



NEWSLETTER 79

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Scotland for information only

**Department for Communities and Local Government (DCLG)
Local Government Pension Scheme Consultation (LGPS)
Draft Investment Regulations**

The DCLG is consulting over a new set of Investment Regulations for the LGPS.

This campaign news informs regions and branches of the consultation. Branches will be supplied shortly with a standardised response and will be asked to take part in a campaign for real change in the LGPS governance and investment process.

Branches may wish to respond as well if you do so please forward a copy to Colin Meech at c.meech@unison.co.uk.

Your comments should be sent by 3 April 2009 to Margaret Dunleavy, Workforce Pay and Pensions Division, Department for Communities and Local Government, Zone 5/F8, Eland House, 123 Victoria Street, London, SW1E 6DE.

Electronic responses can be sent to margaret.dunleavy@communities.gsi.gov.uk

Background

UNISON has been pressing the DCLG to bring the LGPS into line with European and UK law. Principally:

- The EU Directive – Institutions for Occupational Retirement Provision 2003 (or IORP)

- And UK legislation – the Occupational Pension Scheme Investment Regulations 2007

In summary, the above legislation requires the following:

1. **Legal separation of pension schemes from their sponsoring employer**
2. **Investments to be made in the best interests of scheme members, and in their sole interests should a conflict of interest arise**
3. **No borrowing by the employer from the pension fund**
4. **No investments by the pension fund in the sponsoring employer of more than 5%**

Currently, the LGPS falls outside these requirements, and for two years, UNISON has been pressing DCLG to make the LGPS compliant with the law.

However, the proposed new Investment Regulations, while addressing items 3 and 4 above, and requiring separate bank accounts for pension assets, fail yet again to remedy the more serious items 1 and 2, i.e. those regarding legal separation and the requirement to ensure that investments are made in the interest of scheme members, and scheme members alone in the case of a conflict of interest.

UNISON therefore believes that the new consultation represents only limited progress in bringing the LGPS into conformity with the Directive and UK legislation, and as such to be wholly unsatisfactory. The national union will be making representations to Hazel Blears, the Secretary of State for DCLG, presenting the legal and moral case for full and effective reform.

To press this case, additional actions are in hand, including:

- The commissioning of a legal appraisal of the new DCLG proposals
- The drafting of a UNISON response
- A National Seminar to be held on the 26th March
- Campaign proposals, to be circulated shortly

DCLG Consultation

A copy of the proposals are attached to this bulletin.

Listed below are the key consultation proposals, their explanation by DCLG, and some UNISON comments:

Separate bank accounts for LGPS pension funds - regulation 6

DCLG: *“The intention of this amendment is to improve the transparency of cash transactions between pension funds and general local authority accounts, and follows long-standing Audit Commission best practice recommendations...”*

UNISON Comment: This is a welcome proposal, but the new bank accounts will still belong to the council and not the pension fund. The pension fund will still not be legally separated as required under Article 8 of the EU Directive.

Temporary borrowing power- regulation 15

DCLG: *“Regulation 15 proposes 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...”*

Statement of Investment Principles (SIP): stock (share) lending - regulation 11(2)(h)

DCLG: *“Draft regulation 11(2)(h) extends 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...”*

UNISON Comment: Stock (share) lending is a controversial issue, because the borrowers of the shares often use them to drive down the value of companies in order to make a profit. This is often referred to as ‘shorting’, the government suspended this during the early days of the crisis in the banking sector.

The SIP and risk - regulation 11(2)(c)

DCLG: *“An authority’s Funding Strategy Statement will already provide some related information on investment strategy and managing financial risks. Draft regulation 11(2)(c) proposes 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.”*

UNISON Comment: This is insufficient. The proposal is related to Article 18 of the EU Directive, which is far more explicit in the requirement to invest mainly on regulated markets and keep alternative investments such as derivatives, the investment products known as ‘toxic assets’, at a minimum.

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

DCLG: *“The Explanatory Note to the existing regulations does mention that overriding regulations exist, the latest version being the Occupational Pension Scheme (Investment) Regulations 2005, SI 2005/3378 (“OPSIR”). But there is currently no reference to these in the body of the LGPS investment regulations...”*

UNISON Comment: This relates directly to the EU Directive Article 18 requirement to limit investment in the sponsoring employer to 5%. The ‘OPSIR’ regulations are the Department for Work and Pensions (DWP) enactment of Article 18.

Use of Fund Money by the Administering Authority - Revocation of existing regulations 3(4) and 12 – (This is the power to borrow by Administration Authorities from their pension scheme – our emphasis)

DCLG: *“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... 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.”*

UNISON Comment: This relates directly to the EU Directive Article 18 requirement not to allow employers to borrow from their pension schemes. The ‘OPSIR’ regulations are the DWP enactment of Article 18 and were first put on the statute in 2005, they were amended in 2007 to include the LGPS.

DCLG also proposes “other future developments”, including:

Conflicts of Interest

DCLG: *“The Pensions Regulator issued guidance for trust-based occupational schemes in 2008 as part of its Trustee Training Toolkit. (<http://www.thepensionsregulator.gov.uk/trustees/trusteeKnowledge/tku-02.aspx>.) ...*

“...Following the well-established tradition of adopting in the LGPS useful features of the regime for private sector occupational schemes, we intend to come forward in 2009 with scheme-specific best practice guidance to identify and manage potential conflicts of interest. Scheme interests will be consulted in the usual way before the guidance is issued. “

UNISON Comment: This is unacceptable, pension schemes have a duty to invest in the best interests of scheme members, no such provision exists in the LGPS, and in a conflict of interest they must favour scheme members. This is a

requirement of the EU Directive Article 18. It is totally unacceptable for the DCLG to simply issue guidance, they must legislate.

Other Issues - duty of care, governance

DCLG: *“Regulation 4 of The Occupational Pension Schemes (Investment) Regulations 2005, which applies only to private sector schemes, imposes the following requirements:*

“Investment by trustees”

“4.—(1) The trustees of a trust scheme must exercise their powers of investment, and any fund manager to whom any discretion has been delegated under section 34 of the 1995 Act(a) (power of investment and delegation) must exercise the discretion, in accordance with the following provisions of this regulation.

“(2)....

“(3) The powers of investment, or the discretion, must be exercised in a manner calculated to ensure the security, quality, liquidity and profitability of the portfolio as a whole.” [UNISON Comment: This is taken straight from Article 18]

“The provision usefully summarises the fiduciary duty of private sector pension fund trustees, and the investment outcomes which the prudential investment provisions of such regulations would be seeking to achieve.

“More recently, the CIPFA Pensions Panel Working Group’s report on its 2008 review of the LGPS investment regulations proposes, amongst other things, the following definition of “investments”

“The assets of the pension fund must be invested in such a way as to ensure the security, quality, liquidity and profitability of the portfolio as a whole and, in doing so, take the appropriate market, risk and investment advice. In the event of a potential conflict of stakeholder interests, investments must be made in the sole financial interests of the fund.

“CLG has tended to take action to ensure that the LGPS reflects private sector best practice and sustains its position as an exemplar occupational scheme. On this basis, consultees are invited to consider whether a provision of this kind is desirable or necessary to clarify the duty of care owed by those responsible for investment decisions within the LGPS...

“...Other developments within the general area of governance are expected to be considered during 2009, once CLG has had the opportunity to analyse the first

governance compliance statements prepared by administering authorities in accordance with the relevant statutory guidance.”

UNISON Comment: This is a very misleading set of statements, the requirement for trustees is to invest in the best interests of scheme members and not in the ‘financial interests of the funds’. Pension funds have no legal personality. It is ironic that DCLG refuses to acknowledge that the same requirement and duty falls on the LGPS. Furthermore if the DCLG has ‘tended to take action to ensure that the LGPS reflects private sector best practice’ why is there no statutory right for scheme members to have member-nominated representatives in the LGPS?