

A Brief Guide to the

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# Local Government Pension Scheme



# LGPS Basics

The LGPS is a defined-benefit occupational pension scheme set up by government regulations.

This scheme is open to local government employees and public service employers like charities. Benefits, which are set nationally, are very secure, because they're written in statute.

The LGPS is a nationwide scheme made up of many standalone funds, which are usually administered by local authorities. Separate regulations for administration, governance and investments apply in England & Wales, Scotland and Northern Ireland. But the scheme is broadly similar in each country or province.

## Key LGPS Facts: England and Wales

- Made up of 85 regional funds
- Around 6.3 million members
- Total fund assets: £364 billion
- Total expenditure on benefits of £14.4 billion pa

Source: DLUHC LGPS Funds: England and Wales statistical release 2021/22

## Key LGPS Facts: Scotland

- Made up of 11 regional funds
- Over 0.6 million members
- Total fund assets: more than £57 billion
- Total expenditure on benefits of £1.5 billion pa

Source: Scottish Scheme Advisory Report 2020/21

Since 1 April 2014, the LGPS in England and Wales (2015 for the other regions) has been a Career Average Revalued Earnings (CARE) scheme. That means pensions accrue each year based on members' earnings over their career.

The scheme is also 'funded', which means it's built up from employee and employer contributions, investment income and growth to meet future benefit payments. Most other public service schemes are unfunded or pay-as-you-go.

# Pooling LGPS Investments

- Every fund in England and Wales invests a proportion of its assets through one of eight investment pools. The UK government's pooling policy is under review, but the guidance expected later in 2023 is expected to promote further pooling.
- Each administering authority (usually through the pension committee) sets its own objectives, beliefs and strategic asset allocation, as well as setting the fund's policy on ESG matters.
- The responsibility for choosing investment managers sits largely with the pool, depending on the type of pool structure.
- The pension committee must monitor its own fund's arrangements to ensure the pool is performing as required.
- At the time of writing, there are no requirements for pooling in Scotland.

## Resources and training

To help pension committees and boards achieve the right level of knowledge in all these areas, Hymans Robertson has created an online learning tool – the LGPS Online Learning Academy (LOLA). This innovative digital learning plan mirrors the topics of the National Knowledge Assessment, and covers all key areas needed to successfully manage the running of a fund, including:

- Committee Role and Pensions Legislation
- Pensions Governance
- Pensions Administration
- Pensions Accounting and Audit Standards
- Procurement and Relationship Management
- Investment Performance and Risk Management
- Financial Markets and Product Knowledge
- Actuarial methods, Standards and Practices

This cost-effective training provides LGPS funds with the key information required and allows them to record and track all training progress for committees, boards and officers. Funds will receive regular progress reports, allowing them to easily evidence their members' knowledge and skills. Funds can also record all training that has taken place on the platform.

# Who's who in the LGPS

Your own officers will be able to provide you with details of the people involved in your fund, and your governance arrangements. But it's likely that you'll deal with or hear about most of the following groups or individuals.

## The Administering Authority

Usually a council – it has the responsibility of managing all aspects of the fund.

## Advisers

These may include auditors; lawyers; investment managers; actuaries; investment, governance and benefit consultants; and custodians.

## Department for Levelling Up, Housing and Communities (DLUHC)

The central government department responsible for strategic management and policymaking for the LGPS in England and Wales. The Scottish equivalent is the Scottish Public Pensions Agency, while the Northern Irish version is the Department of the Environment.

## Officers

Employees of the administering authority, who carry out the fund's administration and management for the elected members.

## Local Pension Board

Member and employer representatives, who assist the administering authority in the scheme's governance. Unlike the pension committee, local pension boards have no direct delegated decision-making responsibilities.

## The Pension Committee

Usually elected members from the council. Most committees have some delegated authority from the administering authority, but some are advisory only. Normally, the committee has overall responsibility for the fund, like trustees in private sector pension schemes.

## Pools (England and Wales only)

LGPS funds are grouped into eight pools. Each LGPS fund in England and Wales is a member of one of these pools, which were created to reduce costs, improve investment oversight and provide access to alternative asset classes.

## Scheme Advisory Board (SAB)

A national body that works with government and other stakeholders to encourage best practice, increase transparency and coordinate technical and standards issues. There are separate SABs for England & Wales, Scotland and Northern Ireland.

## Scheme Employers

Local authorities, public service organisations and private contractors providing an outsourced service.

## Scheme Manager

The body that runs a public sector pension scheme. Each administering authority is a scheme manager in the LGPS.

## Scheme Members

Active, deferred or pensioner members of the LGPS.

## The Pensions Regulator (TPR)

TPR regulates the governance and administration of pension schemes and has published a code of practice for public service schemes.

Other groups you'll come across include:

- LGA (Local Government Association), who provide guidance on the technical aspects of the LGPS
- CIPFA (Chartered Institute of Public Finance and Accountancy), who support reporting and accountancy aspects

# What are the pension committee's duties?

## Agreeing the fund's objectives and investment beliefs

- Monitoring the fund's progress against its objectives
- Using the beliefs to form the fund's investment strategy

## Deciding an appropriate investment strategy and structure for your fund

- Considering advice from your investment advisers and the fund's actuary
- Identifying and managing the fund's key risks
- Setting ESG-related policy matters, including climate change

## In relation to the management of your fund's assets

- Liaises with your pool on investment options (England and Wales)
- Selects new investment managers (Northern Ireland and Scotland)
- Monitors performance of decisions delegated to other parties (all)

## Dealing with your fund actuary

- Ensuring that you have an appropriate funding strategy for setting contributions
- Agreeing contribution rates at the triennial valuation
- Monitoring the funding level between valuations

## Ensuring all relevant documentation is in order

- Reviewing and updating the mandatory documents (including the annual report, funding strategy statement and governance compliance statement)
- Reviewing administering authority policies
- Approving your pension fund accounts

## Being responsible for risk management of the fund

Maintaining an up-to-date risk register

- Establishing appropriate policies to deal with the admission and departure of employers into or from the fund
- Ensuring smooth administration of the fund for members and employers
- Keeping an eye out for possible long-term risks, eg how your longevity experience is changing over time

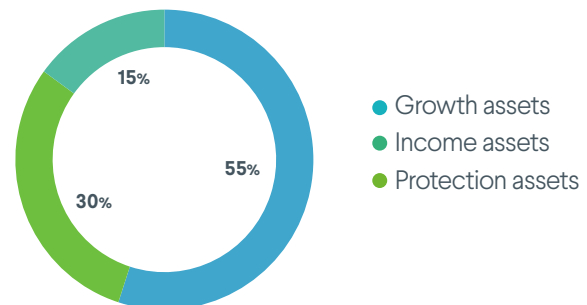
# Investment Decisions

The pension committee's main tasks include setting the fund's investment objectives, beliefs and strategy, as set out in the investment regulations.

Once the objectives and beliefs are established, attention turns to the fund's investment strategy. Funds will typically invest in:

- **Growth** assets, such as equities, which generally provide an above-inflation return over the long term.
- **Income** assets like property, infrastructure and other alternatives that provide diversification. These also typically generate above-inflation returns, with a high proportion as income, which can help to fund benefits payments.
- **Protection** assets like gilts and high-quality corporate bonds, which are usually held for funding stability and security.

A typical LGPS fund's asset allocation could look like this:



- A high allocation to return-seeking assets helps to keep pensions affordable, but also increases downside funding risk.
- A long-term approach, seeking return, is generally considered appropriate – hence the higher allocation to growth and income assets in the LGPS world relative to most private sector pension schemes.
- ESG-related aspects (including climate change) are increasingly important when making investment decisions.

## Types of asset classes

### Equities

Shares in companies, which can provide dividends and the prospect of capital gains. Equities are expected to deliver a higher long-term return than bonds.

### Bonds

These provide a regular income and are repaid in full at maturity. Gilts are bonds issued by the UK government, and corporates are issued by companies. Corporate bonds are perceived as being higher risk than gilts, so they pay a higher interest rate. Index-linked gilts provide income and maturity payments that increase (or decrease) in line with inflation.

### Property

Covers commercial and, increasingly, residential property. Due to the size of individual properties and the need for diversification, investment is often through pooled funds.

### Infrastructure

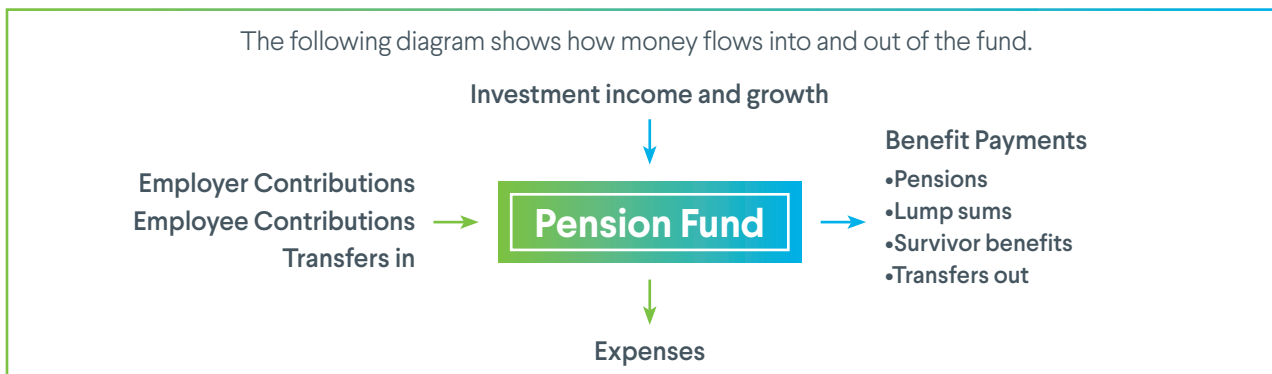
A highly diverse asset class comprising the facilities and essential services for the functioning of modern economies. Covers economic infrastructure like transportation networks, power generation/distribution and telecommunications, and social infrastructure such as schools and hospitals.

### Alternatives

Asset classes that add diversification by delivering returns in a different pattern from equities. Includes hedge funds, infrastructure and diversified growth funds (funds that invest in a range of different assets).

# The actuary's role

Your main objectives when running a pension fund are to ensure there are sufficient funds to pay for the benefits when they're due, and that contributions are paid at an appropriate level.



**Your fund actuary will perform regular actuarial valuations of the fund to:**

- Comply with legislation (valuations every three years are mandatory)
- Monitor the ongoing health of the fund and manage actuarial risks (ie do you have enough money to pay the pensions?)
- Recommend appropriate contribution rates for employers
- Monitor the actual experience of the fund against the assumptions made

To carry out the valuation, assumptions must be made about future experience. The most important decisions will concern the expected investment return, inflation (to determine pension and salary increases) and longevity assumptions. These feed into financial modelling to help decisions about funding strategies. At valuation time, your actuary will provide analysis and advice in determining these assumptions and setting funding strategies.

The Funding Strategy Statement documents how the fund will pay for benefits and the approach the actuary will use when setting employer contribution rates.

## Important definitions for valuation

### Funding strategies

These target full funding for each employer over an appropriate time horizon by balancing future employer contributions with future investment returns. The financial strength and risk profile of employers are key factors.

### Rates and Adjustments Certificate

A document required by the LGPS Regulations, which must be updated after each formal valuation. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the fund until the next valuation is completed.

### Primary contribution rate

The employer contribution rate required to pay for new benefits earned by staff, expressed as a percentage of pensionable pay.

### Secondary Contribution Rate

Any adjustment to the Primary Contribution Rate (such as additional contributions to repair any deficits), which can be expressed as a percentage of pensionable pay or as annual lump-sum amounts.

# LGPS boards

**All LGPS funds must have a local pension board to ensure that funds are governed in line with regulatory and best-practice requirements.**

The local pension board assists the scheme manager (the administering authority) in complying with:

- The scheme regulations
- Other governance and administration legislation
- Any TPR requirements
- Additional matters, if specified by scheme regulations

Boards must have an equal number of representatives from employers and scheme members. Other types of members – independent experts, for example – are allowed, but they won't have a vote.

The law requires local pension board members to have knowledge and understanding of relevant pensions laws, the LGPS and its documentation.

The pension committee's role usually involves decision-making, but members of pension boards should focus on the processes involved in running the fund.

For example, are policies and procedures up to date? Are the requirements of The Pensions Regulator being met? And is the fund following recognised best practice?

Also, separate Scheme Advisory Boards exist for England & Wales, Scotland and Northern Ireland. These encourage best practice, increase transparency and coordinate technical and standards issues.

## Knowledge and skills

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The CIPFA code of practice requires those charged with pension scheme governance to have access to the skills and knowledge for carrying out their role effectively.

Members of local pension boards also have a statutory requirement to have knowledge and understanding of the law relating to pensions and any other matters specified in the regulations.

Unlike local board members, there's no statutory requirement for decision-makers on a pension committee or panel to have a level of knowledge about pensions law or LGPS matters. However, to comply with MiFID II (Markets in Financial Instruments Directive II), fund committees must provide evidence of their knowledge and understanding to be classed as a 'professional client'.

CIPFA's Pensions Knowledge & Skills Framework (KSF) outlines the necessary skills for those responsible for pension financial management and decision-making.

Regulations and guidance on the English and Welsh SAB Good Governance Review is being prepared by DLUHC. It recommends that members of pension committees should be required to obtain the knowledge and understanding necessary to carry out their role effectively.

This isn't the same as being a pensions subject-matter expert: it's about having the skills to ask questions, seek advice and weigh up options.



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