Securing the future of pensions

TPR: Regulating public service pension schemes: the NAPF's response

February 2014

www.napf.co.uk

Contents

NAPF
Securing the future of pensions

Executive Summary

The NAPF has welcomed the expanded role for the Pensions Regulator with regards to the governance and administration of public service pension schemes. We strongly believe that proper and more uniform governance will be crucial to the on-going success of the reforms to funded public sector pension provision. It will be important to ensure that structures are in place to protect member interests and to ensure efficient and effective governance. This is particularly important in the context of the Local Government Pension Scheme where this governance and administration includes the investment of fund monies on behalf of members in order to secure their benefits.

However, we do remain concerned about the role of pension boards in the context of the LGPS which is likely to lead to inefficiencies, especially where a fund is already governed by a pensions committee. We do think that there is a case to be made for local authority funds to share a pension board as this could increase uniformity of management and potentially would increase resources and expertise available to pension boards so that they could do a better job for all.

We recognise that such decisions are not in the gift of TPR but some of the tensions in the new structure do become apparent when the majority of standards in the new code on apply to the pensions board, not the scheme manager. In this context we welcome the fact that TPR has stretched its remit in this regard and made specific references to the scheme manager throughout the code.

It is clear that the LGPS in particular operates in a very different way from the other public service pension schemes. The governance sub-committee of the Shadow LGPS Advisory Board in England and Wales has been working with TPR on this code and is considering what additional guidance may be required to help funds apply the code to the LGPS. We believe that such guidance will be required, especially once the LGPS governance arrangements are finalised and will be very useful for funds assessing how to apply the code.

The new code and draft regulatory strategy strike an appropriate regulatory approach which is consistent with the way TPR regulates private sector schemes, although given its lack of remit around funding it will be interesting to see when it feels that there is sufficient material risk in the governance and administration of schemes as to warrant its stronger interventions.

Overall the code and regulatory strategy are fairly straightforward and there is some useful examples and guidance for scheme managers and pension boards. We also welcome the fact that TPR will be adapting its trustee e-learning toolkit to incorporate public service schemes.

However the requirement to monitor the under and overpayment of contributions could be extremely onerous and impracticable in a CARE scheme with a large number of participating employers. We would urge TPR to be very clear about under what circumstances the fund should be reporting such breaches to ensure that these are proportionate and take full account of the duty in the LGPS on employers to ensure correct contributions are made.

About the NAPF

The National Association of Pension Funds is the leading voice of workplace pension provision in the UK. We represent 1,300 pension schemes from all parts of the economy and 400 businesses providing essential services to the pensions industry. We represent both public and private sector schemes, including over 70% of the local authority pension funds. Our members provide pensions for 16m people and collectively hold assets of around £900bn, making them major institutional investors. Our main objective is to ensure there is a secure and sustainable pensions system in the UK.

Introduction

1. The NAPF has welcomed the expanded role for the Pensions Regulator (TPR) with regards to the governance and administration of public service pension schemes. We strongly believe that proper and more uniform governance will be crucial to the on-going success of the reforms to funded public sector pension provision. It will be important to ensure that structures are in place to protect member interests and to ensure efficient and effective governance. This is particularly important in the context of the Local Government Pension Scheme (LGPS) where this governance and administration includes the investment of fund monies on behalf of members in order to secure their benefits.

2. However, we do remain concerned about the role of pension boards in the context of the LGPS. Whilst some form of compliance function is welcome, to apply this structure to each of the 89 administering authorities, however, may result in inefficiencies, especially where a fund is already governed by a pensions committee. We do think that there is a case to be made for local authority funds to share a pension board, although it would seem that DCLG believes that this is not the intent of the current statutory language. We do not agree that a prohibition on shared pension boards automatically follows from the language of the statute, and moreover there would seem to be some strong arguments for shared pension boards. There may be economic considerations that stop local authority schemes from consolidating altogether, but assisting with compliance by a shared pension board could increase uniformity of management and potentially would increase resources and expertise available to pension boards so that they could do a better job for all.

3. We recognise that such decisions are not in the gift of TPR but some of the tensions in the new structure do become apparent when the majority of standards in the new code only apply to the pensions board, not the scheme manager. In the area of knowledge and understanding in particular it feels inappropriate that the compliance body is required to have a greater knowledge and understanding than the person/body running the scheme and this is something we will continue to pursue with the Department for Communities and Local Government. In this context we welcome the fact that TPR has stretched its remit in this regard and made specific references to the scheme manager throughout the code.

4. It is clear that the LGPS in particular operates in a very different way from the other public service pension schemes. The governance sub-committee of the Shadow LGPS Advisory Board in England and Wales has been working with TPR on this code and is considering what additional guidance may be required or whether there is a case for separate guidance to help funds apply the code to the LGPS. We believe that such guidance will be required, especially once the LGPS governance arrangements are finalised and will be very useful for funds assessing how to apply the code.

5. The new code is accompanied by a draft regulatory strategy, which sets out how TPR plans to regulate public service pension schemes. TPR's general approach is to understand the key areas of risk, with particular focus on knowledge and understanding, records, member communications and management of internal disputes. They focus on education and enablement, through

guidance and support, but they will enforce regulations where standards have not improved. This is an appropriate regulatory approach which is consistent with the way TPR regulates private sector schemes, although given its lack of remit around funding it will be interesting to see when it feels that there is sufficient material risk in the governance and administration of schemes as to warrant its stronger interventions.

6. Some of TPR's existing codes of practice currently apply to the LGPS (such as code 11 on dispute resolution) so it is helpful that this code is all encompassing and brings together all existing requirements for public service schemes into one code.

7. Overall the code and regulatory strategy are fairly straightforward and there are useful examples and guidance for scheme managers and pension boards. We also welcome the fact that TPR will be adapting its trustee e-learning toolkit to incorporate public service schemes.

8. However the requirement to monitor the under and overpayment of contributions could be extremely onerous and impracticable in a CARE scheme with a large number of participating employers. We would urge TPR to be very clear about under what circumstances the fund should be reporting such breaches to ensure that these are proportionate and take full account of the duty in the LGPS on employers to ensure correct contributions are made.

Consultation questions

Q1. Does the code sufficiently address the standards of conduct and practice necessary to evidence compliance with pensions legislation? If not, why not? What improvements would you recommend?

9. Overall the code and regulatory strategy are fairly straightforward and there is some useful examples and guidance for scheme managers and pension boards. We also welcome the fact that TPR will be adapting its trustee e-learning toolkit to incorporate public service schemes.

Q2. Does the level of guidance included in the code provide sufficient detail to enable scheme managers and members of pension boards to comply with pensions legislation and undertake their role effectively?

10. Yes, although further detail will be required for scheme specific circumstances.

Q3. The code relates only to the specific matters on which we are required to issue a code under section 90A(2) of the Pensions Act 2004. Are there any other legal requirements which you think should be brought within the scope of the code? Are there parts of the code which you think go beyond legal requirements, practical guidance or good practice?

11. No.

Section 1: Introduction

Q4. Have we targeted the code at the right groups of people? If not, which have been overlooked?

12. Our members have expressed disappointment that the code focuses on the requirements for the pensions board, rather than the scheme manager. Whilst we recognise this is due to the fact that the legislation does not reflect the structure of the LGPS, they felt it was important to point out this inconsistency. The Shadow Advisory Boards will need to provide LGPS specific guidance.

Q5. Is there any further information or explanation you would like to see in the terms used section of the introduction?

13. Once scheme specific guidance has been developed it would be useful if the code could refer to such guidance in this introduction so that schemes can easily see where to go for scheme-specific guidance.

Q6. Does the code strike the right balance between being as concise as possible and providing enough practical guidance relating to the underlying legal obligations?

14. The balance appears to be a fair one. In terms of language in the code there appeared to be parts of the code that refer to "conversant with" and others that refer to "having knowledge and understanding" and there is a need to establish whether these have different meanings.

Section 2: Governing your scheme

Q7. Do we adequately describe the level of knowledge and understanding required of members of pension boards? If not, why not?

15. The Act requires pension board members to be conversant and knowledgeable in relation to pensions – at a general, scheme and local level in order to carry out their functions. The code highlights that these requirements only apply to pensions boards and, whilst outside TPR's remit, the code suggests that scheme managers should also take account of this. The code provides useful practical examples of how this can be achieved.

16. The code clarifies the level of knowledge - that pension board members should be able to challenge any failure to comply with the scheme rules and legislation relating to the governance and administration of the scheme as well as any failure to meet the standards and expectations set out in this code. This provides a useful tool in persuading pension committees and boards to undertake further training.

17. The code highlights the needs to get board members up to speed as quickly as possible upon their appointment (ideally before). It is welcome that TPR will be adapting their trustee e-learning toolkit to incorporate the public service schemes but they should also take account of existing best practice, eg CIPFA Knowledge and Understanding.

Q8. Does the practical guidance adequately address the risks of the different types of conflicts of interest which may occur? Could you provide better examples of key conflicts which should be provided in the code?

18. The Act requires the scheme manager to ensure pension board members do not have a conflict of interest. Once again, the code highlights the need for scheme managers to be mindful of this guidance. This section focus on identifying, monitoring and managing potential conflicts and the need for documented policy and procedures and provides some very useful practical guidance, in particular on the types of conflict that may arise in a pension scheme that are different from the usual public authority conflicts. One additional conflict of interest example that would be useful is where a board/committee member has budget setting responsibilities with regards to the employer and the committee is setting the funding strategy.

Q9. Does the practical guidance in the code sufficiently capture all of the duties, including any fiduciary duties, owed by pension board members? Do you consider that such duties may arise in the context of public service schemes? Please explain your response.

19. This is a complex, and much-debated area in the context of the LGPS. The Shadow Scheme Advisory Board in England and Wales is currently seeking Counsel's advice on this issue and the Code may require some further amendments following the outcome of this advice.

Section 3: Managing risks

Q10. Have we set out clearly what actions are expected of scheme managers and members of pension boards in relation to risk management and internal controls?

20. The Act extends to public service pension schemes the Pensions 2004 requirement to establish internal controls which are adequate to ensure scheme rules and legislation are adhered to. The code explains that internal controls include areas such as procedures, which create a clear separation of duties, processes for escalation and assessing and managing risk. These include a number of useful examples.

21. An important mention in the code is the need to objectively assess the strength of the employer covenant something that is challenging for scheme managers but needs to considered and reviewed on an regular basis.

Section 4: Administering your scheme

Q11. Does the public service code include sufficient practical guidance on the standards of administration that we expect? Are there any parts of the code that you think are too prescriptive?

Q12. We provide examples of what failures to pay contributions are likely to be materially significant to the regulator. Are there any other examples or scenarios that should be included?

22. In terms of member information, here the code helpfully focuses on the requirement on the scheme employer to ensure the accurate and complete transmission of data and the requirement on the scheme to report a breach.

23. The code also talks to the legal requirement for contribution payments to be made within a specific timeframe and the scheme to report any breach of payment to TPR within specific requirements. Whilst this requirement looks fairly straightforward on the face of it, the requirement to monitor the under and overpayment of contributions could be extremely onerous and impracticable in a CARE scheme with a large number of participating employers. The regulator needs to ensure that the definition of materially significant is proportionate to the number of employers (in the region of 8000) and employer contributions being made into the LGPS each year and the fact that in the LGPS there is a specific requirement on employers to ensure that contributions paid are correct.

24. Information to members. This covers disclosure requirements and is pretty straightforward. However, where the code refers to the need to 'consider' pursuing lost members. Our members felt that 'try' to pursue lost members would be more appropriate.

Section 5: Resolving issues

Q13. Have we made clear the circumstances under which breaches of pensions legislation should be reported to us?

25. The LGPS already has a system in place for resolving disputes and this two-stage process actually goes beyond the minimum legal requirements. Reporting breaches of the law. This applies to a whole host of people and it is useful that the code highlights the need for this duty to report to be part of training for scheme managers and pension board members.

Draft public service regulatory strategy

Q14. Does the strategy, together with the public service code, sufficiently address risks to good governance and administration?

Q15. Does the strategy explain adequately the approach we will take in regulating public service schemes?

26. The new code is accompanied by a draft regulatory strategy, which sets out how TPR plans to regulate public service pension schemes. TPR's general approach is to understand the key areas

of risk, with particular focus on knowledge and understanding, records, member communications and management of internal disputes. They focus on education and enablement, through guidance and support, but they will enforce regulations where standards have not improved. This is an appropriate regulatory approach which is consistent with the way TPR regulates private sector schemes, although given its lack of remit around funding it will be interesting to see when it feels that there is sufficient material risk in the governance and administration of schemes as to warrant its stronger interventions.

Impact assessment

Q16. The impact assessment undertaken by the Treasury concluded that the new governance, administration and regulatory oversight provisions should not result in additional costs for schemes. The code gives practical guidance and sets standards of conduct and practice in relation to those new provisions. Do you agree that the public service code and public service regulatory strategy do not place an additional regulatory burden on schemes? If you do not agree, please explain and quantify additional costs.

27. We do not agree. In the LGPS the requirement to staff and support two boards will be a key resource issue with many funds as there may not be a sufficient supply of informed personnel to take on each function and each body will require its own support - with limited scope of shared services due to the inherent conflicts that arise.

Conclusion

28. The NAPF has welcomed the expanded role for the Pensions Regulator with regards to the governance and administration of public service pension schemes. However, we do remain concerned about the role of pension boards in the context of the LGPS, which is likely to lead to inefficiencies, especially where a fund is already governed by a pensions committee. We recognise that such decisions are not in the gift of TPR but some of the tensions in the new structure do become apparent when the majority of standards in the new code on apply to the pensions board, not the scheme manager.

29. The new code and draft regulatory strategy strike an appropriate regulatory approach which is consistent with the way TPR regulates private sector schemes, although given its lack of remit around funding it will be interesting to see when it feels that there is sufficient material risk in the governance and administration of schemes as to warrant its stronger interventions. Overall the code and regulatory strategy are fairly straightforward and there are some useful examples and guidance for scheme managers and pension boards. We also welcome the fact that TPR will be adapting its trustee e-learning toolkit to incorporate public service schemes.

30. However the requirement to monitor the under and overpayment of contributions could be extremely onerous and impracticable in a CARE scheme with a large number of participating employers. We would urge TPR to be very clear about under what circumstances the fund should be reporting such breaches to ensure that these are proportionate and take full account of the duty in the LGPS on employers to ensure correct contributions are made.

Further information

For further information please contact:

Helen Forrest, Head of Policy and Advocacy

helen.forrest@napf.co.uk

020 7601 1700