KEY PROPOSALS

Amendments to the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 1998

1. Separate bank account for the pension fund

The intention of this proposal is to improve the transparency of cash transactions between pension funds and general local authority accounts. Some administering authorities may already have a separate bank account but the amending regulations allow sufficient lead-in time to enable authorities to introduce new arrangements without any detriment to their investment strategies if that would be helpful. In addition to any general comments about this proposal, consultees are therefore also invited to comment on what would be a suitable and practical lead-in time before any change took effect.

2. Temporary borrowing power

It is proposed that a fund administering authority should have an explicit, but limited, power to borrow for the purposes of its pension fund. Borrowing in order to invest on behalf of the fund would not be allowed.

It is understood that there can be occasions where limited short-term borrowing does, unexpectedly, prove to be necessary for cash flow purposes - for instance as a part of transition management when the allocation of the fund's assets is being changed, or to ensure that all scheme benefit payments can be made on time. The pension fund needs to have identifiable known income it will receive shortly, with which repayment of the amount borrowed can be funded. The cost of the relevant loan repayments, and any interest payable, would be chargeable to the pension fund.

3. Statement of Investment Principles (SIP) : stock lending

It is proposed to extend the existing regulation on this subject to require an authority's statement of investment principles (SIP) to include information about its policy on the lending of stocks or other securities from its LGPS pension fund.

4. Stocklending – References to COLL -

Definition of "investment" – We would intend, in common with CLG, to update references to the relevant Financial Services Authority Sourcebook, now called COLL. They adapt COLL chapter 5.4 to the LGPS context, by making the administering authority responsible for compliance with the rules and guidance specified. The full contents of COLL 5.4 can be seen at http://fsahandbook.info/FSA/html/handbook/COLL/5/4

We would agree with the CLG view that the Regulations don't need to include a reference to COLL 5.4.8G. It is only guidance, and the overall provisions of the LGPS investment regulations cover relevant points already. That approach can be reviewed, however, if consultees consider that a reference is necessary. Were a reference to 5.4.8G to be added, it would have to include appropriate modifications - paragraphs 1 and 2(b)(ii) of COLL 5.4.8G would therefore not apply.

Consultees should note, and may have comments regarding, ways in which COLL chapter 5.4 is different from the equivalent section of the previous Sourcebook. Namely:

- Counterparties may now include certain USA broker-dealers and banks – see 5.4.4(1)(b) (iii) and (iv). We are minded, as are CLG, to provide a modification in the regulations of the new investment regulations, so that COLL 5.4.4(1)(b) (iii) and (iv) would not in fact apply to LGPS Funds.
- The difference in arrangements for stock lending transactions made through the Euroclear Programme are mentioned at 5.4.4(3)
- (Although as explained above this is unlikely to be relevant, 5.4.8(2) has guidance on how cash collateral can be reinvested.)

These changes were explained in an FSA Quarterly Consultation which can be found on their website - FSA 06/18, (No.10) October 2006, paragraphs 6.28 to 6.41.

5. The SIP and risk

An authority's Funding Strategy Statement will already provide some related information on investment strategy and managing financial risks. It is proposed to extend the existing requirement for an administering authority's statement of investment principles to cover its policy on risk, by adding the words "including the ways in which risks are to be measured and managed". The amendment reflects a similar requirement on private sector pension schemes.

6. Reference to overriding regulations concerning employer-related investments - regulation 13(1)

There is currently no reference to overriding regulations in the body of the LGPS investment regulations.

To clarify the situation it is intended that the main regulations will contain a reference to the relevant provisions of the Occupational Pension Scheme (Investment) Regulations 2005 (SI 2005 / 3378 ("OPSIR")

Further information about OPSIR is at **Annex B**. The full text can be seen at http://www.opsi.gov.uk/legislation/about_legislation.htm Use the advanced search, or follow the links from the home page to Legislation – Original – UK Statutory Instruments SIs – Year 2005 – No. 3378.

7. Use of Fund Money by the Administering Authority - Revocation of existing regulations 3(4) and 12

A provision of this kind has featured in the relevant Superannuation Act or scheme regulations since 1937 (with changes to details as time went on), and is subject to the prudential requirements and limits in the current regulations as a whole.

Although it is perhaps arguable that such use represents a safe investment, with the daily interest rate payable being prescribed, after many changes over the years in the wider pensions world it has come to be seen by some commentators as being out of step to allow administering authorities to use fund money in this way. There is no obvious reason why the administering authority should be able to do so when other participating employers cannot. CLG has therefore concluded that when the 1998 regulations are revoked, existing regulations 3(4) and 12 will not be replicated in the new provisions.

A transitional provision is proposed at draft **regulation 16**. This is only intended to be used where appropriate and to enable such arrangements to be unwound in an orderly manner without detriment to the fund.

Proposed amendment to the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008

8. Extract from the English version of the LGPS Administration Regulations for illustrative purposes only

“34 Pension fund annual report

(1) An administering authority must, in relation to each year beginning on 1st April 2008 and each subsequent year, prepare a document ("the pension fund annual report") which contains:

(a) a report about the management and financial performance during the year of each of the pension funds maintained by the authority;

(b) a report explaining the authority's investment policy for each of those funds and reviewing the performance during the year of the investments of each fund;

(c) a report of the arrangements made during the year for the administration of each of those funds;

(d) for each of those funds, a statement by the actuary who carried out the most recent valuation of the assets and liabilities of the fund in accordance with regulation 36 (actuarial valuations and certificates), of the level of funding disclosed by that valuation;

(e) the current version of the statement under regulation 31 (governance compliance statement);

(f) for each of those funds, the fund account and net asset statement with supporting notes and disclosures prepared in accordance with proper practices;

(g) an annual report dealing with:

(i) the extent to which the authority and the employing authorities in relation to which it is the administering authority have achieved any levels of performance set out in the pension administration strategy in accordance with regulation 65(2)(b), and

(ii) such other matters arising from its pension administration strategy as it considers appropriate;

(h) the current version of the statement referred to in regulation 35 (funding strategy statement);

(i) the current version of the statement under regulation 9A of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (statement of investment principles);
(j) the current version of the statement under regulation 67 (statements of policy concerning communications with members and employing authorities); and

(k) any other material which the authority considers appropriate.

(2) The authority must publish the pension fund annual report on or before 1st December following the year end.

(3) In preparing and publishing the pension fund annual report, the authority must have regard to guidance given by the Secretary of State.”