

# preparing the annual report

Guidance for Local Government  
Pension Scheme Funds  
2018 Edition



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Consultation Draft

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Edited by Sarah Williams ([sarah@redlane.org.uk](mailto:sarah@redlane.org.uk))

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# Foreword

When it was introduced into the Local Government Pension Scheme (LGPS) regulations, the requirement to produce an annual report represented a major step forward. All LGPS funds now produce and publish an annual report, promoting awareness of the scheme and providing members and stakeholders with relevant information in an accessible and consistent manner.

A great deal has changed since the last edition of this Guidance was published in 2014. National asset pools, new legislation on investing, governance and benefits, and changes to year end reporting deadlines have brought new challenges for practitioners together with a continued focus on funding levels and investment management costs.

This updated statutory guidance has been fully revised to reflect the current regulatory framework, and to include specific reporting requirements to assist in the compilation of a scheme-wide annual report for England and Wales.



**Mike Ellsmore**  
**Chair, CIPFA Pensions Panel**

# Acknowledgements

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# Contents

<b>Background</b>	<b>1</b>
<b>Statutory basis and requirements</b>	<b>2</b>
<b>Status of this Guidance</b>	<b>4</b>
<b>Publication</b>	<b>5</b>
Manner of publication	5
Timing of publication	5
Authorisation	5
<b>The Guidance</b>	<b>7</b>
A: Overall Fund Management	7
B: Financial Performance	8
C: Investment policy and performance report	9
D: Scheme administration report	11
E: Actuarial report on funds	13
F: Governance	13
G: Fund Account, Net Assets Statement and Notes	15
H: National Asset Pools	15
I: Pensions Administration Strategy Report	18
J: Funding Strategy Statement	19
K: Investment Strategy/Statement of Investment Principles	19
L: Communications Policy Statement	20
M: Any other appropriate material	20
<b>Annex: LGPS Annual Report checklist</b> <i>[To be included following consultation process]</i>	

# Background

The purpose of this guidance is to assist administering authorities with the preparation and publication of the annual report required by:

- England and Wales - Regulation 57 of The Local Government Pension Scheme Regulations 2013;
- Scotland - Regulation 55 of The Local Government Pension Scheme (Scotland) Regulations 2018 (the Scotland Regulations).

Although there is no equivalent Regulation covering Northern Ireland, the organisation responsible for the administration of the LGPS in Northern Ireland does produce a similarly constructed annual report.

The annual report is a key communications channel between pension funds and their stakeholders, who range from individual members and employing bodies to employee representative bodies, government departments, analysts and commentators. In Scotland and Wales the annual report is now a standalone document with the pension fund accounts no longer contained in the administering authority's financial statements. Annual reports should therefore contain sufficient information to meet the demands of this diverse of readership and to be read and understood in isolation.

It is important to stress that this Guidance represents a general framework for reference purposes only and is not a template or example annual report. It identifies the topics that need to be covered but does not prescribe the format or level of detail required. To provide some overall context, pension fund annual reports published in 2016/17 varied from 60 to 326 pages long, with an average length of 150 pages, but there is no "recommended" or "correct" length or layout. Pension fund administering authorities are encouraged to adopt and develop their own house style depending on the preference of users.

The Guidance uses a combination of descriptive text, cross-references to other documents and worked examples to explain how each of the requirements can be achieved in practice, but these examples are for illustration only. Annex 1 contains a summary of the requirements for reference purposes.

CIPFA will continue to keep the content of this Guidance under review and it will be updated as necessary to reflect any subsequent legislative changes.

# Statutory basis and requirements

In England and Wales, the statutory basis for LGPS annual reports for periods beginning on or after 1 April 2014 is Regulation 57 of the Local Government Pension Scheme Regulations 2013, which is reproduced below:

## *Pension fund annual report*

57.—(1) *An administering authority must, in relation to each year beginning on 1st April 2014 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 62 (actuarial valuations and certificates), of the level of funding disclosed by that valuation;*
- (e) *the current version of the statement under regulation 55 (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 Scheme employers 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 their pension administration strategy as they consider appropriate;*
- (h) *the current version of the statement referred to in regulation 58 (funding strategy statement);*
- (i) *[From 1<sup>st</sup> April 2017, the current version of the Investment Strategy Statement as required by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016] (formerly the Statement of Investment Principles);*

(j) *the current version of the statement under regulation 61 (statements of policy concerning communications with members and Scheme employers); 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.*

In Scotland Regulation 55 of the LGPS (Scotland) Regulations 2018 mirrors the above requirements except that Scottish pension funds are required to published a statement of investment principles under the LGPS (Management and Investment of Funds) (Scotland) Regulations 2010 in place of an Investment Strategy.

# Status of this guidance

In England and Wales, the Ministry for Housing, Communities and Local Government has adopted this guidance as statutory guidance for the purposes of Regulation 57(3) in the 2013 Regulations.

In Scotland and Northern Ireland, this guidance is advisory only. However, CIPFA encourages those funds to adopt the guidance on a 'best practice' basis.

## MANNER OF PUBLICATION

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“Publish” in this context can mean production in hard copy of the whole document, or:

- publication by electronic means; for example, in full on the pension fund or administering authority’s website (provided that the document is presented as a whole)
- a summary report in hard copy, supported by a full report in electronic format on the pension fund or administering authority’s website.

In addition to the requirement to prepare and publish a pension fund annual report there are statutory requirements to publish separately many of the documents contained in the annual report, including the funding strategy statement, the investment strategy statement (in Scotland the statement of investment principles), the governance compliance statement, the communication policy (in England and Wales), etc.

## TIMING OF PUBLICATION

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Regulations require the annual report to be published on or before 1 December in England, Wales and Scotland. In Scotland and Wales, the pension fund annual report is a standalone publication containing the year-end statement of accounts, whereas in England the pension fund accounts are also published as part of the administering authority’s audited financial statements.

Administering authorities in England may therefore choose, for practical reasons, to align the publication of the annual report with that of the Council’s main accounts, for which the normal publication deadline is 31 July each year for 2017/18 onwards.

## AUTHORISATION

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Although not specifically required by legislation, the annual report should be formally reviewed by those charged with governance and signed by the chair of the pensions committee and the director of finance (or their equivalents).

This should not be confused with the separate process for the review and approval of the administering authority’s annual accounts, which is a legal requirement under the following:

- England – The Accounts and Audit Regulations 2015;
- Wales – The Accounts and Audit (Wales) Regulations 2014, as amended by The Accounts and Audit (Wales) (Amendment) Regulations 2018; and
- Scotland - The Local Authorities Accounts (Scotland) Regulations 2014 .

# The Guidance

## INTRODUCTION

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This guidance follows the structure of Regulation 57 (Regulation 55 in Scotland) with a section for each of the requirements listed.

## A: OVERALL FUND MANAGEMENT

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### Scheme management and advisers

The report should list the names and, where appropriate, contact details for:

- officers responsible for the fund
- the Asset Pooling arrangements and Operator
- investment managers used by the fund, including where applicable contact details for any elements of the fund which are managed internally
- the fund custodian
- AVC providers
- the fund actuary
- the fund legal advisors
- bankers to the fund
- the fund accountant/director of finance
- the fund auditor
- scheme administrators
- any independent advisers retained by the fund (eg for investment and governance).

### Risk management

The report should contain a commentary on the arrangements for the identification and management of risk which is consistent with disclosures regarding the use of financial instruments in the year-end accounts

The report should explain:

- how risk management is integrated within the governance structure;
- how risks are identified, managed and reviewed;
- a summary of the key risks and what actions are being taken to mitigate those risks;
- assurance provided by the work of Internal Audit;

- how investment risk is managed;
- risks relating to the investment pooling arrangements;
- the approach taken to managing third party risk such as late payment of contributions;
- how assurance is sought over third party operations, eg ISAE3402 (formerly AAF 01/06) and SSAE16 (formerly SAS70) reports.

The 2018 CIPFA publication “Managing Risk in the LGPS” provides more detail on the identification, management and reporting of risks.

Examples of risk management disclosures are provided below:

a) Pension Fund Risk Register

Risk area	Risk rating	Responsible officer	Mitigating actions
<b>ADMINISTRATION</b> 3rd parties undertaking administration work do not maintain accurate and up to date membership records		Director of People Services	Sample testing by Internal Audit of 1% of all files will enable accurate assessment of error rate and resources needed to clear administration backlog
<b>REGULATION</b> MiFID II restricts investment options and increases IM costs		City Treasurer	MIFID II training for all pension committee members and all staff involved in the opting up process
<b>INVESTMENT</b> Fund managers fail to achieve target returns		City Treasurer	Independent monitoring of fund manager performance against targets.  Fund manager performance is reviewed quarterly.

b) Controls assurance reports

Fund Manager	Type of Report	Assurance obtained	Reporting accountant
Bailie Gifford	ISAE 3402	Reasonable assurance	KPMG LLP
Hermes	ISAE 3402	Reasonable assurance	Deloitte LLP
Insight	ISAE 3402	Reasonable assurance	PwC LLP
LGIM	ISAE 3402	Reasonable assurance	PwC LLP
Longview	ISAE 3402	Reasonable assurance	Moore Stephens LLP
Majedie	ISAE 3402	Reasonable assurance	KPMG LLP
Standard Life	ISAE 3402	Reasonable assurance	PwC LLP
<b>Custodian</b>			
Northern Trust	ISAE 3402	Reasonable assurance	KPMG LLP

c) Internal audit testing



System identified frequency Tested this year assessment Benefit payments and lump sums	Annual testing	Yes	
Employee contributions	Annual testing	Yes	
Employer contributions	Annual testing	Yes	
Membership records	Annual testing	Yes	
Administration and Governance costs	Every 5 years	No	N/a
Investment management costs	Every 3 years	No	N/a

## B: FINANCIAL PERFORMANCE

This section of the report provides the opportunity for the fund to demonstrate to stakeholders the effectiveness of its financial stewardship. While the following section deals with the management of pension fund investments, this section looks at the management of other elements of pension fund income and expenditure and overall cash flows.

In line with the triennial valuation cycle, pension funds should disclose the three-year forecast of income and expenditure into and out of the fund (including administrative costs), in addition to an annual cashflow forecast.

This report should identify performance against budget and highlight and explain any significant variances. The budget should cover all operational expenses and income associated with the fund, identifying as a minimum:

- staff costs (both direct and internal recharges), premises, IT, supplies and services, costs of democracy and any other administration costs and miscellaneous income;
- benefits payable, transfers in and out, investment management and governance expenses;
- members' and employers' contributions;
- investment income;
- net inflows and outflows to the fund.

Funds may wish to include indicative forecasts of less controllable or predictable items such as transfer values and investment income forecasts or link investment income forecasts to investment strategies or market performance reports.

The annual report should contain details of fund assets as at the reporting date, analysed as follows:

	UK	Non-UK	Global	Total
	£m	£m	£m	£
Equities				
Bonds				
Property (direct holdings)				
Alternatives				
Cash and cash equivalents				
Other				
Total				

Note that in the above table:

- Alternatives' are taken to mean holdings in private equity, hedge funds, pooled property funds, infrastructure funds and derivatives.
- Other' denotes assets not falling into any other category, such as investments in vehicles where the underlying investments may comprise of assets of more than one type.
- 'Global' holdings are those that include an element of both overseas and UK listed assets.
- Investments in pooled funds should be allocated to categories based on the nature and domicile of the underlying assets.

The annual report should also include:

- In a valuation year, a brief commentary on the movement in assets and liabilities (or a cross-reference to where this can be found in the actuary's report).
- Employers' contributions as a %age of payroll;
- A list of contributing employers and the amount of contributions received from each organization during the year split between employees and employers)
- An analysis of amounts due to the fund from employers at the year-end, including:
  - an analysis of the timeliness of receipt of contributions (value and percentage received on or before the due date; aging of overdue contributions, etc)
  - whether the option to levy interest on overdue contributions has been exercised and, if so, on whom and how much.
- A budget v outturn report on the administrative costs of the fund during the year, including investment management expenses.
- A forecast v outturn report on the fund cash flows and asset values.
- a five-year analysis of pension overpayments, recoveries and any amounts written off, including the results of participation in National Fraud Initiative (NFI) exercises (data matches, overpayments identified, actions taken, etc). For those funds that do not

routinely provide this type of disclosure already, this will need to be built up over time and will demonstrate to stakeholders the effectiveness of overpayment identification and recovery.

## C: INVESTMENT POLICY AND PERFORMANCE REPORT

The investment policy and performance report is intended to demonstrate how the investment strategy has been put into practice during the year and how this links to the statement of investment principles.

The planned asset allocation should be stated along with the actual asset allocation for the beginning and end of the financial year in question, together with explanations for significant changes during the year. Asset allocations should be split by major asset classes in line with the categories employed in the financial statements.

Investment performance should then be disclosed for each asset class with each fund manager's performance disclosed against the benchmarks set for one year, three years and ten years.

The fund's responsible investment policies and any environmental, social and governance issues should be disclosed along with voting arrangements, and other initiatives such as engagement with companies and any collaborative ventures with other funds including progress towards asset pooling (England and Wales only –see also section H). The report should outline the fund's approach to the UK Stewardship Code and also:

- list any bodies of which the fund is member, subscriber or signatory, such as NAPF, LAPFF, UKSIF, UNPRI, etc
- record where and how voting rights have been exercised
- where a commitment to responsible investment is stated, what actions have been taken to pursue these aims
- what actions the fund has taken to demonstrate compliance with the Myners principles.

This section of the report should include details of investment administration and custodianship describing who looks after which part of the portfolio. It should also include a commentary on any matters relating to the implementation and application of the funding strategy statement during the reporting period, such as:

- the implementation of any contribution increases
- the management of admitted bodies
- any bonds or any other secured funding arrangements entered into.

The CIPFA publication "Accounting for Local Government Pension Scheme Management Expenses", published in 2016, recommends that this section of the annual report is also used to explain the total cost of the supply chain involved in managing the pension fund's investments, and the relationship between investment management costs, risk and investment return.

For example, costs incurred by sub-fund managers and other third parties under pooled fund, fund of fund or joint venture funding mandates will not be recorded as expenditure in the

pension fund's accounts because they are not the pension fund's responsibility to pay. Such costs do, however, impact on the overall performance of the fund as they reduce the value of investment income received. Being able to identify these hidden costs is a key step in decision making and in delivering effective and efficient pension fund management, and there is continued public interest in this "transparency agenda".

The aim should be to enable readers of the annual report to understand the effectiveness of the fund's investment management arrangements by reference to the returns and risks associated with the pension fund portfolio. Areas for consideration might include the costs and related returns from:

- Active v. Passive portfolios;
- Different asset classes including alternatives
- Pooled funds, layered funds and "fund of fund" arrangements
- Different fund managers.

This section of the report should also indicate how the pension fund is responding to the Scheme Advisory Board's Transparency Code, and publish any data provided by fund managers using the transparency code templates see

[Http://lgpsboard.org/index.php/structure-reform/cost-transparency](http://lgpsboard.org/index.php/structure-reform/cost-transparency) for further details

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## D: SCHEME ADMINISTRATION

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The scheme administration section of the annual report should cover the following areas:

- How the service is delivered;
- Summary of activity of the service in the year;
- Key performance data; and
- Other information such as customer satisfaction, communications and complaints.

### **How the service is delivered**

The section should include a description of the key areas of technology used by the fund and information sources such as websites, self-service portals, helpdesk facilities and workplace representatives.

The report should set out, for both scheme member and pension administration, a broad outline of the arrangements in place including:

- who undertakes the activity
- how they can best be contacted
- Arrangements in place for ensuring accuracy and confidentiality of personal data.

Where administration functions have been outsourced, provider details should be included together with an outline of steps taken by the pension fund to ensure the effective and efficient delivery of these operations.

The report should contain an outline of the fund's internal dispute resolution procedure including an analysis of new dispute cases raised during the reporting period and their resolutions (where applicable), and contact details for the Pensions Advisory Service and the Pensions Ombudsman.

### **Summary of activity**

This section should outline the work undertaken by the administration section of the Fund during the year, including:

- The major pieces of work/projects undertaken by the Fund (e.g. Guaranteed Minimum Pensions Reconciliation exercises), summarising the actions taken during the year, progress achieved and outline next steps for the following year, where applicable.
- Outline any technology or pensions administration systems developments which have taken place during the year, including details of the impact that they have/will have. For instance, moving from annual to monthly reporting systems in order to improve the timeliness and accuracy of data received from Employers.
- Action to improve Data Quality, outlining:

- The steps being undertaken to audit data annually
- The scores reported to The Pensions Regulator (TPR) in the TPR Scheme Return on Common and Scheme Specific Data
- Further steps the Fund is taking in order to improve the quality of data held by the Fund

### Key performance data

This section of the annual report should include:

- Key administrative performance information used by the Fund as well as performance against regulatory requirements, such as:
  - the number and trend of the top 10 case types processed by the Fund in key casework areas during the year with comparative data for the previous year as a minimum;
  - the percentage of tasks completed on time against regulatory deadlines and key performance indicators
  - speed and accuracy of transactional processing
  - satisfaction levels for employers and members
  - numbers of complaints and the numbers of complaints as a percentage of workload.
- Financial indicators of administrative efficiency, including:
  - unit costs per member including and excluding investment management expenses
  - benchmarking of unit costs against appropriate comparators (either from a formal benchmarking process or an informal peer comparison).
- Key staffing indicators, such as:
  - staff numbers expressed as full-time equivalents and the 5 year trend
  - staff to fund-member ratios and the 5 year trend
  - average cases per member of staff

A working party set up by CIPFA during 2018 to consider scheme administration is aiming to develop a process whereby the above data can be captured on a consistent basis and shared between funds – for further details please contact [neil.sellstrom@cipfa.org.uk](mailto:neil.sellstrom@cipfa.org.uk).

The group has recommended that as a first step all LGPS pension funds collect and publish the following information:

**Table 1 – key performance information**

Process	No. of cases commenced in year	No. of cases completed in year	No. cases outstanding at year-end	% completed in year	Average cases per fte staff member
<b>Deaths</b> – initial letter acknowledging death of member					
<b>Deaths</b> – letter notifying amount of dependants pension					
<b>Retirements</b> – letter notifying estimate of retirement benefits					
<b>Retirements</b> – letter notifying actual retirement benefits					
<b>Retirements</b> – process and pay pension benefits on time					
<b>Deferment</b> – calculate and notify deferred benefits					
<b>Transfers in/out</b> – letter detailing transfer quote					
<b>Refund</b> – Process and pay a refund					
<b>Divorce quote</b> – letter detailing cash equivalent value and other benefits					
<b>Divorce settlement</b> – letter detailing implementation of pension sharing order					
<b>Joiners</b> – notification of date of enrolment					

**Table 2 – key performance indicators**

Process	KPI	%	Legal requirement	%
<b>Deaths</b> – initial letter acknowledging death of member	5 days		2 months	
<b>Deaths</b> – letter notifying amount of dependants pension	10 days		2 months	
<b>Retirements</b> – letter notifying estimate of retirement benefits	15 days		2 months	



<b>Retirements</b> – letter notifying actual retirement benefits	15 days		2 months	
<b>Retirements</b> – process and pay pension benefits on time	15 days		2 months	
<b>Deferment</b> – calculate and notify deferred benefits	30 days		2 months	
<b>Transfers in/out</b> – letter detailing transfer quote	10 days		2 months	
<b>Refund</b> – Process and pay a refund	10 days		2 months	
<b>Divorce quote</b> – letter detailing cash equivalent value and other benefits	45 days		3 months	
<b>Divorce settlement</b> – letter detailing implementation of pension sharing order	15 days		3 months	
<b>Joiners</b> – notification of date of enrolment	40 days		2 months	

**Table 3 – unit cost per member**

Process	2013/14	2014/15	2015/16	2016/17	2017/18
<b>Investment Management Expenses</b>					
Total cost (£'000)					
Total membership (Nos)					
Cost per member (£)					
<b>Administration Costs</b>					
Total cost (£'000)					
Total membership (Nos)					
Cost per member (£)					
<b>Oversight and Governance Costs</b>					
Total cost (£'000)					
Total membership (Nos)					
Cost per member (£)					
<b>Total cost per member (£)</b>					

The administration section of the annual report should also contain:

- A list of contributing employers and the amount of contributions received from each during the year (split by employers and employees).
- A five-year analysis of the fund's membership data (active, deferred and pensioner and

undecided leavers (i.e. those members who are no longer accruing service and to whom a refund of contributions or transfer out may be due)

- Details of new pensioners each year analysed by ill-health, early and normal retirement.
- A commentary on how employer discretions have been exercised in the reporting period
- A summary of the number of employers in the fund analysed by scheduled bodies and admitted bodies which are active (with active members) and ceased (no active members but with some outstanding liabilities). This data should be shown in tabular format as follows:

	Active	Ceased	Total
Scheduled body	xx	xx	xxx
Admitted body	xx	xx	xxx
Total	xxx	xxx	xxx

Finally, this section of the report should set out details of any policies or guidance produced for employing bodies such as:

- Pensions advice for employers undertaking TUPE staff transfers
- Admissions policy for new admitted bodies

## E: ACTUARIAL REPORT ON FUNDS

All LGPS funds are required to commission a revaluation of all of their funds on a specified date every three years.

Regulation 57 in England Wales (Regulation 55 in Scotland) requires the annual report to include:

- a statement by the actuary on the overall funding level as reported at the last triennial valuation;
- either a summary of the last triennial valuation report or details of where the full version of the actuarial report can be obtained;
- the results of any interim valuation;
- key variables such as longevity experience, ill health retirements and use of discretionary powers which are impacting on the fund's solvency.

## F: GOVERNANCE

Regulation 55 of the LGPS Regulations 2013 (Regulation 53 in Scotland) prescribes the content of the Governance Compliance Statement which is required to be included in this section of the annual report. The statement should outline of the overall governance structure of the fund and explain:

- the respective roles and responsibilities of the pensions panel/pensions committee, the local pensions board and any related sub-committees or advisory boards. each element within the structure (including whether each one is executive or advisory)
- policies and processes for managing conflicts of interest;
- membership of each panel, board, committee or sub-committee with a matrix showing each member’s voting rights, record of attendance at meetings and details of training received during the reporting period.

An illustrative example of such a matrix is shown below.

Annual reports should also include some form of commentary to illustrate how governance works in everyday terms for the general reader. This might include, for example:

- Details of codes of conduct and how these operate in practice
- How the CIPFA Knowledge and Skills Framework has been applied, details of training offered and take-up (training is mandatory for local pension board members though not for a pensions committee)
- How the fund meets the requirements of the CIPFA/SOLACE “Good Governance Framework”

	Chair	Vice Chair	AB Council Member	AB Council Member	CD Council Member	CD Council Member	EF Council Member	Other employer	Employee Representative
Committees (3 hours)									
Special Committee April 2017	✓	✓	✓	✓	✓	✓	✓	✓	✓
May 2017	✓	✓	✓	✓	✓		✓	✓	✓
July 2017	✓	✓	✓	✓	✓	✓	✓	✓	✓
Governance (1 day)	✓	✓	✓	✓	✓	✓	✓		✓
Funding & Actuarial (1 day)		✓	✓	✓	✓	✓	✓	✓	✓
Investments (1 day)		✓	✓	✓			✓	✓	✓
Accounting		✓		✓	✓		✓		✓

- Information relating to the oversight committee of the asset pool.

## G: FUND ACCOUNT, NET ASSETS STATEMENT AND NOTES

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The annual report must include a fund account and net asset statement with supporting notes and disclosures prepared in accordance with proper practices for each of its pension funds. The financial statements are to be drawn up in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom issued by CIPFA/LASAAC (which sets out proper practices to be followed).

Currently in England, the primary financial reporting of the pension fund is through the annual statement of accounts for the pension fund administering authority, therefore the pension fund accounts in the annual report should match those in the annual statement of accounts.

In Scotland and Wales, the annual report is the primary reporting route for the pension fund annual accounts.

The external auditor's opinion on the fund's statement of accounts should also be included in the annual report. For Welsh and Scottish pension funds this will be a standalone audit opinion, whereas in England it is more likely to be a "consistent with" opinion referring back to the certificate given on the administering authority's main statement of accounts.

## H: NATIONAL ASSET POOLS

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In 2015 MHCLG issued LGPS: Investment Reform Criteria and Guidance which set out how the Government expected Funds to establish asset pools to deliver:

- benefits of scale;
- strong governance and decision making;
- reduced costs and excellent value for money; and
- an improved capacity and capability to invest in infrastructure.

This has led to the creation of 8 asset pooling arrangements which have significantly changed the approach to investing for LGPS Funds. Although it should be stressed that the fiduciary responsibility including determining asset allocation and investment strategy remains with the LGPS Funds.

In 2016 CIPFA and AON published "Investment Pooling Governance Principles" for LGPS Administering Authorities. This Guide was intended to support LGPS Funds through the transition to asset pools and specifically to ensure they continued to operate strong governance arrangements.

There are number of governance issues to consider with new arrangements specifically around the relationship between the Fund and the Asset Pool and the governance structure of the Pool which may involve the Administering Authority. Areas such as knowledge and skills, conflicts of interest and information and reporting must be considered and addressed in the Annual Report as part of the process of communicating with all stakeholders.

As a minimum, the following elements of a local authority's annual report and accounts should incorporate information relating to the investment pooling arrangements:

#### **A: MANAGEMENT AND FINANCIAL PERFORMANCE REPORT**

- Scheme management and advisors – include name and contact details of pool operator.
- Risk management – incorporate risks relating to the investment pooling arrangements.
- Financial performance – information to include costs associated with the appointment and management of the operator including investment management expenses, as well as costs relating to the oversight committee.

#### **B: INVESTMENT POLICY AND PERFORMANCE REPORT**

- All of the areas in this section will need to clearly outline arrangements in relation to investment pooling, highlighting which areas of the portfolio are part of the investment pooling arrangement and which elements are excluded.
- Where information is being provided in relation to assets that are both pooled and not pooled, it should outline the information in relation to each separately, for example:
  - ◆ planned versus actual asset allocation – within the operator and otherwise
  - ◆ responsible investment policies – how the administering authority, and respectively how the operator, are:
    - exercising voting rights
    - taking action to pursue responsible investment commitments
  - ◆ what action the administering authority, and respectively the operator, has taken to demonstrate compliance with the Myners principles.

The administering authority may also wish to include an annual report from the asset pool oversight committee.

#### **E: GOVERNANCE COMPLIANCE STATEMENT**

- This will be the updated version, including information relating to the pool oversight committee.

#### **F: FUND ACCOUNT, NET ASSETS STATEMENT AND NOTES**

- In preparing this information, local authorities are required to account for pension funds in accordance with the CIPFA/LASAAC *Code of Practice on Local Authority Accounting in the*

*United Kingdom* which includes comment that preparers have due regard to CIPFA's *Accounting for Local Government Pension Scheme Management Expenses* (CIPFA, 2016). Administering authorities should expect all operators to be familiar with and provide information in line with that management expenses guidance as well as with the Code of Practice. Information will also need to be incorporated in relation to the oversight committee, such as training, administration and adviser costs.

#### **I: STATEMENT OF INVESTMENT PRINCIPLES/INVESTMENT STRATEGY STATEMENT**

- With effect from 1 April 2017 (subject to confirmation at the time of writing), this will be the investment strategy statement and will need to include the administering authority's approach to pooling investments.

#### **K: ANY OTHER APPROPRIATE MATERIAL**

- Information relating to knowledge and skills and training relevant to asset pooling.
- Specific requirements – all information relating to assets should quite clearly state whether the assets are held via the operator or not.

CIPFA's "Proposals for Post Pool Reporting", published in May 2018, acknowledged that there was a legitimate public interest in the impact of national asset pools which could not be adequately addressed from financial reporting information currently contained in LGPS year-end accounts. Additional annual report requirements have therefore been identified at 3 specific stages in the transition process, namely in relation to:

- Pool set up costs
- Ongoing investment management costs
- Asset allocations and performance

#### **Pool set up costs**

Since set up costs are likely to straddle more than one financial year, cost disclosures in annual reports will need to include cumulative totals as shown below. For pools operating outside London, costs should be captured as a minimum from March 2015 (business case submission date).

	Direct	Indirect	Total	Cumulative
	£000s	£000s	£000s	£000s
<b>Set up costs:</b>				
Recruitment				
Legal				
Procurement				
Other support costs eg IT, accommodation				
Share purchase/subscription costs*				
Other working capital provided eg loans				
Staff costs**				
Other costs				
<b>TOTAL SET UP COSTS</b>				
<b>Transition costs:</b>				
Transition fees				
Taxation (seeding relief)				
Other transition costs				
<b>TOTAL TRANSITION COSTS</b>				

\* Include the cost of purchasing shares in the asset pool vehicle where this is a company limited by share capital. Even though these costs will have been treated as an investment in the pension fund or single entity authority accounts, these are a directly attributable cost of setting up the asset pool and so should be included in the table above. Similarly until the asset pools are fully operational it is likely that asset pools may need to charge a subscription fee to pool members, which should be included in the set-up costs.

\*\* Include costs of seconded and directly employed staff involved in establishing the asset pool and working for the pool company prior to commencement of trading. For directly employed staff, costs should also include employers' pension contributions and past service pension costs if these have been transferred from their previous employment.

This information should be presented alongside in-year and cumulative savings achieved to date, and total expected costs and savings as set out in Business Case submissions presented to MHCLG.

### Ongoing investment management costs

Information provided in the annual report should enable the reader to compare levels of ongoing investment management costs between national asset pools and other investment arrangements. The approach suggested is base this information on the analysis that most LGPS already follow when preparing the year-end statement of accounts, as follows:

	Asset Pool				Non-Asset Pool				Fund Total	
	Direct	Indirect	Total		Direct	Indirect	Total		£000s	bps
	£000s	£000s	£000s	bps	£000s	£000s	£000s	bps		
<b>Management fees</b>										
ad valorem										
performance										
research										
PRIIPS compliance										
<b>Asset pool shared costs</b>										
<b>Transaction costs</b>										
commissions										
acquisition/ issue costs										
disposal costs										
registration/filing fees										
taxes and stamp duty										
<b>Custody</b>										
<b>Other</b>										
<b>Total £000</b>										

To measure the extent to which pension funds have saved fees as a result of pooling, it is necessary to calculate price and quantity variances. The price variance measures the extent to which fee rates have generated savings. The quantity variance measures the extent to which fees have changed in line with the value of the assets on which they are based. The cost variance analysis should be accompanied by a qualitative explanation (changes in price, volume, asset mix, etc.) and presented in the context of changes in investment performance and risk.

**Asset allocations and performance**

Gross and net investment returns should be reported separately for investment mandates which have transitioned national asset pools and those which have not. It is proposed that gross and net return are reported by asset class and against either the relevant passive index (for quoted investments) or local performance benchmarks for unquoted investments, as set out in the pension fund’s investment strategy.

Performance should be measured over one, three and five year timeframes and annual reports will need to explain exactly which performance benchmark is being applied. Presentation could be in table form, as shown below, alternatively graphs or graphics could be used.



Asset category	Opening value		Closing value		Performance		Passive Index*	Local Target
	£000s	%	£000s	%	Gross %	Net %		
<b>Asset Pool managed investments</b>								
Pooled investment vehicles:								
Active listed equity								
Active fixed income								
Passive listed equity								
Passive listed income								
Private debt								
Property								
Unlisted equity								
Infrastructure								
Cash								
Multi-Asset Funds/ Diversified Growth Funds								
Other								
<b>Total</b>								
<b>Non-Asset Pool managed investments</b>								
Pooled investment vehicles:								
Active listed equity								
Active fixed income								
Passive listed equity								
Passive listed income								
Private debt								
Property								
Unlisted equity								
Infrastructure								
Cash								
Multi-Asset Funds/ Diversified Growth Funds								
Other								

## I: PENSIONS ADMINISTRATION STRATEGY REPORT

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Pension fund administering authorities have discretion as to whether or not they prepare a pensions administration strategy. Where such a strategy is produced, Regulation 59 of The Local Government Pension Scheme Regulations 2013 (Regulation 57 in Scotland) specifies the matters to be included and Regulation 57 (Regulation 55 in Scotland) requires that the strategy is published as part of the annual report.

The annual report should describe the service standards agreed in any service level agreements with fund employers and report performance against those standards by employer. Examples might be:

- the provision of named pensions contacts for the employer
- the provision of an employer discretions policy document
- the submission of statements of compliance regarding the administration of the scheme within the employer
- the timeliness of data submissions by the employer
- the timeliness of employer responses to fund queries.

The report should also set out any use of powers to seek compensation from employers in respect of any service standard breaches.

## J: FUNDING STRATEGY STATEMENT

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Since 2004, administering authorities have been required to prepare, publish and maintain funding strategy statements (FSS) under Regulation 58 of the LGPS Regulations 2013 (Regulation 56 in Scotland). The Regulation requires the pension fund administering authority to keep its statement under review and to make such revisions as are appropriate following a material change either:

- to its policy on matters covered by the statement; or
- to the Investment Strategy Statement (England and Wales) or Statement of Investment Principles (Scotland).

It is possible, therefore, that an authority may publish more than one FSS during the reporting period but, for the purposes of the pension fund annual report, it is recommended that the statement as it stood at the end of the reporting period should be reproduced in full. The report should also direct the reader to where the previous version/s in force during the reporting period may be found.

Guidance has been provided in the 2016 CIPFA publication “Preparing and Maintaining a Funding Strategy Statement”.

## K: INVESTMENT STRATEGY (ENGLAND AND WALES) OR STATEMENT OF INVESTMENT PRINCIPLES (SCOTLAND)

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In Scotland, Regulation 12 of the LGPS (Management and Investment of Funds)(Scotland) Regulations 2010) requires pension fund administering authorities to prepare, maintain and publish a statement of investment principles (SIP).

Regulation 55 of the Scottish Regulations requires that this section of the annual report include the current version of the SIP. The content of the SIP is specified in Regulation 12 of the LGPS (Management and Investment of Funds) (Scotland) Regulations. The SIP sets out the authority's principles for investing fund monies. In doing so it should:

- State the extent to which it complies with statutory guidance for producing the SIP, including any reasons for non-compliance. The CIPFA publication Investment Decision Making and Disclosure in the Local Government Pension Scheme: A Guide to the Application of Myners Principles constitutes the relevant statutory guidance.
- Link with the investment policy and performance section of the annual report (section B).
- Link with the financial instrument risk disclosures included in the pension fund accounts (section F).

In England and Wales, MHCLG guidance published in September 2016 and July 2017 sets out the detailed requirements for local authority pension funds to prepare, publish, and maintain both a Funding Strategy Statement and an Investment Strategy Statement, the latter replaced the Statement of Investment Principles from 2017/18. The guidance requires that the Investment Strategy Statement contains, amongst other things:

- The strategy and processes in place for managing investment risk;
- Allocation of investments across asset class;
- Approach to pooling and participation in national asset pools;
- Risk management arrangements;
- Social and environmental policies;
- Corporate governance considerations.

## L: COMMUNICATIONS POLICY STATEMENT

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Pension fund administering authorities are statutorily required to prepare, maintain and publish a written statement of their policy concerning communication with members, representatives of members and employing authorities. For England and Wales refer to Regulation 67 of the LGPS Regulations 2013 and for Scotland refer to Regulation 59 of the Scottish Regulations.

The requirement to include this statement in the pension fund annual report is not intended to have any effect on the way in which individual administering authorities have chosen to publish

the statement in the past under Regulation 67.

The report should contain a commentary on how the fund has met the commitments set out in the communications policy statement including:

- how scheme information has been provided to members, their representatives and employers
- in what format and how frequently information has been provided
- what steps the fund has taken to promote scheme membership to prospective members.

## M: ANY OTHER APPROPRIATE MATERIAL

### Specific requirements

#### Scottish pension funds – management commentary

Local Government Finance Circular 1/2018 explains that pension accounts are a separate set of accounts of the administering authority for the purpose of the Local Authority Accounts Regulations 2014 (the Accounts Regulations). The Accounts Regulations require local authority annual accounts to include a management commentary and an annual governance statement.

Circular 1/2018 states that the pension fund annual report meets the requirements for a management commentary in respect of the pension fund.

#### Scottish and Welsh pension funds – annual governance statement

As a stand-alone set of financial statements, to meet CIPFA Code of Practice requirements Scottish and Welsh annual reports should include the following:

- a Statement of Responsibilities for the Statement of Accounts;
- Member approval and publication dates;
- an Annual Governance Statement setting out how the pension fund complied with the CIPFA/SOLACE publication “Delivering Good Governance in Local Government: Framework”.

Although not a statutory requirement, best practice is that annual governance reports are produced as the outcome of annual “governance reviews” carried out by management which consider, amongst other things:

- The overall governance and risk management structures in place;
- Any changes made to these arrangements since last year;
- How the organization complies with the CIPFA/SOLACE publication “Delivering Good Governance in Local Government: Framework”;
- Assurance provided through Internal Audit work or third parties;
- Assurance reviews carried out by service managers.

In Scotland Local Government Finance Circular 1/2018 advises that administering authorities adopt one of the following two approaches:

- a single Governance Statement with two sections. The first section being the Annual Governance Statement, and the second section being the Governance Compliance Statement; or
- two separate statements. The first statement is to be the Annual Governance Statement, followed immediately by the Governance Compliance Statement.

At the date of publication, the Welsh Government was considering a similar approach for Welsh pension funds to follow.

## Discretionary additional information

Although Regulation 55 of the LGPS Regulations 2013 (Regulation 57 of the Scottish Regulations) prescribe what must be included in the pension fund annual report, this needs to be seen as a minimum requirement with administering authorities free to include other information as they see fit. For example, funds may wish to include in this section:

- the statement of compliance with the CIPFA Code of Practice on Public Sector Pensions Finance Knowledge and Skills;
- evidence to demonstrate compliance with the Code of Practice, such as a report on officer and member training undertaken during the year (if not reported elsewhere), skills and knowledge reviews undertaken, etc;
- the role played by the administering authority's internal auditors in providing assurance and managing risk, and a summary of assurance activity undertaken during the year (including any key points arising from such reviews or from the review of ISAE 3402 controls assurance reports);
- a report from the Local Pension Board summarising their work plan and major findings during the year.
- a commentary on how employer discretions have been exercised in the reporting period;
- a glossary of commonly used pension fund terms to aid readers.

Consultation Draft

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