

Report To: **GREATER MANCHESTER PENSION FUND – LOCAL PENSIONS BOARD**

Date: 14 December 2017

Reporting Officer: Sandra Stewart, Director of Pensions
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Subject: **LGPS POOLING UPDATE**

Report Summary This report provides an update on recent developments relating to the proposals for pooling investments across the LGPS in England and Wales and the recent activities of GMPF in this area

Recommendations: The Board is recommended to:

- i) note the report and the progress update of the Northern Pool which has been submitted to DCLG;
- ii) consider and comment on pooling developments

Policy Implications: None.

Financial Implications: The aim of pooling of assets is to improve net investment returns in the long term. GMPF is working with other like-minded funds to make pooled investments which facilitate this aim.
(Authorised by the Section 151 Officer)

Legal Implications: Revised LGPS Investment Regulations were issued in 2016. The revisions are in part designed to facilitate the pooling of assets between LGPS funds and improve access to infrastructure investments. From a regulatory perspective, LGPS funds are required to pool their assets in order to meet Regulation 7(2)(d) of the 2016 LGPS Investment Regulations. This regulation requires administering authorities to set out their ‘approach’ to pooling investments, including the use of collective investment vehicles and shared services’ in their Investment Strategy Statement. The accompanying statutory guidance to the 2016 Investment Regulations states that:

(Authorised by the Solicitor to the Fund)

“All authorities must commit to a suitable pool to achieve benefits of scale. Administering authorities must confirm their chosen investment pool meets the investment reform criteria and guidance published in November 2015, or to the extent that it does not, that Government is content for it to continue.”

The Northern Pool administering authorities will be asked in early 2018 to confirm that they believe the criteria and guidance has been met when formalising the governing documentation of the pool.

The LGPS Investment Reform Criteria and Guidance was issued by DCLG in November 2015. The 4 high-level criteria are:

- a) Scale (pools should be in excess of £25bn at 31 March 2015)
- b) Strong governance and decision making
- c) Reduced costs and excellent value for money
- d) Improved capacity to invest in infrastructure

Risk Management:

The Fund has been seeking appropriate financial and legal advice throughout where required on its pooling options to ensure it complies with the law, meets its fiduciary duties and to ensure achieving value for money.

ACCESS TO INFORMATION:

CONFIDENTIAL

This report contains exempt information relating to paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972 (as amended). On balance, under paragraph 10 of Part 2 of Schedule 12A, it would not be in the public interest to disclose this information to the public because disclosure would, or would likely to, prejudice the commercial interests of the Fund and/or its agents which, in turn, could impact upon the interests of the local taxpayer and/or the beneficiaries of the Fund.

Background Papers:

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1 INTRODUCTION

- 1.1 As discussed at previous Board meetings, the Chancellor announced in the summer 2015 budget that he would be seeking proposals for LGPS funds to pool their assets in order to create improvements in the following four areas:
- (i) Scale
 - (ii) Value for money
 - (iii) Governance
 - (iv) Facilitating infrastructure investment
- 1.2 GMPF, Merseyside Pension Fund ('MPF') and West Yorkshire Pension Fund ('WYPF') have developed pooling proposals to meet the above four criteria and have made submissions to Government setting out the operation of the 'Northern Pool'.
- 1.3 All pools are required to be operational by 1 April 2018. To oversee the implementation of the pool a shadow joint committee has been created, which has met every six weeks. This consists of the chairs of each of the participating funds. In early 2018 the Northern Pool Joint Committee will be formally established with Tameside MBC being the lead authority.
- 1.4 Pooling progress updates have featured on the agenda at all recent meetings of the GMPF Management Panel and Board members will have had access to these reports. This report provides an update for the Board on recent pool activity and summarises the next steps in developing the pool.

2. AUTUMN PROGRESS REVIEW

- 2.1 All pools were required to submit their pooling proposals to Government in July 2016 and progress updates on the delivery of these proposals were submitted in April 2017.
- 2.2 All pools received a letter from Government over the summer requesting submission of a further progress update covering the period to 30 September. DCLG issued a template for the autumn progress update, which was very similar to the template for the submission made by pools in April.
- 2.3 The Northern Pool's progress report and supporting documents are attached as **Appendices 1-3** to this report. These documents summarise the Northern Pool's progress in meeting each of the Government's 4 headline pooling criteria, as set out in paragraph 1.1 above.
- 2.4 The main ongoing workstreams for the Northern Pool are set out below and are progressing well.
- Developing a vehicle to make private equity investments on a collective basis. The governance of this vehicle is expected to operate in a similar manner to the GLIL infrastructure vehicle.
 - Procurement of a FCA regulated custodian for the pool to ensure all listed assets of the pool (i.e. internally and externally managed equities and bonds) are held within a single permanent FCA regulated entity. The shortlist is now down to 3 bidders and site visits took place in the first week of November. The custodian will also manage the calls and distributions in the Northern Pool private equity vehicle.
 - Work is underway to procure an FCA regulated operator for the GLIL infrastructure vehicle. This would allow other pools to join. GLIL currently has commitments of £1.3bn to direct infrastructure in the UK, with investments of almost £300m made to date. There is currently little evidence of other pools having made significant progress on developing the capacity for direct infrastructure investment.

- The democratic services functions of each of the administering authorities are progressing the creation of the Pool joint committee, with Tameside MBC acting as lead authority. This joint committee will oversee the Pool and provide a democratic link back to the individual funds. The legal agreements setting out the governance framework of the Pool are not yet finalised as work is being undertaken to ensure that they are aligned with the governance framework of the private equity vehicle.

2.5 Other key points to note in the progress update are as follows:

2.6 In this progress update pools are asked to split out costs between

- a) costs incurred to date;
- b) expected costs between now and the date of implementation, and;
- c) expected costs after implementation.

Northern Pool costs to date are approximately £200,000 compared to the original estimate of implementation costs which was £1.8m.

2.7 Details of GMPF's housing investments have been included in the infrastructure section of the response to demonstrate progress against the Pool's target of building 10,000 homes. Up to 30 September, GMPF has financed 284 completed homes, with a further 236 under construction. Due diligence is currently being undertaken on 9 further projects which would deliver another 3,863 homes. It is hoped that the rate of delivery can be increased via joint ventures with other funds in the Pool.

2.8 Following discussion with DCLG civil servants and Jeff Houston of the LGA (who attended part of the 24th October meeting of the Northern Pool Shadow Joint Committee), the progress update provides further clarity for Government on how the plans for the Northern Pool have evolved since the July 2016 submission was made to Government and how, in the opinion of the participating funds, the pooling Criteria and Guidance are met. This is set out on pages 2 and 3 of Appendix 2, with a summary of the key points provided in Section 3 below.

3. MEETING THE POOLING CRITERIA

3.1 From a regulatory perspective, LGPS funds are required to pool their assets in order to meet Regulation 7(2)(d) of the 2016 LGPS Investment Regulations. This regulation requires administering authorities to set out their 'approach to pooling investments, including the use of collective investment vehicles and shared services' in their Investment Strategy Statement.

3.2 The accompanying statutory guidance to the 2016 Investment Regulations states that:

"All authorities must commit to a suitable pool to achieve benefits of scale. Administering authorities must confirm their chosen investment pool meets the investment reform criteria and guidance published in November 2015, or to the extent that it does not, that Government is content for it to continue."

3.3 A strict interpretation of this paragraph suggests that it is up to administering authorities, rather than Government, to determine that they meet the investment reform criteria and guidance. The Northern Pool administering authorities will be asked to confirm that they believe the criteria and guidance has been met when formalising the governing documentation of the pool.

3.4 The LGPS Investment Reform Criteria and Guidance was issued by DCLG in November 2015. The 4 high-level criteria are:

- e) Scale (pools should be in excess of £25bn at 31 March 2015)
- f) Strong governance and decision making
- g) Reduced costs and excellent value for money
- h) Improved capacity to invest in infrastructure

3.5 The full criteria and guidance for pooling is available via the link below:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/479925/criteria_and_guidance_for_investment_reform.pdf

- 3.6 Subsequent letters from Government have sought to clarify the criteria, in particular that Government expects a 'single legal entity' at the heart of each of the pools and that all pools should have a FCA regulated operator. However, these requirements are not explicitly stated in the Criteria and Guidance. It should also be noted that what does or does not constitute 'pooling' or 'a pool' is not clearly defined.
- 3.7 As has been discussed at previous meetings of the Board, the vast majority of the benefits of pooling for the funds in the Northern Pool are in respect of alternative assets where there is greatest scope to generate further economies of scale and to combine resources to make increasingly direct investments. Following detailed discussions with each of the fund's advisors and the professional advisors to the pool, it was agreed in March 2017 that in order to best meet the **Reduced Costs and Excellent Value for Money** criteria set by Government, the Northern Pool should focus resource on making collective investments in alternative assets (which will commence and start generating material cost savings from April 2018) rather than establishing an Investment Management Company established under the Alternative Investment Fund Managers Directive ('AIFM') as a pool operator in the short term.
- 3.8 The **Scale** and **Strong Governance and Decision Making** criteria can be met by appointing an FCA regulated common custodian for the Pool, which will have custody of all the pool's listed assets (i.e. internally and externally managed equities and bonds). Pooled vehicles for alternative assets will operate via joint-ventures, as per the current operation of the GLIL infrastructure vehicle, but are being designed in such a way that they can be converted to operate as FCA regulated entities as and when required.
- 3.9 Strategic asset allocation will be set by each fund's pension committee with the selection of individual investments and investment managers carried out by appropriately qualified and experienced individuals, operating under the legal framework of specialist investment vehicles where appropriate (i.e. GLIL, Northern Pool private equity).
- 3.10 This will be formally documented in the Terms of Reference of the Pool Joint Committee, the participating funds' pension committees and of the individual investment vehicles established.
- 3.11 It is clear that the Northern Pool and LPP via the GLIL vehicle continue to lead the way in the LGPS regarding direct infrastructure investment. It should therefore be relatively straightforward for the participating administering authorities to determine that the **improved capacity to invest in infrastructure** criterion is met.
- 3.12 Regulation 8 of the 2016 LGPS Investment Regulations sets out the action that Government could take should any authority not comply with the regulations and associated guidance. Such action includes the ability for the Secretary of State (following consultation with relevant stakeholders) to direct how a fund invests its assets.

4. MEETINGS OF THE NORTHERN POOL SHADOW JOINT COMMITTEE

- 4.1 Minutes of the Northern Pool Shadow Joint committee meetings are attached as appendices to the pooling update reports to the GMPF Management Panel. After the joint committee is formally established it is expected that the minutes will be included alongside the GMPF working group and Local Board minutes at the start of the Management Panel agenda.
- 4.2 The minutes of the Northern Pool Shadow Joint committee meeting which took place on 12th September are attached for information at **Appendix 4** to this report. The Shadow Joint Committee also met on 24th October and the minutes of this meeting will be provided at a future meeting once finalised.
- 4.3 The Shadow Joint Committee is next due to meet on 5th December.

5. LGPS POOLING NATIONAL DEVELOPMENTS

- 5.1 There are 8 pools across the LGPS, which are made up as follows:
- Northern Pool
 - London CIV (the 33 London Boroughs)
 - South West Funds + Environment Agency (“Brunel Pensions Partnership”)
 - ‘ACCESS’ (Most of the South-East County Council funds)
 - Central Pool (most of the ‘midlands’ LGPS funds)
 - ‘Border to Coast’ (The remaining northern funds + a small number of others)
 - Wales
 - LPFA/Lancashire (‘the Local Pensions Partnership – LPP’) + Berkshire
- 5.2 The eight pools are at different stages of development. Two of the pools, the London CIV and LPP, are currently operational and are in the process of transitioning assets into the pools. The London CIV has not yet pooled any alternative assets.
- 5.3 All pools are required to be fully operational by 1 April 2018, which is a very challenging timescale. The Secretary of State has been clear that all assets should be invested via the pool unless there is a ‘strong value for money case for delay’.
- 5.4 With the exception of the Northern Pool and LPP, all of the other pools have at least 8 participating funds and therefore require their mandates for listed assets to be amalgamated in order to meet the scale criteria and for collective investments to be managed by a FCA regulated operating company in order to avoid being deemed to be operating an unauthorised collective investment scheme.
- 5.5 The number of participants in the Northern Pool is small enough to allow collective investments to be made in alternative assets via joint ventures, as each fund can be directly involved in the investment decision making process (this approach has worked well to date on the GLIL infrastructure partnership);
- 5.6 The ACCESS and Wales pools are in the process of procuring an FCA regulated operator for their pools. The other pools under development are typically ‘building’ their own operator.

6. RECOMMENDATION

- 6.1 As set out on the front of the report.