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**Louise Adamson**  
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Date: 1 October 2018

Dear Sir/Madam

You are invited to the following meeting:

**Special Pension Fund Committee / Pension Board**  
**Council Chamber, Town Hall, Lerwick**  
**Monday 8 October 2018 at 2pm**

**Please note that in accordance with the agreed terms of reference, this is a concurrent meeting of both the Pension Fund Committee and the Pension Board - SEE MEMBERSHIP OF BOTH BODIES OVERLEAF**

Apologies for absence should be notified to Louise Adamson at the above number.

Yours faithfully

Executive Manager – Governance and Law

Chair: Steven Coutts

## **AGENDA**

- (a) Hold circular calling meeting as read.
- (b) Apologies for absence, if any.

- (c) Declarations of Interest – Members are asked to consider whether they have an interest to declare in relation to any item on the agenda for this meeting. Any Member making a declaration of interest should indicate whether it is a financial or non-financial interest and include some information on the nature of the interest. Advice may be sought from Officers prior to the meeting taking place.

## Item

1. Scottish LGPS Restructure Review  
*F-074*

Pension Fund Committee	Pension Board	
A Cooper S Coutts S Leask E Macdonald R McGregor I Scott C Smith G Smith T Smith R Thomson	<u><b>Employers Representatives:</b></u> M Bell, SIC J Fraser, SIC A Westlake, SIC J Johnston, SRT  <u><b>Joint Secretary</b></u> J Riise, Executive Manager – Governance and Law	<u><b>Trade Union Representatives:</b></u> David Marsh, Unison Alan Goudie, Unite Robert Williamson, GMB Austin Taylor, Unison  <u><b>Substitutes:</b></u> C Wiseman, Unison  <u><b>Joint Secretary</b></u> C Wiseman, Unison



<b>Meeting(s):</b>	<b>Special Pension Fund Committee Special Pension Board</b>	<b>8 October 2018 8 October 2018</b>
<b>Report Title:</b>	<b>Scottish LGPS Restructure Review</b>	
<b>Reference Number:</b>	<b>F-074-F</b>	
<b>Author / Job Title:</b>	<b>Executive Manager - Finance</b>	

## 1.0 Decisions / Action required:

- 1.1 That the Pension Fund Committee and the Pension Board note the key issues detailed in this report, and provide comments to inform further consultation and formulation of a final response; and
- 1.2 That the Pension Fund Committee delegate authority to the Executive Manager – Finance, or his nominee, in consultation with the Chair of the Pension Fund Committee, to conduct further consultation with members of the Committee, Board and Admitted Bodies, in order to inform a final response for submission to the Pensions Institute by 7 December 2018.

## 2.0 High Level Summary:

- 2.1 The Local Government Pension Scheme Advisory Board (SAB), at the request of the Scottish Government Cabinet Secretary for Finance and Constitution is carrying out a consultation on the future of the Scottish Local Government Pension Scheme (SLGPS).
- 2.2 The consultation seeks to establish the views of employers and employee representative groups on whether outcomes for the members and sponsors of the SLGPS can be improved by altering the structure of the scheme.
- 2.3 The consultation asks employers and employee representative groups to consider the advantages and disadvantages of four options ranging from the current structure to consolidating the functions of the Scottish 11 schemes by collaboration or pooling or full merger.
- 2.4 The consultation is predominately focussing on the investment area of the Pension Fund and not at present the administration side. The consultation also has questions on SLGPS investing in infrastructure projects.
- 2.5 Employer and employee representative organisations are asked to respond to the set specific questions in the form accompanying the consultation report and email responses to the Pensions Institute by Friday 7<sup>th</sup> December 2018.

## 3.0 Corporate Priorities and Joint Working:

3.1 The report links to the Council's corporate priorities, defined in its Corporate Plan, specifically in relation to assisting the Pension Fund in ensuring that financial resources are managed effectively.

#### **4.0 Key Issues:**

4.1 A review of the SLGPS was agreed with stakeholders and the Scottish Government Ministers when the changes to the scheme and the new Scheme Advisory Board were introduced in 2015.

4.2 The SAB proposed carrying out this review beginning in 2016. The SAB commissioned research pieces by Mercer (investment consultants) in 2016 and Iain Clacher at Leeds University in 2017, as well as setting up a working party comprising employers, trade unions and fund advisors. From this research the SAB released its own report in 2017.

4.3 The research concluded that Scottish pension schemes face a number of significant challenges and, as a result, the current structure of the scheme in Scotland which has 11 Local Authority Pension Funds should be reviewed. A selection of these significant challenges include: the deficit; investment management costs and their transparency; investment performance; volatile investment markets; low interest rates; a maturing scheme membership and the consequences of implementing investment preferences in respect of certain assets, such as fossil fuels and infrastructure.

4.4 Based on this research the SAB report identified four options for the future of the local government pension scheme in Scotland.

4.5 The four options proposed are:

- Retain the current structure with 11 Local Authority Pension Funds
- Promote cooperation in investing and administration between the 11 funds
- Pool investments between the 11 funds
- Merge the 11 funds into one or more funds

4.6 The four proposed options were presented to Scottish Government Ministers in May 2017. In January 2018, SAB received a letter from Derek Mackay MSP, Cabinet Secretary for Finance and the Constitution seeking a consultation with SLGPS employers and employee membership bodies on the four options. Attached as Appendix A is Derek Mackay's foreword to the consultation document.

4.7 The SAB has commissioned the Pensions Institute to manage the consultation process on the structural review of the SLGPS. The consultation invites employers and employee representative groups to give their views on each of the four options. The consultation was launched during June 2018 and the report and response form are available from: <http://lgpsab.scot/consultation2018/>

4.8 The SAB's 2017 report sets out the four main options for the local government pension scheme and the consultation focuses on four criteria in relation to each option:

- Cost of investing: This is the biggest outlay by each fund in the SLGPS and research suggest even small reductions in investing costs and, in particular,

investment manager fees could have a significant impact on fund performance.

- Governance: Numerous studies show that improving governance produces significantly better outcomes over the long-term and that most pension funds in both the private and public sectors have room to improve in this area.
- Operating risks: Believed to vary significantly among public and private sector pension funds depending on the effectiveness of the governance processes of each fund and the quality of the executive resources available to individual funds.
- Infrastructure investment: There is an increasing political desire that SLGPS funds be able to invest pension assets in infrastructure should they decide it to be in the interest of members and employers.

4.9 The consultation is open to SLGPS employers and employee representative groups only. To have their views heard, they should respond to the questions no later than Friday 7<sup>th</sup> December. The consultation response form questions are attached as Appendix B.

4.10 Responses gathered from the consultation will be evaluated by the SAB and presented to Scottish Government Ministers in 2019 to inform any future course of action. As well as this consultation, Ministers will also take into consideration a governance review of public sector pensions being undertaken by the Scottish Public Service Pensions Agency.

4.11 The four options proposed in the SAB report which employee and employer groups are asked to consider could have very different impacts upon the Shetland Islands Council Pension Fund:

- Retaining the current 11 Local Authority Pension Funds. This is the status quo option, and there would be no change to the present governance, operation and investment of the Pension Fund.
- Promoting cooperation in investing and administration between the 11 funds. The administration officers and the investment officers of the 11 funds already meet quarterly and share information. This would increase the current cooperation, in certain specific areas where beneficial between the Scottish funds. This would involve having a closer working relationship with the other 11 Pension Funds.
- Pooling of investments between the 11 funds. This is following on from England and Wales where 89 funds combined into eight large pooled funds. This option for Scotland would see the 11 funds made into one Scottish Pool, involving the setting up of a new committee and officer operation to look after the Scottish investment pool. Shetland's Pension Fund would still operate similar to before but would only be able to invest in the selection of fund managers that the pool recommended. Costs and benefits would be unclear with this arrangement until the pool structure was operating, but it would add another layer of governance between the fund and the fund manager, with a reduced fund manager investable list.

<ul style="list-style-type: none"> <li>• Merging the 11 Scottish Funds into one or more funds. This would remove all local control and involvement in the Pension Fund from the Council. The new Scottish Fund would have responsibility for all of Scotland's pension investments. There would be no requirement for a Pension Fund Committee or Pension Board, no involvement in the investments and there may be staff issues if administration was included. The Shetland Pension Fund would no longer have any local control.</li> </ul>	
<p>4.12 The Shetland Islands Council Pension Fund will be responding to this consultation and employers within the fund are encouraged to respond. In this regard it is intended that further consultation will be conducted by officers with members of the Committee, Board and Admitted Bodies, in order to inform a final response for submission by the closing date of 7 December.</p>	
<p><b>5.0 Exempt and/or confidential information:</b></p>	
<p>5.1 None</p>	
<p><b>6.0 Implications :</b></p>	
<p><b>6.1 Service Users, Patients and Communities:</b></p>	<p>The report provides the stakeholders with information on the current SAB consultation on the future of the Pension Scheme. The outcome of the consultation could have wide ranging implications on the operation of the Pension Fund.</p>
<p><b>6.2 Human Resources and Organisational Development:</b></p>	<p>Currently the SAB consultation is gathering comments from employee and employer groups. Depending on which future option is preferred from the results of the consultation there could be changes to the local operation of the Pension Scheme.</p>
<p><b>6.3 Equality, Diversity and Human Rights:</b></p>	<p>None</p>
<p><b>6.4 Legal:</b></p>	<p>There are no direct legal implications arising from this report however, legal advice and legal remedies will be sought and used whenever this is appropriate.</p>
<p><b>6.5 Finance:</b></p>	<p>There are no direct financial implications arising from this report.</p>
<p><b>6.6 Assets and Property:</b></p>	<p>Long term investments are assets of the Pension Fund and represent money given to fund managers to manage on its behalf for long term benefit. The SAB consultation is looking specifically at the future management structure of these assets, with four options for consideration, from maintaining the current structure to more cooperation, pooling and complete merger of the 11 Scottish Pension Schemes.</p>
<p><b>6.7 ICT and new technologies:</b></p>	<p>None</p>

<b>6.8 Environmental:</b>	<p>Whilst the fund managers have delegated powers for the acquisition and realisation of investments, fund managers are expected as part of their investment process to consider all factors, including the social, environmental and ethical policies of companies in which they may invest, to the extent that these may materially affect the long term prospects of such companies. The fund managers will also be expected to enter into dialogue with companies in which they invest, in relation to the pursuance of socially responsible business practices, and report on these activities.</p> <p>Corporate Governance is a key responsibility for institutional shareholders and as a matter of principle the Pension Fund will seek to exercise all of its voting rights in respect of its shareholdings. It is recognised however that in practical terms this may not always be possible for overseas holdings. However, for UK stocks all voting rights will be exercised in a positive fashion, i.e. no abstentions. All of the Pension Fund managers are signed up to the United Nations Principles on Responsible Investment.</p> <p>The principles reflect the view that environmental, social and corporate governance (ESG) issues can affect the performance of investment portfolios, and therefore must be given appropriate consideration by investors, if they are to fulfil their fiduciary (or equivalent) duty. The principles provide a voluntary framework by which all investors can incorporate ESG issues into their decision-making and ownership practices, and so better align their objectives with those of society at large.</p>	
<b>6.9 Risk Management:</b>	<p>There are no risk implications from the report but the SAB consultation is looking at the future investment structure of the SLGPS, and depending on the results from the consultation there may be changes to the risk profile of the Pension Fund.</p> <p>All investments carry risk. Risks, such as market risk are mitigated and actively managed through diversification of fund managers, asset classes, markets, size of holdings and through performance monitoring against benchmarks.</p>	
<b>6.10 Policy and Delegated Authority:</b>	<p>The Pension Fund Committee has delegated authority to discharge all functions and responsibilities relating to the Council's role as administering authority for the Shetland Islands Council Pension Fund (the Pension Fund) in terms of the Local Government (Scotland) Act 1994, the Superannuation Act 1972 and the Public Service Pensions Act 2013.</p> <p>The Pension Board is the body responsible for assisting the Scheme Manager in relation to compliance with scheme regulations and the requirements of the Pensions Regulator. The Pension Board will determine the areas they wish to consider.</p>	
<b>6.11</b>	None	

<b>Previously considered by:</b>		
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**Contact Details:**

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**Appendices:**

Appendix A: Cabinet Secretary's foreword to the SAB consultation document  
Appendix B: SAB consultation response form

**Background Documents:**

None



## **Cabinet Secretary's foreword**

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I am delighted to support the launch of the Scottish Local Government Pension Scheme Advisory Board's consultation on a structural review of the Local Government Pension Scheme (LGPS) pension funds in Scotland.

LGPS fund authorities invest in a wide variety of projects including local housing and infrastructure, however investment in Scotland's infrastructure is only a small part of the investment strategy of the Scottish fund authorities. The Scottish Government is ambitious for greater investment by local government funds in Scotland's infrastructure.

There are currently excellent examples of fund authorities collaborating on infrastructure projects in Scotland. We look to LGPS fund authorities to improve their already positive impact on the economy thereby contributing further to sustainable economic growth, creating more jobs and supporting the delivery of key capital infrastructure needs in Scotland, such as transport projects and housing.

A key part of the Scheme Advisory Board's role is to provide advice about the effective and efficient administration and management of the Scheme. So I asked the board to investigate the collaboration between fund authorities to invest in Scottish infrastructure, whilst maintaining overall investment performance to ensure that the interests of LGPS members' are protected.

The Scheme Advisory Board commissioned reports from pension consultants Mercers and Iain Clacher of the University of Leeds on possible future structures for the funds. The reports highlight that the new governance arrangements require a greater focus on cost transparency and performance. The academic evidence on costs and fees also seems to support the premise that there are cost savings available with economies of scale for both the administration and investment of pension funds.

I welcome the Scheme Advisory Board's consultation, which provides four clear options for the future structure of pension funds in Scotland. I encourage you to participate fully in this important debate which could have a wide-ranging impact on the people of Scotland.

Derek Mackay MSP

**Cabinet Secretary for Finance and the Constitution**



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

## CONSULTATION RESPONSE FORM

### 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-institute.org](mailto:consultation@pensions-institute.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](mailto:matthew.roy@pensions-institute.org).

### RESPONDENT DETAILS

#### 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.

full names of responding organisations	type of organisation

#### 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.

names, job titles and organisation of authors	consents

#### Date

Please date the response.

date

**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.

covering text

The consultation questions follow.

## CONSULTATION QUESTIONS

### Question 1: Retain the current structure with 11 funds

The text can wrap onto additional pages.

#### a) 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?*
- *How well does the current system manage investment costs?*
- *How would you improve the measurement and management of investment costs in the current system?*

#### b) Governance:

- *How well informed do you feel about the governance of your fund? What information do you rely on to measure this?*
- *How well is the current system governed?*
- *How would you improve governance of the current system?*
- *How important is it to maintain a local connection with respect to oversight and strategy?*

**How would you determine if the benefits of a local connection in governance outweigh the benefits of scale?**

#### c) 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?*
- *How well are operating risks managed in the current system?*
- *How would you improve the measurement and management of operating risks in the current system?*

#### d) Infrastructure:

- *How well informed do you feel about your fund's investments in infrastructure? What information do you rely on?*
- *How do you rate the current system's ability to invest in infrastructure?*
- *How would you increase investment in infrastructure in the current system?*

#### e) Do you have any additional comments about this option?

## **Question 2: Promote cooperation in investing and administration between the 11 funds**

The text can wrap onto additional pages.

### **a) Cost of investing:**

- *What impact do you think promoting agreements between funds would have on investment costs?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

### **b) Governance:**

- *What impact do you think promoting agreements between funds would have on governance?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

### **c) Operating risks:**

- *What impact do you think promoting agreements between funds would have on operating risks?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

### **d) 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?*
- *What would be the negative impacts?*

### **e) Do you have any additional comments about this option?**

### **Question 3: Pool investments between the 11 funds**

The text can wrap onto additional pages.

#### **a) Cost of investing:**

- *What impact do you think pooling investments between funds would have on the cost of investing?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*
- *If asset pooling were possible, under what circumstances should a fund consider joining an asset pool?*
- *Under which circumstances should the SLGPS consider directing funds to pool?*

#### **b) Governance:**

- *What impact do you think pooling investments between funds would have on governance?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

#### **c) 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?*

#### **d) 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?*

**Do you have any additional comments about this option?**

#### **Question 4: Merge the funds into one or more new funds**

The text can wrap onto additional pages.

##### **a) Cost of investing:**

- *What impact do you think mergers between funds would have on the cost of investing?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*
- *If merging were possible, under what circumstances should a fund consider a merger?*
- *Under what circumstances should the SLGPS consider directing funds to merge?*

##### **b) Governance:**

- *What impact do you think mergers between funds would have on governance?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

##### **c) 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?*

##### **d) Infrastructure:**

- *What impact do you think mergers between funds would have on funds' ability to invest in infrastructure?*
- *What would be the positive impacts?*
- *What would be the negative impacts?*

##### **e) Do you have any additional comments about this option?**



## **Question 5: Preferred and additional options**

The text can wrap onto additional pages.

- a) Which option does your organisation prefer? Please explain your preference.**
  
- b) What other options should be considered for the future structure of the LGPS?**
  
- c) What would be the advantages and disadvantages of these other option for funds' investment costs, governance, operating risks and ability to invest in infrastructure?**
  
- d) Are there any other comments you would like to make?**

The consultation questions end.