

Regulating public service pension schemes

An interim report of the consultation on:

- Draft code of practice no. 14 – Governance and administration of public service pension schemes
- Draft regulatory strategy – Ensuring high standards of governance and administration in public service pension schemes

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Introduction

The Public Service Pensions Act 2013 ('the 2013 Act') enables the establishment of new pension schemes for those working in the public services. In addition to provisions relating to the design of schemes and cost control, the 2013 Act includes requirements for the governance and administration of these schemes and provides for extended regulatory oversight by The Pensions Regulator (the regulator).

The 2013 Act requires us to issue one or more codes of practice containing practical guidance and the standards of conduct and practice expected from those involved with public service schemes in relation to certain duties and obligations set out in pensions legislation. Following our initial discussions with stakeholders we published our public service consultation package on 10 December 2013. This consisted of a consultation paper, a draft code of practice and a draft regulatory strategy.

This document summarises what we said in the consultation, what feedback we received and our plans for taking account of this feedback. In particular we are not providing a response or responses to the feedback at this stage. We will do this following the similar consultation in Northern Ireland to provide a consolidated response to both consultations.

Consultation process

The formal consultation process started on 10 December 2013 and closed on 17 February 2014. It consisted of two publications:

1. Draft code of practice no. 14 – Governance and administration of public service pension schemes (the draft code)
2. Draft regulatory strategy – Ensuring high standards of governance and administration in public service pension schemes (the draft regulatory strategy)

These publications were issued with a consultation document which included 16 questions addressing issues pertinent to each of the publications above and how we intend to regulate public service schemes.

What the consultation said

The consultation sought views on our draft code of practice for public service pension schemes providing practical guidance and setting standards on certain requirements of pensions legislation and our draft regulatory strategy to support the delivery of high standards of governance and administration of public service pension schemes.

The documents outlined our view that:

- governance and administration standards and practices in public service pension schemes impact upon the overall service provided to members (and other beneficiaries) including the correct payment of benefits at the right time, and
- good governance and administration should improve the efficiency of public service schemes and result in them being more cost effective for employers, including the government departments responsible for the schemes.

Our draft code sets out those specific matters about which we are required to issue a code. It has been designed to provide those responsible for running public service pension schemes with practical guidance about the legal requirements, as well as the standards of conduct and practice we expect from scheme managers, members of pension boards and others to help improve and maintain the governance and administration of their schemes.

The draft code provides a central reference point for the key areas of activity for public service pension schemes – governing your scheme, managing risks, administration and resolving issues. Where we come across situations in which there are breaches of pensions legislation or where there are poor standards of governance and administration, we will refer to the code when deciding on appropriate action.

The objective of our draft regulatory strategy is to support those involved in public service pension schemes in delivering well governed and administered schemes. To achieve this, the primary focus of our regulatory framework is to educate, enable and promote good practice to help those responsible meet their legal obligations and run their schemes competently. We want to provide the right tools that enable schemes to operate effectively and demonstrate compliance with their legal requirements. The draft regulatory strategy also explains the factors we will take into account when considering enforcement action if we believe that a breach of law has occurred and sets out how we intend to measure the impact of our activities.

In our consultation we asked a series of questions in relation to the draft code and draft regulatory strategy. They focused on the clarity and extent of the practical guidance and standards of conduct and practice necessary to evidence compliance with pensions legislation and on our approach to regulating public service schemes.

A list of consultation questions and a summary of feedback can be found in Appendix A.

Responses to the consultation

We are grateful to everyone who responded to our consultation. We received 48 responses from a wide range of stakeholder groups including government departments, pension administrators, legal and actuarial advisers, pensions consultancies and trade unions. Appendix B contains a full list of respondents.

Key issues raised in responses

The responses were generally very thorough and included some detailed views on the consultation questions and other areas addressed in the consultation documents. Our analysis has identified a number of common themes and we have summarised these below. Appendix A contains a more detailed analysis of the responses.

The common themes were:

- differences between the schemes
- participating employers
- pension boards of public service schemes
- regulatory sanctions/powers
- Career Average Revalued Earnings (CARE) schemes
- impact assessment.

Differences between the public service pension schemes

Our draft code and draft regulatory strategy relate to all schemes established under the 2013 Act. These schemes range from those which operate on an unfunded 'pay as you go' basis to those, such as the local government pension scheme (LGPS), which are funded and from those with many participating employers to those with either very few or a single employer.

Respondents generally welcomed and supported the draft code and draft regulatory strategy. However, some respondents felt that we had taken a 'one size fits all' approach to regulating the schemes and had not acknowledged sufficiently the differences among them and in particular between the unfunded and funded schemes. The same respondents questioned whether due to the differing nature of each scheme, our approach should be scheme by scheme when setting standards and assessing levels of compliance. They also questioned whether the variances in the type, size and funding nature of the schemes should be taken into account in considering how the legal requirements should be applied.

Similarly, many respondents with LGPS interests raised concerns that we had omitted from the scope of the draft code what they considered to be the unique nature of the LGPS. This includes the existing governance structure generally involving committees established under section 101 of the Local Government Act 1972 and the interaction of these committees with the scheme advisory board and the pension board in the new regime. They also expressed a view that we had not provided sufficient practical guidance relating to the governance of funding and investment matters.

Participating employers

The 2013 Act does not place any governance or administration requirements upon participating employers of public service pension schemes. While the consultation did not specifically ask about employers, a large number of responses raised issues in relation to them. Some respondents noted that scheme managers will be highly reliant upon employers to carry out certain functions which will enable them to comply with legal requirements under the 2013 Act. They suggested that many of the current administration problems were largely due to the failure of employers to competently and efficiently carry out what is required of them. It was suggested that this is also exacerbated by the large number and variety of employers participating in some of the schemes and the complexity this can bring to achieving compliance. In addition, a number of respondents referred to the increasing workload arising from the need to monitor employer covenants in multiple employer schemes.

Pension boards of public service schemes

The 2013 Act requires scheme regulations to provide for the establishment of a pension board for public service schemes but does not prescribe how pension boards shall be constituted. The only requirements set out are that pension boards must have an equal number of employer and member representatives and that prospective and existing members must not have a conflict of interest.

A large number of respondents expressed concern that we have not included within the scope of the draft code information relating to representation on pension boards, nor defined the principles that we would expect scheme managers to follow in establishing and maintaining them. These respondents indicated that they were keen to see specific guidance and good practice standards in relation to areas including how pension boards should be constituted, the appointment process, the selection of pension board members and whether there should be separate representation for distinct groups of employers and scheme members on the board. They also suggested we should provide further information on engaging with members and employers in relation to representation on the pension board and offer support for scheme managers on how to ensure this requirement is met.

Regulatory sanctions/powers

We have a range of enforcement powers under the 2013 Act if schemes fail to comply with legal requirements. Several respondents suggested that it would be helpful for the draft code or draft regulatory strategy to set out the sanctions/powers that we have and specify the information that we might expect to collect from schemes to fulfil our regulatory duty. Respondents considered that it would also be helpful to have an insight into what we will expect of them and the consequences of non-compliance.

CARE schemes

The 2013 Act introduced new pension arrangements for public service schemes including the use of a CARE basis, with benefits based on a proportion of the member's pensionable earnings during their career, instead of their final salary.

Some respondents expressed concern over the complexity of how a CARE pension is calculated and the administrative burden this will create in terms of record-keeping and maintaining contributions. They argued that the impact the CARE arrangements will have on schemes has not been recognised or clearly understood. These respondents commented that the new arrangements will have a detrimental impact on the effective administration of schemes and increase the costs involved.

Impact assessment

The consultation asked whether the draft code and draft regulatory strategy would place additional regulatory burden on schemes. Generally respondents commented that they did not expect any significant additional burden in relation to our activities. Some highlighted their expectation that schemes would review their processes in light of the code and would want to take steps to more readily demonstrate compliance with the underlying legal requirements but noted that this would assist with improvements to governance and administration.

Most respondents welcomed our new role in providing independent oversight of the governance and administration of public service schemes. However, a large number of respondents noted that additional resources would be needed to comply with the new legal provisions in relation to the establishment and maintenance of pension boards and also the administrative requirements of the reformed schemes.

Next steps

This consultation is in relation to the draft code which we are required to issue as a result of changes to the Pensions Act 2004 made by the 2013 Act. Corresponding legislation in Northern Ireland – the Public Service Pensions Act (Northern Ireland) 2014 – received royal assent on 11 March 2014 (which in turn amends the Pensions Order (Northern Ireland) 2005, also requiring us to issue a code). Now that the necessary provisions have commenced, we are consulting on an equivalent draft code in Northern Ireland.

For this reason, in this interim consultation report we are reporting the feedback we have received on the draft code and draft regulatory strategy but are not, at this stage, providing our response to that feedback. Once the consultation in Northern Ireland has closed we will update this interim report with further feedback received and will then provide our response to the points raised.

We will then make any appropriate modifications to the draft code prior to sending it to the Secretary of State who, if it is approved, must lay the final code in Parliament. For Northern Ireland we will follow a similar process with the Department of Social Development who must lay the final code in the Northern Ireland Assembly. Our aim is to achieve a consolidated public service code for the United Kingdom and be able to lay this in the respective legislatures in autumn of this year.

Appendix A

Consultation questions and a summary of feedback

Responses to the consultation

We asked a total of 16 questions and this section sets out in further detail the main points raised by respondents in relation to each of the consultation questions.

Draft public service code

1. 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?
 - Respondents generally welcomed and supported the draft regulatory strategy, draft code of practice and practical guidance
 - Some respondents felt we had taken a 'one size fits all' approach to regulating public service schemes. For example, they did not consider that the draft code had taken into account the differences between unfunded and funded schemes. Others suggested that we should take a scheme by scheme approach when setting standards and assessing levels of compliance due to the difference in type, size and funding nature of the schemes
 - Similarly, many respondents with LGPS interests were concerned that we had not included within the scope of the code the uniqueness of the LGPS or the structure and roles their schemes will have in place. They also commented that we have not provided sufficient practical guidance relating to governance of funding and investment matters
 - A few respondents commented that they felt that the draft code had been written with a private sector pensions approach and did not draw attention to the specific nature of public service schemes
 - A common question raised by respondents was in relation to our approach to compliance and enforcement. Respondents queried how they will know if they have met our standards, what we consider to be high risk activities and how we will monitor and identify non-compliance.

2. 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?
 - Many respondents expressed concern that we have not included within the scope of the draft code or practical guidance information relating to representation on pension boards, nor defined the principles that we would expect scheme managers to follow in establishing and maintaining them
 - Some respondents suggested that it would be helpful for the code to set out the sanctions/powers that we have and explain the types of risk we will be assessing. They also commented that it would be helpful if we specified the information that we might expect to collect from schemes to fulfil our regulatory duty, what we expected from them and the consequences of non-compliance.
3. 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?
 - While the consultation did not specifically ask about employers, many responses raised issues in relation to them. They did not consider that we had addressed the responsibilities of participating employers in ensuring effective governance and administration of the schemes
 - Some respondents also raised the issue of the large number of employers (in the thousands in the case of some schemes) participating in their schemes and the complexity this can bring to achieving compliance. In addition, a number of respondents referred to the increasing workload arising from the need to monitor employer covenants in multiple employer schemes
 - One respondent considered that the draft code went beyond what is required under the legislation and that the practical guidance contained too much specific and prescriptive detail and as such may be seen as the only way to comply.

Section 1: Introduction

4. Have we targeted the code at the right groups of people? If not, which have been overlooked?
 - Many respondents raised a concern that employers had not been acknowledged or addressed within the draft code and that they are a key stakeholder for public service schemes
 - A few respondents felt that we had not acknowledged that the new governance structures of schemes, in particular the LGPS, will not only involve scheme managers and pension boards but will involve other groups ie committees, civil servants, administrators, government officials, outsourcers, professionals etc
5. Is there any further information or explanation you would like to see in the 'terms used' section of the introduction?
 - Some respondents queried our use of the term 'schemes' and suggested that as the legal responsibility would always remain with the scheme manager that the use of the term introduced an element of ambiguity on who is legally responsible
 - Some respondents commented that it would be helpful to include the terms 'legal requirement', 'legal duty' and 'legal function'
 - Many respondents commented that it would be helpful to include the term 'participating employers'
 - A few respondents commented that it would be useful to define the term 'materially significant' (paragraph 109) in relation to the duty to report to the regulator on breaches of the law.
6. Does the code strike the right balance between being as concise as possible and providing enough practical guidance relating to the underlying legal obligations?
 - One respondent expressed a view that our approach to the draft code goes beyond what is required under the 2013 Act and that the practical guidance and good practice standards were too specific and prescriptive.

Section 2: Governing your scheme

7. Do we adequately describe the level of knowledge and understanding required of members of pension boards? If not, why not?
- Many respondents agreed that the level of knowledge and understanding is adequately described in the draft code
 - A few respondents raised concerns that we had not acknowledged that there is potential for pension board members to change on a regular basis and the additional burden this would create in having to deliver ongoing training
 - A few respondents raised concerns that there is not a specified induction or grace period within which it is reasonable to expect pension board members to acquire the knowledge and understanding required following their appointment
 - Some respondents commented that it would be helpful if the regulator could provide criteria or accreditation standards by which pension board members could demonstrate that they have the correct level of knowledge, understanding and skills expected
 - One respondent commented that the responsibility for ensuring that pension board members invest sufficient time in learning and development should not rest on the scheme but with the individual themselves
 - A few respondents with LGPS interests raised the concern that the draft code did not cover knowledge and understanding in relation to funding, investments and assessing and monitoring employer covenant. They also requested that we provide practical guidance for scheme managers, scheme advisory boards and the pension committees for the LGPS
 - Some respondents commented that it would be helpful for the code to distinguish between the overall knowledge and understanding requirements of a pension board versus the core knowledge and understanding of the individual members of a pension board.

8. 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?
- A few respondents commented that it would be helpful for the code to address conflicts of interest that apply to other roles that are involved with running of public service schemes including the scheme manager, pension committees, pension administrators etc
 - Some respondents raised concerns in relation to the trade union representative example in the conflict of interest section
 - A few respondents commented that the draft code did not address conflicts in relation to government officials with dual interests being appointed onto the pension board
 - Some respondents noted that they would like further practical guidance on identifying, monitoring and managing conflicts along with case study examples
 - One respondent expressed a view that with a pension board consisting of employer and employee representatives, actual conflicts of interest will exist and will need to be managed.
9. 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.
- Many respondents acknowledged the difficulty in transposing the concept of fiduciary duties to non trust based schemes. However, some respondents suggested that it would be helpful if we could set an explicit obligation of this nature to help focus the attention and understanding of members of boards when exercising their duties.

Section 3: Managing risks

10. 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?
- Some respondents commented that it would be helpful to see examples of 'core or critical risks' that schemes should identify and our expectations in relation to these risks
 - One respondent with LGPS interests raised a concern that the draft code did not cover the risk management of risks relating to investment, funding and the custody of assets.

Section 4: Administering your scheme

11. 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?
 - Some respondents expressed their concern over the complexity of how a CARE pension is calculated and the administrative burden this will create in terms of record-keeping and maintaining contributions
 - Many respondents raised the issue that data collection and record-keeping was not always in the control of the scheme manager and that we should address in the code how participating employers and outsourced administrators may impact the scheme managers' ability to comply
 - One respondent suggested that to improve transparency, we should include in the practical guidance relating to the 'information to be published about schemes' section that pension board members should declare their current employment/office position and for this to be published by schemes
 - A few respondents requested that we explain in the code how we will monitor compliance with the record-keeping regulations
 - A few of respondents commented that it would be helpful if the code could explain what the regulator expects from schemes with regards to reviewing their data/carrying out an annual 'full data review' as this could be burdensome on schemes to complete.
12. 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?
 - Many respondents were keen to see further detail and examples on what we believe to be materially significant and what should be reported
 - Some respondents felt that it would be useful to define the term 'materially significant' in relation to maintaining contributions and the duty to report to the regulator on breaches of the law.

Section 5: Resolving issues

13. Have we made clear the circumstances under which breaches of pensions legislation should be reported to us?
- A few respondents commented that it would be helpful if we could identify and provide practical guidance for others who have a responsibility to report breaches of legislation, eg employers and advisers in relation to reporting breaches
 - Some respondents requested further guidance on what we consider to be 'materially significant' to avoid the over-reporting of breaches
 - A few respondents commented that it would be helpful for the code to set out the sanctions that are available to us when dealing with breaches of legislation.

Draft public service regulatory strategy

14. Does the strategy, together with the public service code, sufficiently address risks to good governance and administration?
- Some respondents commented that we should expand the regulatory strategy to include all of the stakeholders participating in public sector schemes, including employers in public, private and third sectors
 - A few respondents commented that it would be helpful if we could set out in the code or regulatory strategy the sanctions/powers that we have and the information that we will be collecting from schemes as part of our regulatory activities
 - One respondent raised a concern that we have applied a private sector methodology in producing our draft regulatory strategy and that it does not sufficiently address risks to good government and administration in public service schemes
 - One respondent suggested that in the 'measuring impact' section of the regulatory strategy that we include obtaining feedback from the schemes as one of those measures.
15. Does the strategy explain adequately the approach we will take in regulating public service schemes?
- Some respondents commented that we should outline key principles for the regulation of public service schemes including a core set of principles for all scheme types with additional principles for funded schemes
 - A few respondents raised a concern that we have taken a private sector approach to regulation which is not feasible for public sector schemes.

Impact assessment

16. 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.
- Generally respondents commented that they did not expect any additional burden in relation to our activities, although some highlighted their expectation that schemes would review their processes in light of the code and would want to take steps to more readily demonstrate compliance with the underlying legal requirements. They also generally welcomed the new role of the regulator in providing independent oversight of the governance and administration of public service schemes
 - Many respondents commented that the 2013 Act and corresponding secondary legislation will require additional resources. In particular they mentioned the establishment and maintenance of pension boards and the administrative tasks to support the reform of the scheme benefits.

Appendix B

List of respondents to the consultation

| | |
|---|---|
| Aon Hewitt | Ministry of Defence (The Armed Forces Pension Scheme) |
| Association of Pension Lawyers | National Association of Pension Funds |
| Association of Principal Fire Officers | National Association of Schoolmasters Union of Women Teachers |
| Avon Pension Fund | National Union of Teachers |
| Bedfordshire Pension Fund | NHS Pensions Scheme Governance Group |
| Cabinet Office (Civil Service Scheme) | Northern Ireland Public Service Alliance |
| Cabinet Office (Civil Service Pension Scheme Management Board Member) | Norfolk Pension Fund |
| Capita (Police Pension Scheme) | Paul Burns GFireE, Divisional Fire Officer (Rtd) |
| Department for Communities and Local Government (Local Government Scheme) | Pensions Administration Standards Association |
| Department for Education (Teachers' Pension Scheme) | Police Negotiating Board Scotland Standing Committee |
| Department of Health and NHS Business Authority (NHS scheme) | Police Negotiating Board Staff Side |
| Fire Officers' Association | Public and Commercial Services Union |
| First Division Association | Sackers and Partners LLP |
| General Municipal Boilermakers | Scottish Public Pensions Agency |
| Hertfordshire County Council | Shropshire County Pension Fund |
| Heywood (aquilaheywood) | Society of Pension Consultants |
| Hymans Robertson LLP | Squire Sanders (UK) LLP |
| Institute of Chartered Accountants of Scotland | Suffolk County Council Pension Fund |
| Leicester, Leicestershire and Rutland Combined Fire Authority | Trade Union Centre |
| Local Government Pension Committee | Unison |
| Local Government Shared Services Pensions | Voice |
| London Pension Fund Authority | West Midlands Pension Fund |
| Mercer UK | West Sussex Pension Fund |
| Mid and West Wales Fire and Rescue Service | Wiltshire Pension Fund |

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