Unite response to the Ministry of Housing, Communities and Local Government (MHCLG) consultation on the Local Government Pension Scheme (England and Wales): Fit for the future – 16th January 2025

This response is submitted by Unite the Union, the UK and Ireland's largest trade union representing over one million members across all sectors of the economy including transport, manufacturing, financial services, food and agriculture, construction, energy and utilities, information technology, service industries, health, local government and the not for profit sector. Unite also organises in the community, enabling those who are not in employment to be part of our Union.

Unite has facilitated and negotiated pension benefit changes, agreed between members and employers, for many schemes. It is a key part of our role to balance the benefits provided, cost of that benefit provision and the risk that the scheme can afford to take, recognising the impact that this has on the funding level, investment strategy and affordability.

The most important consideration is pensions adequacy, which should drive decisions relating to pensions investment.

The government should enact policy to support the re-opening of defined benefit (DB) schemes (and the reinvigorating of DB provision) which in turn would affect their investment strategies.

Workers must have at least equal representation to employers in the governance of all pension funds.

Investment policies adopted by pension funds must have an explicit pro-worker approach, supporting unionisation at investee companies and assets.

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

Pooling hasn't delivered the returns and cost savings we were promised.

So how do the Government expect to fix this?

Making trade union members more integral in the governance structures would be a start.

There needs to be union member nominated representatives on the pools and they must have full voting powers, not just observers as is the case in some pools now.

Pools have not been tracking and analysing their own performance against each other, against the performance of assets held by member funds but not invested through the pool, or against relevant benchmarks in a consistent way.

Independent analysis is necessary before considering mandating further pooling or a particular pooling model.

Local Government Pension Scheme (LGPS) funds benefit from member engagement in governance which is not replicated in pools. Any future consistent model of pooling needs to have member involvement in a strong and effective layer of governance at the pool level, as well as continued democratic local control over the investment strategy for the assets administered by individual funds which belong to members of that fund.

In addition, the timescales involved in this consultation are extremely challenging.

The deadline for pool business plans is especially challenging for those pools that are not structured in a way that meets all or most of the minimum standards set out.

LGPS members must be at the heart of considerations about what is best for funds and pools.

It is absolutely right that where pools are implementing investment strategies and managing the transfer and investment of assets, as well as identifying suitable new investable opportunities for their funds, that they should have the expertise and capacity to do that in the best way for their partner funds.

It is critical that pools are properly able to take on the functions that government wishes them to in order to avoid additional unnecessary costs from duplication with services the fund already procures and pools having to externally procure services which could, with sufficient time, be built and delivered from within.

Question 2: Do you agree that the investment strategy set by the administering authority should include high-level investment objectives, and optionally, a high-level strategic asset allocation, with all implementation activity delegated to the pool?

Unite does not support introducing either incentives or requirements for schemes to invest in particular UK asset classes. Mandating in particular would compromise the ability of trustees to exercise their fiduciary duty in managing the investment of members' funds. It could also lead to poor value and increased systemic risk by encouraging herding into certain asset classes.

Support for investment in UK infrastructure can't conflict with fiduciary duty, so must have the right risk and return profile.

Unite members expect to see serious investment in public services following the disastrous years of Conservative austerity government. This requires increased tax revenues. But the burden should be borne by those who can afford it, not by short-changing those who have done the right thing by diligently saving for retirement. Unite has set out detailed plans for how a wealth tax, targeted at the richest in the UK, could underpin the investment the UK needs.

A properly sized National Investment Bank / Wealth Fund could attract pension fund investment into infrastructure or industry transition projects by issuing specific bonds targeted for this purpose, rather than through PE type equity deals.

Unite believes LGPS funds should be required to publish plans for investment with local benefit and that doing this would encourage levelling up by spreading investment around the country and encouraging pools and funds to develop and use local knowledge. This would bring together funds' fiduciary duty with their local characteristics. Ensuring that pools are geographically coherent would also enable them to take a regional as well as a local approach to place-based investing.

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

The primary fiduciary duty is to ensure pensions are paid in full and on time and this is what should remain at the heart of considerations about the future of LGPS pools.

A further risk is the loss of a relationship between funds with specific beneficiaries and workplaces which may lead to less real beneficiary engagement and a loss of sense of who the fund works for. Particularly as funds recruit from commercial asset managers to build internal investment capability it is very likely this can negatively affect internal culture. Anecdotal feedback from asset owners and managers from the UK and elsewhere confirm that this is indeed a risk unless funds have a very clear commitment to beneficiaries' interests.

It is also key for funds to have the ability to flex their strategy when needed, perhaps for cash flow reasons or in response to unforeseen investment or economic conditions/factors, in order to effectively discharge their fiduciary duty.

<u>Question 4: What are your views on the proposed template for strategic asset allocation in the investment strategy statement?</u> ***<u>(listed equity, private equity, private credit, property/real estate, infrastructure, other alts, credit, UK govt bonds, cash)</u>***

The government should enact policy to support the re-opening of DB schemes (and the reinvigorating of DB provision). Closed DB schemes represent a large proportion of total UK pension fund assets. However, because they are closed they have shifted away from growth assets and into bonds and other investments that match their investments more closely. Reopening DB schemes would inevitably affect their investment strategies and they would consider a wider range of asset classes.

Pension funds, and other institutional investors, will only invest in something if they consider that it will deliver desirable risk-adjusted returns. It is unlikely that the failure of pension funds to invest in 'UK asset classes' is driven by a lack of scale.

It is also important to remember that UK-listed or incorporated companies are not necessarily UK employers. The City conflates the two because elements within it are principally focused on transactions and the revenue derived from them. This contributes to the decline of the number of UK-listed companies because they are not opposed to delisting (because the delisting process is another transaction that generates revenue).

Without an explicit pro-worker investment approach the benefits of any economic activity driven by increased investment will not necessarily be broadly felt. Rather increased allocations to asset classes such as infrastructure and private equity may simply serve to enrich intermediaries and extend their ownership and control of important parts of the UK economy.

Unite has concerns about the growing allocations by LGPS and other pension funds to private credit. We note that organisations including the Bank of England and IMF have raised concerns about the opacity of the asset class and potential risks. The floating rate nature of loans made by private credit managers can put significant pressure on borrowers. In addition, the growth in Payment in Kind, effectively just deferring debts, is a possible indication of risks ahead.

Unite is currently in dispute with Oscar Mayer, a food manufacturing business that was taken over by its lender Pemberton Asset Management, a private credit manager, in 2023. Prior to the takeover Oscar Mayer saw interest charges and debt repayments surge. Since the takeover Oscar Mayer management has sought to force through cuts to workers pay. Pemberton has raised well over £0.5bn from LGPS funds including the London CIV and Wales Pension Partnership pools.

This is why it is why it is vital that members are involved in the oversight of asset managers in order to hold those that support attacks on workers' terms and conditions accountable. Professional investment staff are likely to feel more affinity with their asset manager service providers than the workers whose capital they are investing or whose terms and conditions those managers are undermining.

Unlisted infrastructure and other private equity investments are also not necessarily a good thing for the UK economy if the result is the extraction of value rather than real investment. The experience of Thames Water demonstrates how such investments can be very damaging.

In addition the UK Government has a poor track record of staying the course on long term UK infrastructure projects and tend to drop them when they become politically unfavourable, so Government should guarantee, underpin any long term investment.

The LGPS can't just be expected to be given the UK infrastructure projects that the private sector isn't interested in and at no point should members benefits and contributions in the LGPS be undermined.

Question 5: Do you agree that the pool should provide investment advice on the investment strategies of its partner AAs? Do you see that further advice or input would be necessary to be able to consider advice provided by the pool – if so, what form do you envisage this taking?

Regulation 7(5) of the 2016 Investment Regulations states that funds "must consult such persons as it considers appropriate as to the proposed contents of its investment strategy" and must also take "proper" advice.

Key areas, such as the fund's approach to responsible investment, need to remain close to the fund and may well require specialist and/or independent advice.

From a governance perspective, perceived and actual conflicts of interest could arise where the pool is the fund's principal, and possibly only, source of investment advice.

One way of managing these conflicts is to have proper Trade Union member nominated representation, so this can be managed transparently via robust governance arrangements.

Question 6: Do you agree that all pools should be established as investment management companies authorised by the FCA, and authorised to provide relevant advice?

Unite is concerned that requiring FCA authorisation may not lead to tangible improvements in how pools operate or, crucially, how they deliver outcomes for their LGPS funds. It is also a process that is likely to take a lot of time and cost over the next year. If the Government's intention by requiring FCA authorisation is to effectively force pools to merge than has been the case to date, then it would be better for government to be clear about that.

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

In Australia, the not-for-profit – or profit-for member – trusts that are operated jointly by employee and employer representatives with a fiduciary relationship with the beneficiaries have a long track record of outperforming the for-profit retail funds where the fiduciary relationship is between trustees and shareholders.

This reflects an understanding that trustees' fiduciary duty goes beyond maximising short-term returns. Members are workers and benefit from a strong domestic economy that delivers good jobs and prosperity. This means that governance structures with a strong fiduciary duty are likely to not only increase levels of asset diversification and domestic investment, but to bring a focus on the social and environment impact of those investments, for example - promoting health and safety standards, collective bargaining, respectful management of change, and the protection of workers' human rights.

Unite believes that regional inequality should be seen as both a social issue that ought to be addressed by government, and something which will impact on the likely availability of investable opportunities for funds locally.

To increase exposure to UK productive finance, the onus is on the Government to identity investable projects in need of finance, and to package them in ways that meet the needs of pension funds.

Question 14: Do you agree that administering authorities should work with their Combined Authority, Mayoral Combined Authority, Combined County Authority, Corporate Joint Committee or with local authorities in areas where these do not exist, to identify suitable local investment opportunities, and to have regard to local growth plans and local growth priorities in setting their investment strategy? How would you envisage your pool would seek to achieve this?

The National Wealth Fund and British Business Bank should work together to pull together a pipeline of investable opportunities for LGPS funds and institutional investors more generally. The Government should create and market a selection of social impact bonds. Currently these tend to be at too small a scale to interest LGPS investors but the aggregation of appropriate opportunities would allow all funds to invest at a scale that is appropriate for them.

Question 15: Do you agree that administering authorities should set out their objectives on local investment, including a target range in their investment strategy statement?

Support for investment in UK infrastructure can't conflict with fiduciary duty, so must have the right risk and return profile. UK Governments have a poor track record of staying the course on UK infrastructure projects when they become politically unfavourable, so government should guarantee to underpin any investment.

Question 16: Do you agree that pools should be required to develop the capability to carry out due diligence on local investment opportunities and to manage such investments?

Conducting due diligence is obviously an important requirement but ultimately who will be taking the decision the pool or the fund? As these decisions could be political, these decisions are best being made at fund level.

Question 17: Do you agree that administering authorities should report on their local investments and their impact in their annual reports? What should be included in this reporting?

Yes.

The Good Economy's Annual Assessment of the Place-Based Impact of GMPF's Local Investment Portfolio shows that the impact themes across GMPF's two local investment portfolios are jobs, place and economic development. Metrics utilised in the report fall under these themes and examples include number of jobs supported or created, number of homes completed, in development or planned and the number of clean energy and sustainable assets.

So, something similar to this would be good. Metrics included will depend on the audience and also how impact investing is approached.

<u>Question 19: Do you agree that administering authorities should be required to prepare and publish a governance and training strategy, including a conflict-of-interest policy</u><u>?</u>

Paragraph 91 of the consultation document mentions in extremely broad terms the need for 'representation' to be covered in the new strategy document. Can you confirm that this is shorthand for the recommendation in the Good Governance action plan that the Government expects the full recommendation to be specifically covered?

C.1 Each fund must produce and publish a policy on the representation of scheme members and non-administering authority employers on its committees, explaining its approach to voting rights for each party.

Unite believes the requirement for each administering authority to publish a clear policy on representation, as set out above, should be explicitly committed to for the avoidance of doubt. Unite would also emphasise that voting rights need to be meaningful. The policy should also state how member and employer representatives can be supported, through information and officer time, to the same degree that elected members on Committees are supported.

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

Member nominated representatives should not have the same requirements. The Pension Toolkit should be sufficient as it is currently in all other private sector DB schemes for member nominated representatives.

The guidance will need to use insight from officers who are already providing a successful training program for their committee and board members, take into consideration the effectiveness of different training methods, consider any barriers in place which may prevent access to training and incentives which could improve training take-up.

<u>Question 26: What are your views on whether to require administering authorities to appoint an independent person as adviser or member of the pension committee, or other ways to achieve the aim?</u>

How does this fit with existing legislation on local authority committees and voting rights?

What evidence is available which suggests there are 86 individuals who fit the criteria to be able to support the role requirements to encompass supporting the committee on investment strategy, governance and administration? Has MCHLG carried out any research into the likely cost of this proposal?

What is the expected impact of this proposal on remuneration of other pension committee members?

If someone doesn't have one of the first two qualifications, what is classed as 'significant experience'?

Again, member nominated representatives should not have the same requirements. The Pension Toolkit should be sufficient as it is currently in all other private sector DB schemes for member nominated representatives.

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

Trade union member nominated representation at pool level with full voting powers is needed.

There should be a minimum of three Trade Union member nominated representatives. One for each recognised Trade Union.

Regular reporting, surveys, attendance at fund events, open communication channels in member documents by the pools will help.

As noted previously, without direct member involvement it is likely that pools shift towards a greater affinity with the asset management industry than with beneficiaries, particularly as staff are likely to shift between the two.

It would be a significant mistake for the government to be complicit in the reduction of member involvement in the governance of their own retirement savings. This risks permanently tilting the field in favour of financial intermediaries and away from the interests of workers.

Unite urges the government to talk to trade unions globally about their experience of pension funds with different governance models and how this affects their orientation to the interests of workers. Several European countries' pension systems and the superannuation system in Australia have strong member representation that offer examples.

Question 29: Do you agree that pools should report consistently and with greater transparency including on performance and costs? What metrics do you think would be beneficial to include in this reporting?

The existing pool returns to MHCLG should have been published and there should have been more transparency to date.

The question needs to be 'what happens if sub-level performance and/or costs increase unfavourably in comparison to peers?'

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John Neal – National Pensions Officer, Unite the Union 16th January 2025