



## Report of the Section 151 Officer

Pension Fund Committee - 17 November 2021

### **Competition and Markets Authority (CMA) – Setting Objectives for Investment Consultants**

<b>Purpose:</b>	To set and monitor measurable objectives for appointed investment consultants as required by CMA requirements
<b>Policy Framework:</b>	To comply with CMA requirements
<b>Consultation:</b>	Legal, Finance and Access to Services.
<b>Recommendation(s):</b>	It is recommended that the Pension Fund Committee:  1) Approves the Investment Consultants' identified objectives and their progress against the same attached at Appendix 1, subjective to periodic review by the Deputy Chief Finance Officer.
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#### **1. Background**

- 1.1 At the end of 2018, the Competition and Markets Authority (“CMA”) published its report following a review of the investment consulting and fiduciary management markets. Earlier this year, following on from this review, the CMA issued an order, setting out requirements for the appointment and governance of fiduciary managers, and for Pension Scheme Trustees (Pension Scheme Trustees means the trustees or

managers of Occupational Pension Schemes that have their main administration in the United Kingdom. The CMA requirements extend to both Trust-based schemes, and Local Government Pension Schemes (i.e. Pension Committees) to set objectives for their investment consultants.

## **2. What are the requirements?**

2.1 The CMA has stipulated that Pension Scheme Trustees should set objectives for their investment consultants, and that such objectives should be:

- 1 'closely linked' to the pension scheme's strategic objectives
- 2 reviewed at least every three years, and after a significant change to the investment strategy or objectives
- 3 established no later than 10 December 2019 (i.e. 6 months following the date of the final Order published by the CMA) or prior to appointment of a new investment consultant

The CMA has set out specific actions that must be carried out by trustees using fiduciary managers. We can provide separate guidance addressing these requirements should this be relevant for your scheme.

## **3. The Importance Of Objectives**

3.1 Establishing long term objectives is part of a well organised and well managed governance approach. Provided that appropriate resources are allocated to support longer term goals, having clear, structured and measurable objectives can greatly enhance the chances of long term success for your scheme.

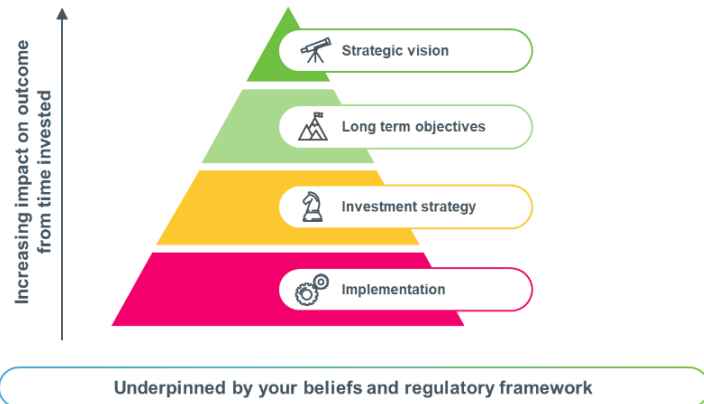
3.2 The extension to set objectives for investment consultants could be regarded as a natural progression towards all stakeholders being aligned towards a common goal. Indeed, we believe that best practice would be to establish objectives for all key service providers supporting Pension Scheme Trustees in achieving their longer-term goals, not just your investment consultants.

## **4. Establishing Objectives For Consultants**

4.1 In their accompanying explanatory, the CMA states that objectives for consultants should include a clear definition of the outcome expected, and timescales for achieving this. In addition, objectives should be measurable thereby supporting reporting to Pension Scheme Trustees.

Your funding and investment objectives will reflect your strategic vision and specific circumstances.

And so the objectives for your investment consultant should equally be tailored to reflect this.



We envisage that such objectives can be set in the context of the governance model illustrated.

4.2 By way of an example, a pension scheme may have the following long-term investment objective:

- *“Achieve the returns from investments to meet the long-term funding objective whilst keeping risk within acceptable levels to support stable and affordable contributions from the employer”.*

A corresponding objective for investment consultants may be:

- *For DB schemes, to “Provide advice on the investment strategy to deliver a target net return of XX% over gilts on the scheme’s investments with as little risk as possible, in order to support full funding by 20XX and stable and affordable contributions from the employer.”*

4.3 In addition to strategic advice, trustees will typically look for their consultant to provide advice around the implementation of the strategy. This might be captured by objectives around the following:

- Effectiveness of strategy to meet cashflows and liquidity requirements
- Effectiveness and efficiency of implementation of the strategy

Other broad areas that we believe you may wish to capture in the objectives, but which are less directly measurable, include:

- Efficiency in the governance of the strategy
- Provision of regulatory updates and meeting compliance requirements
- Ongoing monitoring of the investment arrangements
- Quality and timeliness of advice to enable timely, informed decision making.

## 5. Measuring Success in Practice

- 5.1 One of the key challenges of measuring success is that many methods and metrics for assessing performance are typically short-term in nature and can be unhelpful for the purpose of measuring 'success' of long-term objectives. In some cases, these methods and metrics could lead to counterproductive decisions and hence hinder success when not considered in the context of what trustees are trying to achieve over the long term.
- 5.2 Trustees should align the measurement of investment consultants to appropriate time periods. Based on the example above, such measures for DB schemes may include:
- *Strategy*: measure over rolling 5 year periods, the contribution from the investment strategy toward achieving the agreed long term strategic targets, and the extent to which progress has remained within expected tolerances given the agreed risk profile.
  - *Implementation*: measure over rolling 3 year periods the return on the Scheme's assets relative to the Scheme's composite benchmark return and target return, net of fees.

## 6. Reporting Compliance

- 6.1 As set out in their Order, the CMA has established that those subject to the new requirements should report on their compliance on an annual basis. This covers both the adherence to setting objectives for consultants and assessing the extent to which investment consultants are on track to meet those objectives.
- 6.2 In addition to this, if applicable, Pension Scheme Trustees will also be required to report on the appointment and governance of fiduciary managers.
- 6.3 Pension Scheme Trustees will be required to submit their first round of compliance reporting no later than 12 months and 4 weeks after the date that the relevant requirements came into force. This translates into a deadline of early January 2021.
- 6.4 On 29 July 2019, the Department for Work and Pensions ("DWP") released its consultation to turn the CMA's requirements into legislation. As part of their draft legislation, the DWP has specified that trustees (excluding LGPS) would be expected to report compliance annually via the Pensions Regulator's scheme return. The Pensions Regulator is also consulting on draft guidance, focussing mainly on how trustees should assess the performance of their investment consultants relative to

objectives.

6.5 The former Ministry for Housing, Communities and Local Government is clarifying how the requirements will translate to the LGPS.

## **7. Legal Implications**

7.1 There are no direct legal implications arising from this report.

## **8. Financial Implications**

8.1 There are no financial implications arising directly from this report.

## **9. Equality and engagement Implications**

9.1 There are no equality implications arising from this report.

**Background Papers:** None

### **Appendices:**

Appendix 1 - Investment Consultant Performance Objectives

## Investment Consultant Performance Objectives

<b>1</b>		<b>Demonstration of value added advice services</b>
	1.1	Help the trustee to implement an investment strategy which adds value through the integration of ESG (including climate change) and stewardship considerations in their investment manager appointments
	1.2	Enable the Pension Fund Committee to access a wider range of opportunities and portfolios of assets (and/or build portfolios of assets)
	1.3	Assisting the Committee in setting well-defined strategic objectives for the Fund: <ul style="list-style-type: none"> <li>- Achieving full funding with an acceptable degree of risk</li> <li>- Ensuring sufficient liquidity of assets to meet pension cashflows</li> <li>-</li> </ul>
	1.4	Providing strategic advice to ensure a strategy consistent with Fund's objectives
	1.5	Advising on cost-efficient implementation of the investment strategy at all times <ul style="list-style-type: none"> <li>-</li> </ul>
<b>2</b>		<b>Delivery of specialist services</b>
	2.1	Help the Pension Fund Committee to decide on an appropriate risk and performance objectives
	2.2	Help the Pension Fund Committee to decide' in consultation with key stakeholders, to do the following: <ul style="list-style-type: none"> <li>• to help the Pension Fund Committee to develop and define their investment beliefs, ESG Policies, RI Policies, Voting Policies</li> <li>• to help the Pension Fund Committee to review their investment governance arrangements and terms of reference for any subcommittees or delegated authorities</li> </ul>
<b>3</b>		<b>Proactivity of advice</b>
	3.1	Advise the Pension Fund Committee on new investment opportunities or emerging risks
	3.2	Advise the Pension Fund Committee on market pricing opportunities to mitigate or manage risk
	3.3	Deliver training to enable the Pension Fund Committee to engage with new investment opportunities, emerging risks or opportunities to

		manage risk
	3.4	Advise on any changes in the investment governance arrangements or delegated authorities which are necessary to enable the Pension Fund Committee to best access the emerging opportunities
<b>4</b>		<b>Support with member engagement and communication</b>
	4.1	Through the use of communication and behavioural techniques, help the Pension Fund Committee effectively engage with their membership to better understand their needs
<b>5</b>		<b>Support with scheme management and compliance</b>
	5.1	On a regular (quarterly) basis, monitor the performance of the scheme's investment strategies and also the performance of the scheme's investment managers
	5.1	Produce investment reports, briefing papers and investment advice in advance of trustee meetings and on a timely basis
	5.3	Assist the Pension Fund Committee with the review and update as appropriate the scheme's Investment Strategy Statement
	5.4	Provide periodic written advice on any direct investments held
	5.5	Provide trustee training as required
	5.6	Ensure compliance of the scheme's investment arrangements with the regulations
<b>6</b>		<b>Relationship and service standards</b>
	6.1	Agree any changes of (named) investment consultant(s) and meeting covers with the Deputy Chief Finance Officer in advance
	6.2	Maintain fees in line with tender submission
	6.3	Agree fee budget with officers for any significant piece of work
	6.4	Clear understanding of the scheme's goals and objectives
	6.5	Appropriate quality and quantity of resourcing to meet the needs and requirements of the scheme
	6.6	Strong positive working relationship with the Pension Fund Committee
	6.7	Appropriate conflicts of interest or management and mitigation of any conflicts

<b>7</b>		<b>Support with additional matters arising</b>
	7.1	Provide advice and assistance to the Pension Fund Committee on any other investment issues arising (for example following court rulings affecting the scheme)