

EXPLANATORY MEMORANDUM TO
THE LOCAL GOVERNMENT PENSION SCHEME (MANAGEMENT AND
INVESTMENT OF FUNDS) REGULATIONS 2016

2016 No. 946

1. Introduction

- 1.1 This explanatory memorandum has been prepared by the Department for Communities and Local Government and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

- 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 under Regulation 7.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 None.

Other matters of interest to the House of Commons

- 3.2 This entire instrument applies only to England and Wales.
- 3.3 In the view of the Department, for the purposes of House of Commons Standing Order 83P the subject-matter of this entire instrument would be within the devolved legislative competence of the Northern Ireland Assembly if equivalent provision in relation to Northern Ireland were included in an Act of the Northern Ireland Assembly as a transferred matter and the Scottish Parliament if equivalent provision in relation to Scotland were included in an Act of the Scottish Parliament.

4. Legislative Context

- 4.1 The Public Service Pensions Act 2013 (“the 2013 Act”) enables the Secretary of State to make regulations creating schemes of pensions for, amongst others, local government workers.
- 4.2 In England and Wales, such a scheme is created by the Local Government Pension Scheme Regulations 2013 (“the 2013 Regulations”). The 2013 Regulations were made exercising powers in the Superannuation Act 1972 but section 18 of the 2013 Act provides for them to take effect as scheme regulations made under that Act.

4.3 The scheme created by the 2013 Regulations is a funded scheme administered by 89 administering authorities. These Regulations make provision in relation to the management and investment of the funds held by those authorities.

5. Extent and Territorial Application

5.1 The territorial extent and application of this instrument is England and Wales.

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

7.1 The regulations are the culmination of work looking into local government pension scheme investments that began early in 2013. They have been developed in response to a consultation “Opportunities for collaboration, cost savings and efficiencies”, which considered whether savings might be delivered through collective investment and greater use of passive fund management. A copy of the consultation and the Government’s response is available on the Government’s website <https://www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies>.

7.2 The regulations also reflect various recommendations made by a small working group established to look at whether the approach to risk management and diversification in the existing regulations was still appropriate.

7.3 The main provisions are described in paragraphs 7.5 to 7.12.

Preliminary Provisions

7.4 Regulations 1 and 2 cover the citation, commencement, interpretation and extent of the regulations. Regulations 11 and 12 cover consequential amendments and revocations and transitional provisions.

Main Provisions

7.5 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 who a person with whom a contract of insurance can be entered into is.

7.6 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.

7.7 Regulation 5 outlines the limited circumstances under which an administering authority can borrow money that the pension fund is liable to repay.

7.8 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.

- 7.9 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. A copy of the guidance is available on the Government's website at <https://www.gov.uk/government/publications/local-government-pension-scheme-guidance-on-preparing-and-maintaining-an-investment-strategy-statement>
- 7.10 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.
- 7.11 Regulation 9 details how an administering authority must appoint external investment managers.
- 7.12 Regulation 10 allows administering authorities to invest in Treasury approved collective investment schemes.

Consolidation

- 7.13 These regulations revoke and replace the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 and one instrument which amended those regulations.

8. Consultation outcome

- 8.1 The regulations were subject to a statutory consultation between 19 November 2015 and 19 February 2016. As at 7 March, 23,516 responses had been received. The format of the consultation included a narrative section explaining the consultation process and policy context and a set of draft regulations.
- 8.2 The consultation papers were sent to the Welsh Assembly, the Chief Executives of all principal local authorities in England and Wales, all local government trade unions, the Trades Unions Congress, the Government Actuary's Department and various separate representative bodies including the Association of Consulting Actuaries and the Chartered Institute of Public Finance and Accountancy. Copies of the consultation paper and a full list of consultees can be found at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/479642/Consultation_on_investment_reform.pdf
- 8.3 As shown below, about 98% of the 23,516 responses were received from members of the public.

Origin of response	Total
Councils/Administering Authorities	62
Trade unions	278

Representative bodies	2
Religious groups	6
Asset managers	7
Pension lawyers	6
Consulting actuaries	3
Investment consultants	3
Members of the public	23,131
Other	18
Total	23,516

The main areas of concern from members of the public and other groups are summarised below.

- Over 23,000 members of the public disagreed with the proposal to grant the Secretary of State the power to intervene in local authorities' investment decisions. It is claimed that the proposal would undermine the rights and choices of pension fund members and the independence of financial decision making to act in members' interests.
- A similar number claimed that the proposed intervention power undermines the Government's policy of transferring power to local government.
- A significant number of respondents also considered that the proposed regulations would prevent administering authorities from taking ethical considerations into account when making investment decisions. In particular, concerns were expressed about the way in which the policy on compliance with UK foreign policy was to be taken forward in the guidance to be published under Regulation 7(1).

8.4 The Government's response to these representations can be found at <https://www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies>.

8.5 The main alteration in the final version of the regulations is an extension to the period in which the new investment strategy statements under Regulation 7 need to be published from 1st October 2016 to 1st April 2017. The period during which existing statements of investment principles under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 can remain in force until the new statements are published is similarly extended.

9. Guidance

9.1 Regulation 7(1) requires administering authorities to formulate an investment strategy statement which must be in accordance with guidance issued by the Secretary of State. The Department will issue the guidance at the same time as the government's response to the consultation is published on the clear understanding that it will have no legal impact until Regulation 7 comes into effect.

10. Impact

10.1 The legislation does not impact on business, charities or voluntary bodies.

10.2 The legislation does not impact on the public sector.

10.3 An impact Assessment has not been prepared for this instrument.

11. Regulating small business

11.1 The legislation does not apply to activities that are undertaken by small businesses.

12. Monitoring & review

12.1 These regulations will be monitored by the Department and reviewed on a regular basis. To assist in this process, the Department will rely on the function conferred on the scheme advisory board to advise the Secretary of State on scheme changes.

13. Contact

13.1 Chris Megainey at the Department for Communities and Local Government
Telephone: 0303 444 3145 or email: chris.megainey@communities.gsi.gov.uk can answer any queries regarding the instrument.