

WIRRAL COUNCIL

PENSIONS COMMITTEE

25 JANUARY 2016

SUBJECT:	LGPS – INVESTMENT REFORM CRITERIA AND GUIDANCE
WARD/S AFFECTED:	NONE
REPORT OF:	STRATEGIC DIRECTOR TRANSFORMATION & RESOURCES
KEY DECISION?	NO

1.0 EXECUTIVE SUMMARY

- 1.1 This report provides Members with details of the criteria by which the Government will assess proposals by administering authorities of the Local Government Pension Scheme to pool investments to deliver significantly reduced costs while maintaining overall investment performance.
- 1.2 This report also seeks Members' approval for officers to continue to develop proposals for pooling in consultation with the Chair and for an initial response to be issued by 19 February 2016.

2.0 BACKGROUND AND KEY ISSUES

- 2.1 A report to November's Pensions Committee set out the background to the Government's proposals for pooling of LGPS investments to create up to six British Wealth Funds, each with at least £25bn of assets.
- 2.2 On 25 November, the consultation documents were issued to coincide with the Chancellor's Comprehensive Spending Review statement. The following four principal criteria set out how administering authorities can deliver against the government's expectations of pooling assets.
- 2.3 **Asset pool(s) that achieve the benefits of scale:** The 90 administering authorities in England and Wales should collaborate to establish, and invest through asset pools, each with at least £25bn of Scheme assets. The proposals should describe these pools, explain how each administering authority's assets will be allocated among the pools, describe the scale benefits that these arrangements are expected to deliver and explain how those benefits will be realised, measured and reported. Authorities should explain:
 - The size of their pool(s) once fully operational.
 - In keeping with the supporting guidance, any assets they propose to hold outside the pool(s), and the rationale for doing so.
 - The type of pool(s) they are participating in, including the legal structure if relevant.
 - How the pool(s) will operate, the work to be carried out internally and services to

- be hired from outside.
- The timetable for establishing the pool(s) and moving their assets into the pool(s). Authorities should explain how they will transparently report progress against that timetable.

2.4 Strong governance and decision making: The proposed governance structure for the pools should:

- I. At the local level, provide authorities with assurance that their investments are being managed appropriately by the pool, in line with their stated investment strategy and in the long-term interests of their members;
- II. At the pool level, ensure that risk is adequately assessed and managed, investment implementation decisions are made with a long-term view, and a culture of continuous improvement is adopted.

Authorities should also revisit their internal processes to ensure efficient and effective decision making and risk management, while maintaining appropriate democratic accountability. Authorities should explain:

- The governance structure for their pool(s), including the accountability between the pool(s) and elected councillors, and how external scrutiny will be used.
- The mechanisms by which the authority can hold the pool(s) to account and secure assurance that their investment strategy is being implemented effectively and their investments are being well managed.
- Decision making procedures at all stages of investment, and the rationale underpinning this.
- The shared objectives for the pool(s), and any policies that are to be agreed between participants.
- The resources allocated to the running of the pool(s), including the governance budget, the number of staff needed and the skills and expertise required.
- How any environmental, social and corporate governance policies will be handled by the pool(s).
- How the authorities will act as responsible, long term investors through the pool(s), including how the pool(s) will determine and enact stewardship responsibilities.
- How the net performance of each asset class will be reported publically by the pool, to encourage the sharing of data and best practice.
- The extent to which benchmarking is used by the authority to assess their own governance and performance and that of the pool(s), for example by undertaking the Scheme Advisory Board's key performance indicator assessment.

2.5 Reduced costs and excellent value for money: In addition to the fees paid for investment, there are further hidden costs that are difficult to ascertain and so are rarely reported in most pension fund accounts. To identify savings, authorities are expected to take the lead in this area and report the costs they incur more transparently. Proposals should explain how the pool(s) will deliver substantial savings in investment fees, both in the near term and over the next 15 years, while at least maintaining overall investment performance.

Active fund management should only be used where it can be shown to deliver value for money, and authorities should report how fees and net performance in each listed asset

class compare to a passive index. In addition authorities should consider setting targets for active managers which are focused on achieving risk-adjusted returns over an appropriate long term time period, rather than solely focusing on short term performance comparisons.

- A fully transparent assessment of investment costs and fees as at 31 March 2013.
- A fully transparent assessment of current investment costs and fees, prepared on the same basis as 2013 for comparison.
- A detailed estimate of savings over the next 15 years.
- A detailed estimate of implementation costs and when they will arise, including transition costs as assets are migrated into the pool(s), and an explanation of how these costs will be met.
- A proposal for reporting transparently against their forecast transition costs and savings, as well as how they will report fees and net performance.

2.6 An improved capacity to invest in infrastructure: Only a very small proportion of Local Government Pension Scheme assets are currently invested in infrastructure; pooling of assets may facilitate greater investment in this area. Proposals should explain how infrastructure will feature in authorities' investment strategies and how the pooling arrangements can improve the capacity and capability to invest in this asset class. Authorities should explain:

- The proportion of their fund currently allocated to infrastructure, both directly and through funds, or "fund of funds".
- How they might develop or acquire the capacity and capability to assess infrastructure projects, and reduce costs by managing any subsequent investments directly through the pool(s), rather than existing fund, or "fund of funds" arrangements.
- The proportion of their fund they intend to invest in infrastructure, and their ambition in this area going forward, as well as how they have arrived at that amount.

2.7 Authorities are asked to submit their initial proposals to the Government by 19 February 2016. Submissions should include a commitment to pooling and a description of their progress towards formalising their arrangements with other authorities. Authorities can choose whether to make individual or joint submissions, or both, at this first stage.

2.8 Refined and completed submissions are expected by 15 July 2016, which fully address the criteria in this document, and provide any further information that would be helpful in evaluating the proposals. At this second stage, the submissions should comprise:

- for each pool, a joint proposal from participating authorities setting out the pooling arrangement in detail. For example, this may cover the governance structures, decision-making processes and implementation timetable; and
- for each authority, an individual return detailing the authority's commitment to, and expectations of, the pool(s). This should include their profile of costs and savings, the transition profile for their assets, and the rationale for any assets they intend to hold outside of the pools in the long term.

2.8 Once submitted, the Government will assess the final proposals against the criteria. A brief report will be provided in response, setting out the extent to which the criteria have

been met and highlighting any aspects of the guidance that the Government believes have not been adequately addressed. In the first instance, the Government will work with authorities who do not develop sufficiently ambitious proposals to help them deliver a more cost effective approach to investment that draws on the benefits of scale. Where this is not possible, the Government will consider how else it can drive value for money for taxpayers, including through the use of the “backstop” legislation, should this be in place following the outcome of the consultation.

2.9 Merseyside Pension Fund

Members will be aware that Merseyside Pension Fund has worked closely with a number of other funds to collaborate in producing a report under the banner of Project POOL which had three goals:

1. to produce an evidence based and objective analysis of pooling options
2. to enable LGPS stakeholders to gather round one or a small number of options which satisfy the Government’s criteria
3. to form a basis of discussion between the LGPS and Government on the best way forward

The report is expected to be issued shortly and the analysis contained therein will be useful in assessing likely cost savings.

- 3.0 The Fund has also had a number of meetings with ‘Northern Funds’ to discuss options for pooling. At the time of writing, MPF has agreed in principle to work with two other funds to develop a proposal to pool investment management, for submission to government in February.

3.0 RELEVANT RISKS

- 3.1 It is important that appropriate governance arrangements are put in place to ensure that the pooling arrangements work well both now and in the future.
- 3.2 As set out in the Project POOL report, the costs and resource required to deliver this change programme should not be under-estimated, particularly in the context of continuing budgetary pressures and severe internal resource constraints within local authorities. Also, the risks of a transition of assets on the scale required are considerable. Strong project management and the use of the most skilled and experienced transition managers will be critical to managing these risks.
- 3.3 The tight timescales for responding to the consultation are not giving much time for data to be collected and assessed appropriately and there is a risk that decisions are ill-considered or that projected cost savings are unrealistic.

4.0 OTHER OPTIONS CONSIDERED

- 4.1 All appropriate options remain under consideration.

5.0 CONSULTATION

- 5.1 The Chair of the Pensions Committee has been consulted and has been involved in several meetings including with DCLG and other LGPS funds..

6.0 OUTSTANDING PREVIOUSLY APPROVED ACTIONS

6.1 N/A

7.0 IMPLICATIONS FOR VOLUNTARY, COMMUNITY AND FAITH GROUPS

7.1 There are none arising from this report.

8.0 RESOURCE IMPLICATIONS: FINANCIAL; IT; STAFFING; AND ASSETS

8.1 The government's proposals are intended to deliver substantial savings from the investment manager fee base within the 89 funds of the LGPS. However, as set out in the Project POOL report, the costs and resource required to deliver this change programme should not be under-estimated. As one of the funds participating in the Project POOL report, a contribution of £10,000 was made towards the cost of producing the report.

9.0 LEGAL IMPLICATIONS

9.1 There are none arising from this report

10.0 EQUALITIES IMPLICATIONS

10.1 Has the potential impact of your proposal(s) been reviewed with regard to equality?

(b) No because there is no relevance to equality.

11.0 CARBON REDUCTION AND ENVIRONMENTAL IMPLICATIONS

11.1 There are no carbon usage implications, nor any other relevant environmental issues arising from this report.

12.0 PLANNING AND COMMUNITY SAFETY IMPLICATIONS

12.1 There are none arising from this report.

13.0 RECOMMENDATION/S

13.1 That Members note the report and authorise officers to continue developing pooling options. Future papers for the Committee will provide further information on likely costs/benefits and any material costs incurred in working up proposals. Any final decision will be subject to Committee approval.

14.0 REASON/S FOR RECOMMENDATION/S

14.1 In view of the tight timescales and requirement for detailed proposals to be developed, it is important that work continues in parallel with reports to this Committee.

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APPENDICES None

BACKGROUND PAPERS/REFERENCE MATERIAL

Local Government Pension Scheme: Investment Reform Criteria and Guidance

BRIEFING NOTES HISTORY

Briefing Note	Date

SUBJECT HISTORY (last 3 years)

Council Meeting	Date
Pension Committee	November 2015
Pension Committee	September 2015