, and therefore the public finances of local government and taxpayer.

Our comments on the specifics of each standard are covered in the remaining questions of our response.

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?

We believe that if Administering Authorities retain the responsibility for the LGPS Fund's liabilities, then they should also retain the responsibility for setting the investment strategy - both investment objectives and strategic asset allocation. How a fund then executes this responsibility should be up to them.

If a pool does set the high-level strategic asset allocation, there should be requirements on the pool to explain and demonstrate how they have taken local fund factors into account (such as cashflow profile, funding level, liability profile, employer base). It will be important to have a clear understanding of how the pool will monitor or be aware of changes to the Fund which may require a change to their strategic asset allocation.

To be able to deliver a Fund's strategic asset allocation effectively, a pool should consult with the partner funds to ensure a strategy can be delivered rather than focussing solely on efficiency of implementation.

Question 3: Do you agree that an investment strategy on this basis would be sufficient to meet the administering authority's fiduciary duty?

We believe that fiduciary duty would be met only if pools were able to effectively deliver on Funds' investment strategy, including at a sub-asset class level, and considering any relevant responsible investment objectives for each Fund. Our rationale is that these are the biggest drivers of investment returns and would have the most material impact on the future evolution of a fund's funding position.

We do not believe that the proposed model will allow funds to specify this level of detail and therefore be able to comply with their fiduciary duty.

Question 4: What are your views on the proposed template for strategic asset allocation in the investment strategy statement?

A consistent template across pools and Administering Authorities will help with efficiency, particularly if Administering Authorities can invest across pools.

We don't believe the proposed template is sufficiently granular enough to be able to effectively deliver a Fund's strategic asset allocation. For example, being able to specify preferred regional equity allocations; having control on the proportion of the assets that are invested actively or passively, and to which asset classes; having the ability to invest in thematic and nascent asset classes that support a Net Zero ambition, such as to natural capital or climate solutions. We also believe the fixed income and alternatives buckets are too broad and do not allow Funds to be able to be more granular with their asset allocation.

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?

If a pool has the capability to deliver investment advice to partner Administering Authorities, and an Administering Authority wishes to take up this option, then this should be allowed. However, the management of actual and perceived conflicts of interests will need to be carefully considered and transparently governed.

We do not believe that all Administering Authorities should have to take investment advice from the pool. As the ACA includes investment consulting actuaries, we are conflicted in answering this question however, we believe it is important for Administering Authorities to be able to seek independent investment advice to enhance overall governance, oversight and scrutiny of the investment decisions made by the pools.

Given the size of the assets in the LGPS and the impact that being unable to meet future pension promises would have on members and/or local government, limiting the availability of, and therefore potentially quality of, advice to Administering Authorities seems like a backward step in improving the governance of the scheme.

There is already a deep investment advisory market to the LGPS which provides a ready-made option for Administering Authorities to obtain their primary source of investment advice or further advice or input to consider advice provided 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?

We do not believe that this is a necessary requirement to meet the stated objectives of pooling. To date, different approaches and operating models have been developed and taken by the pools which have successfully delivered against the government's original aims. The lack of any clear evidence that one operating model is better than another, suggests that this requirement should be dropped for one that focusses on tangible outcomes.

We also note that the implementation timeframe proposed by the government is very challenging, particularly for those pools that currently do not have FCA authorisation. This could lead to an inefficient and potentially costly transition of local fund assets to each pool, which would be exacerbated if there were subsequent mergers across pools.

Question 7: Do you agree that administering authorities should be required to transfer all listed assets into pooled vehicles managed by their pool company?

We are supportive of the proposal for Administering Authorities to transfer all listed assets into their pool company only if the pool is able to fully support the investment strategy, including the responsible investment objectives, of each partner Fund.

Question 8: Do you agree that administering authorities should be required to transfer legacy illiquid investments to the management of the pool?

We do not see the benefits of transferring legacy illiquid investments to the management of the pool. This would require additional resource at each pool to be able to manage the cashflow requirements for each legacy fund including drawdown management, which typically have relatively short payment windows, and distribution management. Most Administering Authorities have established and effective processes for meeting the cashflow needs of these investments. Transferring the ownership of these investments to a pool would incur both legal and management costs.

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?

Some pools will not have the necessary expertise nor infrastructure to be able to deliver the proposals, most notably around illiquid assets. Some pools currently outsource some of their manager selection decisions to third parties (such as in the real asset space). Attracting experienced talent to the pools may be challenging if remuneration packages are not competitive enough compared to the wider asset management community.

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?

The timeframe is challenging for ensuring FCA authorised status for all pools and having sufficient resource and expertise to be able to provide investment strategy advice as well as onboarding and management of legacy illiquid assets.

The transition of legacy listed markets should be achievable within the timeframe proposed.

Any future potential mergers of pools are unlikely to be completed by March 2026.

Given the complex nature of the pools and existing investment arrangements, we are concerned that rushing any implementation will lead to additional costs and additional risk to the LGPS.

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?

We are supportive of increased collaboration between pools however, we would not want this to be at the expense of an additional layer of management fees or the enforcement of any exit penalties from a pool.

Some thought would need to be given to the risk of a lack of diversification if all assets for a particular class are only invested in a small number of solutions.

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?

We believe that there is potential for collaboration between partner funds on these issues.

However, the LGPS already has a strong track record in collaboration between funds (both inside and outside of the same pool) with various examples of effective solutions across the country. Therefore, we believe that no further intervention is required in this area, especially if this distracted pools from their primary requirement of delivering strong investment outcomes for partner funds.

Question 13: What are your views on the appropriate definition of 'local investment' for reporting purposes?

From the point of view of diversification, our preference would be to define 'local investment' as UK based so all Administering Authorities have access to a broad range of investment opportunities. This is particularly important if there are opportunities for Administering Authorities to invest in multiple pools.

For reporting purposes, we have considered the desire for members to be able to understand where and how LGPS is investing. Members are likely to be focussed on their geographical region, however this may be wider than a fund's boundaries and smaller than the area covered by the pool (especially given the geographical spread of some pools). We therefore suggest that the Government considers different layers of reporting, potentially one focussed on the local area (defined such as the CA/MCA/CCA/GLA/CJC/Local Authority area) and one focussed on UK as a whole (which should be of importance to members given the strength of the UK will have a direct upon them).

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?

We are supportive of the idea in principle however we are concerned at the level of resource that this would place on the Administering Authority. Additionally, it would require a certain level of skill and knowledge to understand growth plans and priorities and identify potentially viable investment opportunities. Alternatively, all potential opportunities would flow directly through to the pool with no triage which may create an unmanageable volume for the pool.

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?

We are supportive of funds setting out a target range as this is an important strategic asset allocation decision. However further consideration is required for how this will work in practice. There is no standalone local investment asset class, and we note that this is not an asset class set out in the strategic asset allocation template (Table 2) in the consultation. Therefore, implementing, achieving and reporting on progress against a target range will require more detail.

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 believe that this will be an important skillset for the pool to have going forward for the LGPS to achieve and realise its local investment ambitions. However, given the level of expertise that would be required both at the asset class level and the underlying investment level, it may be unrealistic to expect pools to always be able to carry out the necessary due diligence and management. In these examples, due diligence and/or management may be better undertaken by external investment managers.

If other bodies are involved in the due diligence and management of local investments, guidelines should be given (or a central set agreed) as there may be unique non-financial factors that have to be considered eg political.

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?

We agree that reporting on local investments will be helpful for funds to provide clear information on this important aspect. However, comparison and aggregation across the scheme can only be achieved with consistency, therefore a clear set of principles will need to be created. Additionally, any reporting will need to be proportionate. Administering Authorities are already required to report on many aspects of the operation of the fund, resulting in annual reports of significant length. It should be recognised in the level of reporting required that local investment, whilst important, is only one aspect of the operation of a fund.

Given that pools will be managing the local investments, for Administering Authorities to meet any reporting requirements, they will require the pools to provide the relevant information. Therefore, the pools will need to be consulted in the development of any reporting requirements.

Question 18: Do you agree with the overall approach to governance, which builds on the SAB's Good Governance recommendations?

We are supportive of the Government taking steps to implement the SAB's Good Governance recommendations. Whilst some LGPS funds have already taken steps to voluntarily implement some of the changes, the Government's proposed action will help achieve greater consistency across the scheme. Proposed statutory guidance will help achieve this as well.

The Government should consider how any changes are implemented and the associated timescales – some of the proposed requirements will take time to achieve.

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?

Yes, we agree that funds should prepare and publish a governance and training strategy, including a conflicts of interest policy. It may be easier for these strategies and policy to be separate documents eg practicality, ease of reference and flexibility to update.

Question 20: Do you agree with the proposals regarding the appointment of a senior LGPS officer?

Yes, we agree with the proposed requirement to appoint a senior LGPS officer in each LGPS fund and that the fund is their main priority. We would expect that this will exclude the s.151 officer from being the senior officer, given the s.151's wide-ranging role in the authority's finances.

More clarity could be provided in:

- how the senior officer role's proposed delegated authority would interact with the Administering Authority's Pensions Committee (which typically has the delegated authority under s.101 of the Local Government Act 1972).
- the senior officer's role in the budget setting process. The current wording, "should be involved in the local authority's budget-setting process", implies that the senior officer must be involved in the budget of the wider authority, not just those of the fund.

Question 21: Do you agree that administering authorities should be required to prepare and publish an administration strategy?

Yes we agree that Administering Authorities should be required to prepare and publish an administration strategy.

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 we agree with the proposal to change how these strategies are published.

Question 23: Do you agree with the proposals regarding biennial independent governance reviews? What are your views on the format and assessment criteria?

We agree with the principle of an independent governance review as it will provide an objective assessment of how well funds are meeting the required standards of governance. For this to deliver benefit to the LGPS, the review should not become a way of ranking funds. Instead, it should help enhance governance, sharing best practice and supporting funds.

The consultation does not contain any significant level of detail around the format and assessment criteria for us to be able to pass comment. We would hope to see a further consultation on any legislation and/or guidance that sets out details of how the review will be administered.

Question 24: Do you agree with the proposal to require pension committee members to have appropriate knowledge and understanding?

Yes we agree with the proposal.

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 we agree with the proposal.

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 do not believe that this requirement will deliver the desired improvement in governance and/or scrutiny and challenge on advice and delivery.

It is unlikely that there will be a sufficient number of persons that are suitably skilled and knowledgeable in all the fields covered by the role (investment, administration and governance). Each of these fields are complex and specialised in their own right, particularly so in the LGPS which is materially different from other public service pension schemes and private sector pension schemes.

We are also unsure how such an appointment would align with the local democratic accountability of pensions committees. This could effectively introduce two tiers of members of the pensions committee which may then feed through into decision making and lead to unintended outcomes. For example, the advisor may be sidelined and their opinion ignored due or, conversely, the advisor's opinion is held in higher regard than others.

On balance, we believe that LGPS funds should be able to continue to procure advice from a range of advisors according to their needs and in line with any regulatory and professional requirements.

Question 27: Do you agree that pool company boards should include one or two shareholder representatives?

We believe that pool company boards should include shareholder representatives. This will help hold pools to account and present the views of partner funds in decision making. The exact number of representatives will likely vary between pools depending on each pool's board constitution and governance structure. It will be important that the representatives have the correct level of knowledge and experience to execute the role effectively. How best to achieve this should be considered by Government.

Question 28: What are your views on the best way to ensure that members' views and interests are taken into account by the pools?

Given the local nature of the LGPS, we believe the best way to engage with members to understand their views and interests is via the Administering Authorities. The information obtained can then be fed by the Administering Authority to the pool.

The pool could then publish an annual report on the views received and how they have been considered and, if applicable, actioned upon.

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 we agree with the proposal. Given the proposed increase in role and influence of pools in the LGPS, pools should provide regular and transparent reporting in a way that allows easy comparison between the pools. This will allow funds and other stakeholders, including Government, to better understand whether their pool has been performing on an absolute basis and relative to peers.

We believe the following reporting would be beneficial:

- **Monthly performance for each investment fund** (where possible, both returns (net of all fees and costs) and volatility, absolute and relative to the benchmark, on a monthly basis).
- **The turnover of portfolios and costs incurred**
- **Climate metrics, ESG scores and voting and engagement activity**
- **Total costs of operation** (split out into key categories, including salaries, both total and for the top executives)

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.

We do not consider there to be any particular groups with protected characteristics who would either benefit or be disadvantaged by these proposals.

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