

Pensions Board

2 July 2019

Report title	LGPS Central Investment Pool Update	
Originating service	Pension Services	
Accountable employee(s)	Jill Davys Tel Email	Assistant Director, Investments & Finance 01902 550555 Jill.davys@wolverhampton.gov.uk
Report to be/has been considered by	Rachel Brothwood Tel Email	Director of Pensions 01902 551715 Rachel.brothwood@wolverhampton.gov.uk

Recommendations for noting:

The Board is asked to note:

1. The update on the LGPS Central investment pool product development, transition and governance arrangements

1.0 Purpose and background

- 1.1 This report provides an update on the ongoing development of LGPS Central Ltd, a jointly owned investment management company established by West Midlands Pension Fund and seven Partner Funds to deliver investment pooling in accordance with the criteria laid down by the Secretary of State.
- 1.2 LGPS Central Ltd (“the Company”) obtained FCA authorisation of the operator and Authorised Contractual Scheme (ACS) in January and February 2018 respectively. These represented key achievements for both the Company and Partner Funds in progressing delivery of a full operating model ahead of the April 2018 deadline and establishing a platform to assist in securing longer term investment cost savings and meet Partner Funds’ strategic investment objectives.
- 1.3 Since the Company formally launched in April 2018, investments products and services to be provided to Partner Funds have been developing, supported and overseen by the governance structures established within the Company and across the wider investment pool. The Shareholder Forum and Joint Committee each met twice during 2018, with the supporting Officer group (the Practitioner Advisory Forum - PAF) meeting at least monthly. The Shareholder meeting held in February approved the 2019/20 budget and business plan. The first Joint Committee meeting of 2019 took place on 21 June with the focus very much on client oversight of investment pooling progress and governance of pooling arrangements.

2.0 Investment Sub-Fund Development and Asset Transition

- 2.1 The first three ACS sub-funds were successfully launched on 3 April 2018 for internal passive equity sub-funds covering UK, Global ex UK and Dividend Growth, with West Midlands Pension Fund (WMPF) assets of around £5.2bn transitioned. Following the launch of the three-internal passive sub-funds, the focus for the pool has been on the product development pipeline to deliver new sub-funds to meet Partner Fund strategic investment requirements. Over the next 2-3 years, a range of internally and externally managed sub-funds are expected to be developed and launched for liquid (e.g. equities and bonds) and alternative more-illiquid asset classes (e.g. private equity, property, infrastructure).
- 2.2 The first transition which took place in April 2018 for the Fund’s internal passive equity assets, has now undergone rigorous internal audit review and has received substantial assurance on the transition of the Fund’s first £5.2bn worth of assets to LGPS Central Ltd. The first active external equity sub-fund was launched as part of the ACS in November 2018 with total assets of £2.1 billion transitioned in February 2019 from five partner funds including around £790m from WMPF. In addition, the Fund made a commitment to LGPS Central Ltd’s first private equity sub-fund of £200m
- 2.3 Other sub-funds currently in the launch process include Emerging Market Equities, Corporate Bonds and Low Carbon Factor Based Index. The Fund’s Investment Advisory Panel, comprising external advisers, the Director of Pensions and Assistant Director (Investment and Finance) continue to review options for investment in these sub-funds, taking into account due diligence in the investment process and the strategic fit for the WMPF.

- 2.4 Fund Officers continue to work closely with Partner Funds and the Company in considering the future product development pipeline for sub-fund launches, recognising changing strategic investment priorities, available resource within LGPS Central Ltd and the potential for cost savings. The Practitioners Advisory Forum working in close co-operation with the company have developed a product development protocol for future sub-fund launches. This has 9 stages of development but offers commencing with high level overview of partner fund requirements with numerous touchpoints for both funds and the company to check that the product development is on track and that the ultimate product will meet partner fund requirements and see the level of investment required. This also provides Partner Funds with the opportunity to undertake due diligence of the process and products as they progress along the development pipeline.
- 2.5 Current products in early stages of development include multi-asset credit, emerging market debt, infrastructure, UK equity, target return and smaller companies. WMPF is unlikely to be participating in all sub-funds and will focus its engagement efforts in those sub-funds where it has a strategic need.
- 2.6 The Pensions Committee are kept updated on product development and will be asked to re-confirm delegations to transition assets as appropriate to these emerging sub-funds, with final decisions and amounts transitioned to be confirmed by the Director of Pensions and Assistant Director, taking into account additional input from the Fund's Investment Advisory Panel.
- 2.7 It is recognised that the development pipeline needs to be flexible and may well differ from the original timetable set out in the business plan.

3.0 Governance

- 3.1 As previously reported to the Board, the governance arrangements for the LGPS Central pool include a Shareholder Forum (as the group of "owner" representatives) and the Joint Committee (focused on investment matters and client-side). The Joint Committee has invited a trade union representative to join the Committee and is waiting for a nomination from the TUC. A representative from the West Midlands' Pension Committee is currently attending on an informal basis. The Practitioners Advisory Forum, PAF (officer group) support both groups and act as a liaison with the Company.
- 3.2 LGPS Central Ltd budget for the 2019/20 financial year along with the business plan was agreed at the Shareholder meeting on 12 February 2019. Regular budget monitoring and updates on progress against the business plan will be kept under review with the company AGM due to take place in November 2019.
- 3.3 The most recent Joint Committee meeting took place on 21 June 2019 where the Committee considered items which focus on the Committee's role as investors and clients. Key items included an update on workstreams from the Practitioners Advisory Forum (including finance, investment, client and governance oversight and responsible investment), along with an investment pool risk register and audit assurance framework. LGPS Central Ltd presented an update on progress along with information on client focused KPIs.

- 3.4 The Board were previously advised of draft guidance issued by MHCLG, noting in particular, the emphasis on the Pool governance structures, and expectation that Administering Authorities undertake oversight and scrutiny of the Pool operating companies. It is understood that a formal consultation is due to be issued, possibly as early as mid-July to ensure formal guidance is in place by the autumn. The PAF Client Oversight and Governance Group is working closely with the company on ensuring that comprehensive client reporting is in place to meet the reporting and oversight requirements for the Joint Committee that will help demonstrate that the governance arrangements are fully in place to meet any new statutory guidance.
- 3.5 LGPS Central Limited's own governance arrangements include an Investment Committee, Executive Committee and oversight from the Non-Executives through the company board and sub committees (Remuneration and Audit and Compliance). The Company also sought and obtained permission from shareholders to recruit for an additional non-executive director and the recruitment for that post is currently underway with the focus being on a representative with a strong understanding of the LGPS and to help meet more of a client input role for the Board.
- 3.6 The Board have been advised that the new CEO, Mike Weston had been appointed and early evidence of his work so far would indicate an enhanced understanding of client requirements and greater partnership working. The company continues to recruit particularly in the investment management area to support ongoing delivery of the products that clients require both for the investment pooled products but also more broadly in terms of advisory and discretionary mandates.

4.0 Financial implications

- 4.1 As previously reported, the final cost of setting up the jointly owned company (over the period July 2016 to launch in April 2018) was just over £4 million; this has been shared equally between the Partner Funds, with West Midlands' share being slightly over £500,000.
- 4.2 The Company's operating budget for 2018/19 was £9.1 million and assumed a progressive build of employees and capability over the year, the final expected outturn for the year was £8.2 million. The operating budget forecast for 2019/20 is £10.6 million, this was approved by Shareholders alongside the Company's strategic business plan for the year at the Company meeting in February.
- 4.3 The ongoing cost of running the FCA-regulated Company operator LGPS Central Ltd and the recharges arising fall under 3 key categories: governance; operator; investment management charges, with governance costs shared on a 1/8th basis and operator and investment management charges shared on an assets under management basis.
- 4.4 New CIPFA guidance on the Pension Fund Annual Reports requires all Pension Funds to fully disclose progress on transition of assets, performance and costs in relation to both the ongoing management of the Pool and transition, thereby providing high levels of transparency on the implementation of investment pooling and the delivery against the business case. The new reporting format is required for the 2018/19 annual report and requires Funds to report in detail on the pool set up costs; ongoing investment management costs both inside and outside the pool and the savings being delivered by pooling.

5.0 Communications

- 5.1 The Investment Team at LGPS Central Ltd are providing Funds with quarterly strategy updates along with broader market and training information. Quarterly stewardship reports covering engagement and voting are also being provided to Partner Funds as well as being accessible on the Company website, the latest quarter can be found at:
<https://www.lgpscentral.co.uk/wp-content/uploads/2019/03/LGPS-Central-Quarterly-Stewardship-Report-Third-quarter.pdf>
- 5.2 Monthly and Quarterly reporting on the LGPSC Ltd sub-funds is being provided and the client oversight and governance group is working closely with the Company to further develop these reports to ensure that they will meet the reporting requirements of Partner Funds as the range of products and assets under management grows.
- 5.3 In conjunction with Partner Funds, LGPS Central Ltd are arranging a Responsible Investor information day to which Pension Committee and Pension Board members have been invited. This is aimed at covering a range of topical issues in connection with Environmental, Social and Governance (ESG).

6.0 Legal implications

- 6.1 The requirement to pool fund investments is a requirement of law, failure to work collaboratively and meet the Government's criteria and timetable for delivery may result in Government intervention.
- 6.2 The key risks are: -
- failure to manage costs and savings in line with the agreed business case
 - failure to meet the requirements of the FCA regulator
 - failure to recruit appropriately skilled and experienced senior personnel to the new company
- 6.3 Comprehensive programme governance arrangements are in place to ensure that the statutory deadline for the implementation of pooling was achieved and that costs and savings are managed in accordance with the agreed business case. The S151 officers of each of the Partner Funds (or their nominated representative) sit on the Practitioners Advisory Forum, the Director of Pensions and Assistant Director, Investments and Finance are the WMPF/WMITA representatives on PAF. Regular meetings are held between the Chairs and/or Vice-Chairs/Nominated representative of the respective Pension Fund Committees through the Joint Committee.
- 6.4 MHCLG issued updated draft statutory guidance relating to investment pooling for informal consultation in January 2019. Both the Fund and LGPSC Ltd have provided responses to the consultation with a formal consultation expected to be issued shortly.

7.0 Equalities implications

- 7.1 There are no direct implications

8.0 Environmental implications

8.1 There are no direct implications

9.0 Human resources implications

9.1 Employees who were previously employed by the Partner Funds to manage their investments or perform other related activities transferred under the Transfer of Undertakings (Protection of Employment) regulations (TUPE) to the new company in April 2018. This followed detailed consideration of current and future roles, TUPE meetings with all relevant staff and formal notification of the transfers.

10.0 Corporate landlord implications

10.1 LGPS Central Ltd is based at 2 locations, Wolverhampton and Matlock, Derbyshire.

10.2 The office in Wolverhampton is based in Mander House, and the office in Matlock is based in Derbyshire County Council Offices.

11.0 Schedule of background papers

11.1 Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016
<http://www.legislation.gov.uk/ukxi/2016/946/contents/made>

11.2 Public Contracts Regulations 2015
<http://www.legislation.gov.uk/ukxi/2015/102/contents/made>

12.0 Schedule of Appendices

12.1 None