

WIRRAL COUNCIL

PENSIONS COMMITTEE

16 JULY 2019

SUBJECT:	NORTHERN LGPS OPERATING AGREEMENT
WARD/S AFFECTED:	NONE
REPORT OF:	DIRECTOR OF PENSIONS
KEY DECISION?	NO

1.0 EXECUTIVE SUMMARY

- 1.1 This report provides Members with a progress report on the implementation of governance arrangements in relation to Merseyside Pension Fund's participation in the Northern LGPS pool (NLGPS).
- 1.2 A copy of the Operating Agreement for the Northern LGPS, which was taken to Council on 15 July for approval, is attached at Appendix A. The Operating Agreement was the subject of a report to Pensions Committee on 29 October 2018.

2.0 BACKGROUND AND KEY ISSUES

- 2.1 In the July Budget 2015, the Chancellor announced the Government's intention to work with Local Government Pension Scheme (LGPS) (the Scheme) administering authorities to ensure that they pooled investments to significantly reduce costs while maintaining overall investment performance. The Government subsequently issued the following criteria which set out how administering authorities could deliver against the Government's expectations of pooling assets. This report addresses the second of those criteria - **Strong governance and decision making**.

Pooling has been a standing item on the Pensions Committee agenda since that time.

Pooling Criteria

- I. **Asset pool(s) that achieve the benefits of scale:** The 89 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.

II. **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.

III. **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.

- IV. **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.
- 2.2 Pooling of investments has resulted in some fundamental changes to the oversight and management of LGPS assets. Importantly, administering authorities retain responsibility for most aspects of pensions including matters such as: investment strategy, pension liabilities, asset allocation and responsible investment policy. However, manager selection has been explicitly made a Pool decision. Practically speaking, this makes little difference to current arrangements at MPF where fund officers have significant involvement in the management of the fund's assets including the selection of managers. Officers will continue to manage this area but collaboratively with officers of the pool partner funds.
- 2.3 In response to the Government's pooling requirements, eight pension pools have been established across England & Wales encapsulating the 88 local government pension funds - and a range of pooling structures have been put in place. Merseyside Pension Fund has formed the Northern LGPS pool with two other local government pension funds; Greater Manchester and West Yorkshire Pension Funds, all large, cost effective Metropolitan funds. The individual funds will retain their current role of setting asset allocation and investment policy, and will delegate the implementation of that policy to the Northern LGPS.
- 2.4 A Joint Governance Committee will be formed which will have responsibility for ensuring the appropriate structure and resources are in place to implement the policy required by each fund, those resources to be provided by the three Funds. The principal activities of the Joint Governance Committee are set out in Schedule 2 of the appendix.
- 2.5 The Joint Governance Committee will consist of two Members appointed by each Fund plus a total of three trade union representatives and will not have any direct involvement in the appointment of managers or selection of investments. As required in the Guidance, these matters will be fully delegated to professional officers.

- 2.6 The long-term vision for the pool is to provide access to:
- a range of internal and externally managed listed assets at low cost
 - collective investment in alternatives, while building skill to enable cost reduction by increasing direct access
 - working arrangements with other pools where greater size may add value.
- 2.7 The investment philosophy is to maintain simple arrangements, with a relatively low number of managers, low manager and portfolio turnover, an increasing proportion of assets managed internally within the pool, with individual funds retaining the ability to select asset class, territory, and active or passive management.
- 2.8 A meeting was held in March 2018 with the advisors to all three funds and the NLGPS shadow Joint Governance Committee to consider options for developing the pool. The unanimously supported conclusion was to design a simple, low cost pool that will continue delivering the performance the funds expect.
- 2.9 The Northern LGPS Operating Agreement is attached to this report as Appendix A, and sets out how the Northern LGPS will operate, with the three partners having equal voting rights, being responsible for costs on an equal basis (except investment management costs which will be attributed in proportion to the assets being managed). The Agreement also appoints Tameside Borough Council (the administering authority for Greater Manchester Pension Fund) as the host council. The key items to note are those contained in the first three schedules to the agreement, which determine the:-
- Matters reserved to the Pooling Partners
 - Joint Governance Committee Terms of Reference
 - Joint Governance Committee Procedure
- 2.10 An earlier iteration of this Operating Agreement has been approved at Council meetings of both the partner funds' administering authorities.
- 2.11 Since approval by Bradford Council and Tameside Council, the Ministry of Housing, Communities and Local Government has issued further Pooling Guidance. This was the subject of an informal consultation which closed in March 2019. The Pool's response to this consultation is available at: https://northernlgps.org/assets/pdf/2019-03-19_statguidanceresponse.pdf There has been no formal response to the consultation. The Minister has announced, subsequently, that the Guidance will be reissued for a formal consultation. However, the timetable for this to happen is unclear and it is important that an oversight body is formally constituted by NLGPS in order to comply with the extant 2015 guidance.
- 2.12 The recently issued draft Pooling guidance contained a number of changes, setting out the requirements on administering authorities in relation to the pooling of LGPS assets, building on previous Ministerial communications and guidance on investment strategies, and taking account of the current state of progress on pooling. If the Guidance was to be issued as drafted, the most significant implication for the Northern LGPS would be the requirement, as set out in section 3, to establish a pool company for the majority of assets which 'must be a company

regulated by the Financial Conduct Authority (FCA) with appropriate FCA permissions for regulated activities'. Was this to be the case, the governance arrangements proposed for approval would remain essentially intact although the Joint Committee's oversight would be in relation to the pool company rather than the Officer Working Group - as detailed in Schedule 4.

2.13 Following agreement by Pensions Committee on 29 October 2018, the Director of Pensions and the Borough Solicitor have been reviewing the Operating Agreement and liaising with pool partners and advisors with a view to ensuring a mutually acceptable agreement that provides Wirral, as administering authority, with the ability to discharge its responsibilities.

2.14 The pooling reports have also been extensively reviewed by the Local Pension Board which has commended the approach adopted by the Northern LGPS.

3.0 RELEVANT RISKS

3.1 Pooling will result in fundamental changes to oversight and management of LGPS assets. It is essential that appropriate governance arrangements are put in place to ensure that Pensions Committee can exercise its responsibilities in accordance with the Council's constitution.

4.0 OTHER OPTIONS CONSIDERED

4.1 No other options have been considered.

5.0 CONSULTATION

5.1 The Pooling consultation has been discussed with the Merseyside Directors of Finance and stakeholders have been kept informed of the pooling consultation and its implications.

6.0 OUTSTANDING PREVIOUSLY APPROVED ACTIONS

6.1 There are no previously approved actions outstanding.

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 There are none arising directly from this report. The anticipated financial costs of establishing pooling arrangements and the projected savings over the long-term are set out in the Fund's pooling submission of 15 July 2016.

9.0 LEGAL IMPLICATIONS

9.1 There is a requirement to establish a Joint Governance Committee with Tameside and Bradford Councils in order to oversee the implementation of the pooling arrangements by the officers of the 3 Councils;

9.2 The Committee will need to re-consider the pooling arrangements in the light of future guidance from MHCLG;

9.3 The details of the Operating Agreement have yet to be finalised with Tameside and Bradford Councils but no major differences have been identified.

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

Subject to the decision of the full Council at its meeting on 15/7/19, it is recommended that;

13.1 The Committee approves and commends to the Full Council the proposed principles of governance contained in the draft Operating Agreement and delegates to the Director of Pensions and the Director: Governance and Assurance the authority to negotiate and agree with Tameside and Bradford Councils the final draft of the Operating Agreement in consultation with the Chair.

13.2 That Members note the in principle approval of the Operating Agreement by Council and consider whether any amendments are required before it is formally adopted in the Constitution.

14.0 REASON/S FOR RECOMMENDATION/S

14.1 Guidance issued by MHCLG requires that a Pool oversight body is established by administering authorities. Pooling will result in fundamental changes to oversight and management of LGPS assets.

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APPENDICES

BACKGROUND PAPERS/REFERENCE MATERIAL

BRIEFING NOTES HISTORY

Briefing Note	Date

SUBJECT HISTORY (last 3 years)

Council Meeting	Date
An update report is brought to each Pensions Committee	