

Report of the Director West Yorkshire Pension Fund to the meeting of Pension Board to be held on 9 November 2016.

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Subject: The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016

Summary statement:

The Department for Communities and Local Government (DCLG) has laid The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, which enable the pooling of investments.

The new regulations, in summary, make three changes:-

- The introduction of an Investment Strategy Statement (replacing the Statement of Investment Principles) and the removal of the prudential limits.
- The requirement for funds to pool their assets.
- The introduction of the power for the Secretary of State to intervene where an Investment Strategy is deemed not acceptable, a fund does not make satisfactory pooling arrangements, or a fund does not make suitable arrangements to make investments determined by the Secretary of State.

Recommendations

It is recommended that members note that the Regulations do not cause any concerns on the matters pertaining directly to investments, but that there have been no restrictions applied to the power of the Secretary of State to intervene in local authorities investment decisions, which does not support the policy objective of making local authorities clearly accountable for their decisions by removing the schedule of investment limits.

Rodney Barton
Director

Phone: (01274) 432317
E-mail: Rodney.barton@wypf.org.uk

1. Background

- 1.1 DCLG consulted at the beginning of the year on these Regulations, and a response was duly submitted by WYPF, the main issue being concerns surrounding the power for the Secretary of State to intervene in investment decisions made by councillors who are democratically accountable under the primary legislation.
- 1.2 The Regulations were laid before Parliament on 23 September 2016, and are due to come into force on 1 November 2016. This may be delayed, as there is to be a debate on the Regulations in the House of Lords.

2. The Investment Regulations

- 2.1 The regulations make provision in relation to the management and investment of pension funds held by administering authorities required to maintain such funds by the Local Government Pension Scheme Regulations 2013. They revoke and replace the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009.
- 2.2 Specific provision is made for administering authorities to publish an investment strategy in accordance with guidance issued by the Secretary of State and for the Secretary of State to issue a direction to any authority which fails to act in accordance with its statutory obligations, or guidance issued.
- 2.3 Regulation 3 defines what is meant by an “investment” for the purposes of the regulations. For clarification, the definition makes express reference to futures, options, derivatives, limited partnerships and some types of insurance contracts. It also defines with whom a contract of insurance can be entered into.
- 2.4 Regulation 4 sets out the monies that an administering authority must credit to its pension fund. It also sets out the administering authority’s responsibility to pay benefits to members, and that costs of administering the scheme can be charged to the fund except where prohibited by other regulations.
- 2.5 Regulation 5 outlines the limited circumstances under which an administering authority can borrow money that the pension fund is liable to repay.
- 2.6 Regulation 6 requires administering authorities to deposit all pension fund monies in a separate bank account and lists those institutions that can act as a deposit-taker. A deposit taker cannot use pension fund monies to set-off any other account held by the administering authority or a connected party.
- 2.7 Regulation 7 places an obligation on administering authorities to consult on and publish an investment strategy statement, which must be in accordance with guidance from the Secretary of State. The statement must demonstrate that investments will be suitably diversified and should outline the administering authority’s maximum allocations for different asset classes, as well as their approach to risk and responsible investing. Separate guidance from the Secretary of State will clarify how the Government’s announcement on boycotts,

sanctions and divestments should be taken into account when investment decisions are taken. The guidance is available on the Government's website at <https://www.gov.uk/government/publications/local-government-pensionscheme-guidance-on-preparing-and-maintaining-an-investment-strategystatement>

- 2.8 Regulation 8 provides the Secretary of State with the power to intervene in the investment function of an administering authority if he is satisfied that the authority is failing to act in accordance with the regulations and guidance. The regulation also enables the Secretary of State to initiate enquiries if an intervention is warranted and must consult the authority concerned. The Secretary of State can intervene by directing the authority to undertake a broad range of actions to remedy the situation.
- 2.9 Regulation 9 details how an administering authority may appoint external investment managers.
- 2.10 Regulation 10 allows administering authorities to invest in Treasury approved collective investment schemes.

3. Investment Strategy Statement

- 3.1 The Regulations remove the existing schedule of limitations on investments, and authorities will be expected to take a prudential approach, demonstrating that they have given consideration to the suitability of different types of investment, have ensured an appropriately diverse portfolio of assets and have ensured an appropriate approach to managing risk.
- 3.2 This will be set out in the Investment Strategy Statement (ISS), which authorities will be required to prepare, having taken proper advice, and publish. The statement must cover:
 - A requirement to use a wide variety of investments.
 - The authority's assessment of the suitability of particular investments and types of investments.
 - The authority's approach to risk, including how it will be measured and managed.
 - The authority's approach to collaborative investment, including the use of collective investment vehicles and shared services.
 - The authority's environmental, social and corporate governance policy.
 - The authority's policy on the exercise of rights, including voting rights, attached to its investments.
- 3.3 WYPF presently has a Statement of Investment Principles, which covers most of these matters, but will be reviewed, and presented to the January 2017 meeting as the ISS. Pooling is a new area to be covered by the ISS, so we will work with our partners in preparing a common section on pooling.
- 3.4 The ISS must be published by 1 April 2017.

4. Secretary of State Power of Intervention

4.1 Under Regulation 8 the Secretary of State may make a direction requiring all or any of the following:

- that the authority make such changes to its investment strategy under as the Secretary of State considers appropriate, within such period of time as is specified in the direction;
- that the authority invest such assets or descriptions of assets as are specified in the direction in such manner as is specified in the direction;
- that the investment functions of the authority under these Regulations and under the 2013 Regulations be exercised by the Secretary of State or a person nominated by the Secretary of State for a period specified in the direction or for so long as the Secretary of State considers appropriate;
- that the authority comply with any instructions of the Secretary of State or the Secretary of State's nominee in relation to the exercise of its investment functions under these Regulations and the 2013 Regulations and provide such assistance as the Secretary of State or the Secretary of State's nominee may require for the purpose of exercising those functions.

4.2 Before making a decision whether to issue a direction the Secretary of State must consult the authority concerned.

4.3 In reaching a decision whether to issue a direction the Secretary of State must have regard to such evidence of the manner in which the authority is discharging or proposes to discharge its investment functions as is reasonably available including

- any report from an actuary appointed under section 13(4) of the Public Service Pensions Act 2013 (employer contributions in funded schemes) or by the authority under regulation 62 of the 2013 Regulations (actuarial valuations of pension funds);
- any report from the local pension board appointed by the authority or from the Local Government Pension Scheme Advisory Board;
- any representations made by the authority in response to the consultation;
- any other evidence that the Secretary of State regards as relevant to whether the authority has been complying with these Regulations or acting in accordance with guidance.

An authority must comply with any request from the Secretary of State to facilitate the obtaining of information

5. Government Response to the Consultation

5.1 The Government received 23,516 responses to the consultation on these Regulations, which can be found at:

<https://www.gov.uk/government/consultations/local-government-pension-schemeopportunities-for-collaboration-cost-savings-and-efficiencies>.

Over 23,000 disagreed with the proposal to grant the Secretary of State the power to intervene in local authorities' investment decisions.

Contact Officer: Rodney Barton
Telephone Number: 01274 432317

Email: rodney.barton@wypf.org.uk

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