PUBLIC

MINUTES of a meeting of the **PENSIONS AND INVESTMENT COMMITTEE** held on 21 July 2021 at County Hall, Matlock.

PRESENT

Councillor D Wilson (in the Chair)

Derbyshire County Council

Councillors R Ashton, B Bingham, D Murphy (substitute member), G Musson, and P Smith

Derby City Council

Councillor M Carr

Also in attendance – M Fairman, D Kinley, and S Webster and R Graham (representing the Pension Board)

Apologies for absence were received on behalf of Councillors N Atkin and M Foster (Derbyshire County Council) and L Care (Derby City Council) and M Wilson (Trade Union representative)

34/21 **MINUTES** **RESOLVED** that the minutes of the meeting held on 9 June 2021 be confirmed as a correct record and signed by the Chairman.

35/21 **DERBYSHIRE PENSION FUND – UPDATES ON THE FUNDING STRATEGY STATEMENT (FSS)** The FSS is usually reviewed every three years as part of the Fund's actuarial valuation and is also subject to review following a material change in the administering authority's policy on the matters covered by the document (this would normally follow amendments to relevant scheme regulations or statutory guidance). The most recent version of the FSS was published in March 2020 after being approved by the Committee at its meeting on 4 March 2020 following consultation with the Fund's stakeholders.

Following a consultation undertaken by the Ministry of Housing, Communities and Local Government (MHCLG), the Local Government Pension Scheme (Amendment) (No.2) Regulations 2020 (2020 Regulations) came into force from 23 September 2020. These regulations allowed for greater flexibilities for reviewing employer contribution rates and for collecting exit payments from employers ceasing their active participation in the Fund (these employers are known as exiting employers). An exiting employer is liable to pay an exit payment if their LGPS liabilities exceed their LGPS assets or alternatively may be entitled to receive an exit credit if their LGPS assets exceed their LGPS liabilities.

The 2020 Regulations give administering authorities the power to:

- Review employer contributions between the triennial actuarial valuations in certain situations
- Allow an exiting employer to spread an exit deficit payment rather than pay it fully at the point of exit
- Allow an employer to continue to pay contributions to the Fund as a 'deferred employer' under a formal 'Deferred Debt Agreement' and for those contributions to be reviewed at future valuations

The new powers (known as employer flexibilities) have been introduced to increase the range of options available to administering authorities to manage covenant risk in the LGPS which arises where a Scheme employer may be unable to meet its future obligations. They are intended to help administering authorities ensure that employer contribution rates are set at an appropriate level and that exit payments are managed, with steps taken to mitigate risk, where appropriate. There is no requirement on administering authorities to use the new powers and the 2020 Regulations require that an authority may only do so where it has set out its policy with respect to the new flexibilities in its FSS, in order to ensure consistency and transparency.

MHCLG had published statutory guidance to assist administering authorities in implementing and operating the new regulations on employer flexibilities. The guidance, attached at Appendix 2 to the report, set out that in developing new policies for inclusion in their FSS and in using the new powers, administering authorities should aim to ensure:

- Consistent use of any new policies in relation to all employers within the fund
- A clear and transparent process of applying the new policies

The LGPS Scheme Advisory Board (SAB) had subsequently produced detailed operational guidance to be considered in conjunction with the MHCLG statutory guidance, attached at Appendix 3 to the report.

The updates to the FSS, which largely reflect the Fund's policy on the new employer flexibilities, were drafted in consultation with the Fund's actuary and in consideration of the guidance from MHCLG and the SAB. The proposed changes to the FSS were highlighted in the draft updated FSS attached at Appendix 4 to the report, with the matters that the Fund will consider under each flexibility clearly set out. In drafting the proposed changes related to employer flexibilities, the interests of the employer concerned and the interests of all the other employers in the Fund had been considered.

LGPS 2013 already provided that a Fund could undertake a review of an employer's contributions where it may become an exiting employer. The new regulations allow a review of employer contributions to take place between actuarial valuations in the following additional circumstances:

- It appears that the amount of liabilities arising, or likely to arise, for an employer or employers have changed significantly since the last valuation
- It appears likely that there has been a significant change in the ability of an employer or employers to meet their obligations
- Where an employer or employers have requested a review and have undertaken to meet the costs of that review

The SAB guidance made it clear that whilst a review of contribution rates as part of the actuarial valuation takes into account changes in economic and demographic conditions, as well as changes in membership and individual employer circumstances, a review under the new regulations would only be triggered as a result of either a significant change in membership data or an employer's circumstances. The draft updated FSS includes details of the circumstances that the Fund would consider as a potential trigger for a review and clarifies that an employer's reason for requesting a review would be expected to fall into one of the same trigger categories. The requirement for the employer to meet the cost of a requested review was is clearly documented.

At the point of an employer exiting the Fund, a formal assessment of the employer's funding position (its assets compared to its liabilities) at the date of exit is undertaken by the Fund's actuary.

Where an employer can demonstrate that the payment of the debt in a single immediate payment would have a material detrimental impact on its normal operations, the Fund will in future be able to consider entering into a debt spreading arrangement with the employer subject to actuarial, legal and covenant considerations.

Deferred Debt Agreements (DDA) will allow employers to continue paying contributions to the Fund as a deferred employer when they no longer had any active members, essentially allowing an employer to defer the payment of an exit debt in return for an on-going commitment to meet their responsibilities as an employer in the LGPS. A DDA is different to a debt spreading arrangement in that the employer does not formally exit the Fund and it allows for the flexibility of active membership returning.

It also allows for employers whose preference is to remain in the Fund and continue to share the risks of continuing participation (e.g. potentially benefiting from investment returns) rather than crystalising any debt at the point of active membership ceasing. Under a DDA, an employer continues in the Fund with the same obligations as an active employer, with the exception of paying contributions on employees' active LGPS membership (i.e. primary contributions, which fund ongoing future service accrued by employees). The Fund's actuary would determine a level of secondary contributions (which fund liabilities accrued from historic LGPS membership) and review the level of secondary contributions at each triennial valuation which falls within the period of the DDA.

In addition to proposed changes to reflect the Fund's policy on the new employer flexibilities, a small number of other minor revisions have been included in the draft updated FSS. The FSS now includes a reference to the Fund's Exit Credits Policy, which sets out the policy for determining the payment of an exit credit if pension liabilities had been overfunded at the date of an employer exit. The Exit Credits Policy is included as part of the Fund's Admission, Cessation and Bulk Transfer Policy. The Local Government Pension Scheme (Amendment) Regulations 2020 allow LGPS funds to take into account pension risk sharing arrangements and the extent of an exiting employer's contributions to the fund when making an exit credit determination. This required a minor change to the Fund's Exit Credits Policy and subsequently to the policy being referenced in the FSS. The change has been highlighted in the draft updated FSS and in the Fund's Admission, Cessation and Bulk Transfer Policy attached at Appendix 5 to the report.

A revision to the summary of the Fund's approach to the McCloud judgement during the 2019 valuation has been included in the draft updated FSS. A brief summary of the possible impact of the Goodwin tribunal on Fund liabilities, which may have cost implications for all public service pension schemes, has also been included in the updated FSS.

The Fund may, at its sole discretion, allow an employer to make advance payments of its employer contributions in return for a discount determined by the Fund's actuary. The draft updated FSS confirms that where prepayments calculated on forecast payrolls have been approved by the Fund and result in an 'excess' payment when actual payrolls were taken into account, no refund would be payable to the employer, instead the surplus would remain allocated to the employer's assets within the Fund.

A consultation would be undertaken on the draft updated FSS with all of the participating employers in the Fund. It was anticipated that the consultation would run for a period of four weeks from 26 July 2021 to 22 August 2021. The result of the consultation will be reported to Committee in September when the final FSS will be presented for approval.

RESOLVED to (1) note the proposed changes to the FSS following the introduction of new powers for administering authorities to review employer contributions between actuarial valuations and to adopt more flexible methods of collecting exit payments from exiting employers;

(2) note the Fund's intention to consult with all participating employers on the updated FSS; and

(3) to approve the minor amendments to the Fund's Exit Credits Policy, which was incorporated in the Admission, Cessation and Bulk Transfer Policy.

36/21 **DERBYSHIRE PENSION FUND RISK REGISTER** The Head of Pension Fund presented the Derbyshire Pension Fund Risk Register. The Risk Register was kept under constant review by the risk owners, with quarterly review by the Director of Finance & ICT. A detailed annual review of the Risk Register by Derbyshire Pension Board was also introduced in early 2021. A copy of both the Summary and Main Risk Registers were attached to the report as Appendix 2 and Appendix 3 respectively. Changes from the previous quarter were highlighted.

The Risk Register included a target score which showed the expected risk score once the proposed additional risk mitigation controls and procedures had been implemented. The difference between the actual and target score for each risk item was also shown to allow users to identify those risk items where the proposed new mitigation and controls will have the biggest effect.

The Fund's Business Continuity Plan has continued to work well and all of the Fund's critical activities had been maintained throughout the period of business disruption caused by the pandemic. Alternative processes set up to accommodate remote working, remained under review, taking into consideration the possibility of the current working arrangements being in place for some time.

The Risk Register had the following four high risk items:

(1) Fund assets insufficient to meet liabilities (Risk No.19)
(2) LGPS Central related underperformance of investment returns (Risk No.30)
(3) Impact of McCloud judgement on funding (Risk No.37)
(4) Impact of McCloud judgement on administration (Risk No.44)

Details of each of the high risks were presented. With regard to the impact of McCloud judgement risks, the Committee were informed that a Project Board had been set up to formalise the governance of this major project. The Fund will continue to keep up to date with news related to the McCloud remedy and the cost cap process from the Scheme Advisory Board, the Local Government Association, the Government Actuary's Department and the Fund's actuary.

One new risk had been added to the Risk Register this quarter; Risks arising from a significant acceleration of the academisation of schools (Risk No. 18).

In April 2021, the Secretary of State for Education announced an acceleration of the academisation of schools noting: ‘the government’s vision for the school system to continue to move decisively towards a single model built on strong multi-academy trusts as its foundation’, although no timetable was attached to this statement.

Academies were state-funded schools that were independent from local authorities and were directly funded and controlled from the Department for Education. All maintained schools, which were funded and controlled by a local authority, were allowed to convert to academy status. Maintained schools were pooled with their local authority for the purpose of membership of the LGPS for their non-teaching staff. When a maintained school converted to an academy, it became a participating employer in the scheme in its own right.

Given the large number of remaining maintained schools in Derbyshire (over 300), there could potentially be a further big increase in the number of individual employers in the Fund despite the likelihood that many converting schools would join a multi-academy trust. Any further division of LGPS members into an increasingly wider pool of employers, will increase pressure on several areas of Fund operations.

This new risk had been included under the Governance section of the Risk Register as it had both funding and administrative implications. The Fund would continue to monitor local developments with respect to academisation and would monitor the administrative resource required by the Fund to support any increase in the number of participating employers. The funding implications of any academies consolidating in another LGPS fund would also be kept under review.

No risks had been removed and no risk scores had been changed, however, the narrative for the following risks had been updated:

Risk No. 22, relating to the risk of failing to correctly assess the potential impact of climate change on the investment portfolio and on the funding strategy, had been updated following a discussion on the appropriate wording when the Risk Register was last considered by Committee.

Risk No. 24, relating to employer covenants, had been updated to reflect the new employer flexibilities which had given administering authorities greater flexibilities for collecting exit payments from employers ceasing their active participation in the Fund.

Risk No. 40, relating to the level of cyber liability insurance relating to the pension administration system, had been updated following further consideration of the level of cover.

Risk No. 42, relating to potential delays to issuing Annual Benefit Statements and Pension Savings Statements, had been updated to reflect possible delays caused by the roll-out of the member self-service system ‘My Pension Online’.

The Chairman thanked Dawn Kinley, the Head of Pension Fund for her presentation. It was requested if there was any further background information in relation to the risks that could provide a history of how the scores had fluctuated. Officers would give this some thought.

RESOLVED to note the risk items identified in the Risk Register.

37/21 ARRANGEMENTS FOR THE DETERMINATION OF STAGE 2 APPLICATIONS UNDER THE LGPS APPLICATIONS FOR ADJUDICATION OF DISAGREEMENTS PROCEDURE Under Regulation 74 of LGPS 2013, Derbyshire County Council (DCC), as the administering authority of Derbyshire Pension Fund (the Fund/Pension Fund), and each participating employer in the Pension Fund, are required to appoint an adjudicator to consider applications by pension scheme members, or other stakeholders, for adjudication of their disagreement with a pension related first-instance decision made by the administering authority or the scheme employer. The adjudicators are required to make decisions on each application at Stage 1 of the ‘Applications for Adjudication of Disagreements Procedure’ (AADP) and provide written notice of their decision, or reasons for any delays in being able to make a decision, to the applicant within two months of the application having been received.

Under Regulation 76 of LGPS 2013, DCC, as the administering authority of Derbyshire Pension Fund, must consider appeals from Fund members or others who disagree with an adjudicator’s Stage 1 findings, at Stage 2 of AADP. LGPS 2013 requires that no person involved in the making of either the first-instance decision or the Stage 1 decision is involved in the reconsideration process at Stage 2.

All applications referred to the administering authority at AADP Stage 2 were currently reviewed and determined by the Committee during the exempt part of meetings following consideration of a detailed report prepared by officers of the Fund. Information related to individual members, which often included confidential medical records, was anonymised and redacted where appropriate.

The complexity of administering and managing LGPS funds has increased in recent years due to the introduction of the new scheme in 2014, the increased number and diversity of employers in the scheme, and the introduction of investment pooling. At the same time, oversight of LGPS funds has increased following the introduction of the LGPS Scheme Advisory Board (SAB) and Local Pension Boards and the extension of The Pension Regulator's duties to include oversight of the governance and administration of the LGPS.

Putting in place alternative arrangements for considering individual applications at AADP Stage 2, would allow Committee to increase its focus on strategic matters, further strengthening Committee's oversight of the governance of the Pension Fund. Additionally, alternative arrangements outside of the Committee's cycle of meetings would support decision making within the required timescales.

To assist the Committee's review of arrangements for AADP Stage 2 adjudications, Fund officers had undertaken a survey of six other LGPS funds who collaborated on joint LGPS working groups. The results of the survey were attached at Appendix 2 to the report and demonstrated that other Funds' operational arrangements for adjudicating Stage 2 applications were managed without reference to their local pensions committee, instead periodic summaries of cases are reported to committee to facilitate oversight.

The Committee were asked to delegate the determination of arrangements for adjudication of AADP Stage 2 applications to the Director of Finance & ICT. The Director of Finance & ICT would be responsible for ensuring that each AADP Stage 2 application would be adjudicated by an appropriately competent person from the following options:

- Director of Legal Services, DCC
- Assistant Director of Legal Services, DCC (except where the same officer had already adjudicated the case at AADP Stage 1)
- A suitably competent adjudicator from a different LGPS employer (except where the same person had already adjudicated the case at AADP Stage 1)
- A senior officer from a different LGPS Fund
- An external specialist lawyer

A guidance note will be prepared by officers to assist with the adjudication process.

Committee had previously decided to retain the consideration of Stage 2 adjudications in order to provide members with reassurance about the robustness of the process. The alternative arrangements set out above will be equally robust, whilst providing access to specialist expertise and more timely decisions, and they were supported by the Pension Board. The continuing provision of an annual summary report of all AADP cases will enable the Committee to retain oversight of the AADP process.

RESOLVED to approve the delegation of arrangements for the adjudication of AADP Stage 2 applications to the Director of Finance & ICT.

38/21 **LOCAL GOVERNMENT PENSION SCHEME INVESTMENT POOLING** The Committee were updated on the Fund's participation in the LGPS Central Pool (the Pool), the products launched by the Pool's pooling company, LGPS Central Limited (LGPSC/the company), and the plan for the transition of Derbyshire Pension Fund (the Fund) assets into LGPSC and collaboratively procured products. Mike Weston, Chief Executive Officer, Patrick O'Hara, Director of Responsible Investment & Engagement and Valborg Lie, Stewardship Manager of LGPS Central Ltd attended the meeting to give Members a brief update on the achievements to date and responsible investments.

The new Committee Members were provided with details and the legislative background that led to Derbyshire County Council (the Council) entering into an inter-authority agreement known as the LGPS Central Pool. LGPS Central Ltd had been established to manage investments on behalf of the pool of the eight Local Government Pension Scheme (LGPS) funds (collectively known as the Partner Funds) across the Midlands. The Company received authorisation from the Financial Conduct Authority in January 2018 and launched its first products in April 2018. The details of the products the Company had launched to date were provided and the following products were forecast to be launched during 2021:

- Private Equity Fund
- Targeted Return Fund
- Sustainable Equity Fund
- Property Fund

The Fund currently had approximately £580m invested in LGPSC products via the Emerging Market Equity Multi-Manager Fund and the Corporate Bond Multi-Manager Fund, representing approximately 10% of total Fund assets under management (AUM). A further 38% of AUM was currently invested in other collaboratively procured vehicles/life policies, with around 4% invested in direct property and around 9% invested in legacy alternative illiquid investment vehicles in unwind, and almost 6% held in cash.

Due diligence was currently being undertaken on the LGPSC Climate Multi Factor Fund, the Private Debt Fund, and the Infrastructure Fund and would be undertaken on the Sustainable Equity Fund in due course.

Based on the Fund's current asset allocation, it was expected that by 2025, around 80% of the Fund's assets would be invested in either LGPSC products or in other collaboratively procured vehicles/life policies, with the balance made up of investments in direct property, remaining legacy alternative illiquid assets in unwind, renewable infrastructure and cash. The forecast transition plan was contingent on the Fund's future asset allocation, and satisfactory due diligence on the relevant products.

Members were afforded the opportunity to ask questions of LGPS Central Ltd. A question was asked in relation to transition costs of the Corporate Bond Fund and were these taken into account. There were differing viewpoints on this between LGPS Central Ltd and officers and Mr Weston would seek clarification and report back in due course.

The Chairman wished to thank the representatives from LGPS Central Ltd for their attendance and informative presentation.

RESOLVED that Members note the contents of the report.