**Pension Fund Committee**

**3 March 2016**

# Local Government Pension Scheme Investment Regulations

## Don McLure, Corporate Director Resources

### Purpose of Report

1. To update Members on the Pension Fund's response to the Government's consultation on the revocation and replacement of the Local Government Pension Scheme (Investment and Management of Funds) Regulations 2009.

### Background

2. The 2009 Investment Regulations detail the ways that the administering authorities for Local Government Pension Scheme (LGPS) funds must manage and invest those funds. The regulations are detailed and prescriptive, for example setting out how and under what terms investment managers should be appointed and their performance monitored, as well as listing types of permissible investments and limits on what proportions of a fund can be allocated to particular assets or asset classes.

3. The Government's consultation document sets out proposals to revoke and replace the 2009 Investment Regulations with the draft Local Government Pension Scheme (Investment and Management of Funds) Regulations 2016 (the 2016 Investment Regulations).

4. A report was presented to the Pension Fund Committee in December 2015 detailing this consultation.

5. At this meeting, the Pension Fund Committee gave its agreement to the Corporate Director Resources responding to the consultation, after consulting with the Chairman and Vice Chairman and after taking advice from the Fund's investment advisers.

### Consultation response

6. The response of Durham County Council Pension Fund was submitted by the Corporate Director Resources, after consulting with the Chairman and Vice Chairman, before the deadline of 19 February 2016. It is attached as Appendix 1 for your information.

## Recommendation

7. Members are asked to note the contents of the response to Government on the revocation and replacement of the Local Government Pension Scheme (Investment and Management of Funds) Regulations 2009.

## Background Papers

(a) Pension Fund Committee – 15 December 2015 – The Local Government Pension Scheme Investment Regulations.

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**Appendix 1: Consultation Response**

# Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009

Submission by: Durham County Council as Administering Authority for Durham County Council Pension Fund

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Durham County Council (DCC) welcomes the opportunity to respond to the consultation 'Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009'.

Our response provides answers to the questions raised alongside additional comments where appropriate.

## Proposal 1: Deregulating and adopting a local approach to investment

***Q1: Does the proposed deregulation achieve the intended policy aim of removing any unnecessary regulation while still ensuring that authorities' investments are made prudently and having taken advice?***

The proposed deregulation appears to achieve the intended policy objectives.

The proposed Investment Strategy Statement appears to have similar contents to those of the existing Statement of Investment Principles. There is an argument that the timescale for reviewing the Investment Strategy Statement should be consistent with the review of the Funding Strategy Statement in order that the two documents can be aligned and take into account the latest actuarial valuation.

Section 3.8 of the consultation document highlights that guidance on how a Fund's policies on environmental, social, and corporate governance issues are taken into account should reflect UK foreign policy and related issues will be issued prior to the new regulations taking effect. It is difficult to make any comments on this section as the guidance has yet to be issued, however we would like to stress that pension funds make long term investments in order to maximise returns for its investors whereas UK foreign policy can change significantly over the short term.

***Q2: Are there any specific issues that should be reinstated? Please explain why.***

No, we do not believe there are any specific issues that should be reinstated.

***Q3: Is six months the appropriate period for the transitional arrangements to remain in place?***

The proposed timeframe, to publish the Investment Strategy Statement within 6 months after the regulations come into force (i.e. by 1 October 2016), would be extremely challenging and will put a strain on limited staff resource. We suggest a period of between 9 to 12 months would be more practicable.

During this 6 month period staff will be busy with the production of their Pension Fund Accounts and Annual Report, developing their submission on pooling to meet the deadline of 15 July 2016, whilst compiling information for the triennial valuation.

***Q4: Should the regulation be explicit that derivatives should only be used as a risk management tool? Are there any other circumstances in which the use of derivatives would be appropriate?***

In addition to being a risk management tool, derivatives could also be used for efficient portfolio management purposes.

Being prescriptive in terms of the ways in which derivatives should be used would not be consistent with the general relaxation of the regulatory framework for Fund investments.

**Proposal 2: Introducing a safeguard – Secretary of State power of intervention**

***Q5: Are there any other sources of evidence that the Secretary of State might draw on to establish whether an intervention is required?***

The proposed power of intervention provides the Secretary of State with wide-ranging powers to intervene in the operation of an individual fund. Therefore, it is imperative that when considering an intervention the Secretary of State considers all available evidence before deciding to intervene and should only do so as a last resort.

The Secretary of State would have to ensure consistency of application across different funds, in order to avoid discrimination.

***Q6: Does the intervention allow authorities sufficient scope and time to present evidence in favour of their existing arrangements when either determining an intervention in the first place, or reviewing whether one should remain in place?***

As there are no timescales laid down in the draft regulations it is impossible to comment as to whether authorities have sufficient time to present evidence. However, it should be reiterated that the regulations should ensure that authorities have sufficient time to consider the evidence presented by the Secretary of State as well as to present its own evidence to support a counter argument.

***Q7: Does the proposed approach allow the Secretary of State sufficient flexibility to ensure that he is able to introduce a proportionate intervention?***

As there is very little detail in the regulations and associated consultation document it would appear that the Secretary of State has sufficient flexibility to ensure he is able to introduce a proportionate intervention.

Whilst it is appreciated that it is the intention that the power to intervene is deliberately broad so that it can be applied in a wide range of circumstances there is an argument that the power is too broad. A detailed guidance document should be produced to provide examples of the circumstances under which there is likely to be intervention. This guidance document would need to be far more extensive than the small number of examples given in the consultation document. Interventions should only be considered in extreme circumstances.

***Q8: Do the proposals meet the objective of the policy, which are to allow the Secretary of State to make a proportionate intervention in the investment function of an administering authority if it has not had regard to best practice, guidance or regulation?***

It is appreciated that the Secretary of State requires some form of tool to prevent an adverse impact from the proposed deregulation and to ensure that all funds participate in the requirement to pool assets. However, the circumstances under which this power of intervention would be used need to be further communicated to ensure that it is only being used when an authority materially departs from best practice, guidance or regulation and cannot provide an adequate justification for this action.

Section 4.9 of the consultation document states that all costs relating to an intervention will be met by the pension fund assets however the nature and cause of those costs should determine who ought to bear the costs.

Don McLure
Director Corporate Resources

17 February 2016