



# Pensions Committee

## 25 June 2014

**Report Title** LGPS Reform Consultation

**Originating service** Pension Services

**Accountable officer(s)**

Geik Drever	Director of Pensions
Tel	01902 55(2020)
Email	Geik.drever@wolverhampton.gov.uk

**Report to be/has been considered by**

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**Recommendation(s) for action or decision:**

The Committee is recommended to:

1. Note the contents of the report and endorse the Fund's response to the Department of Communities and Local Government's (DCLG's) consultation on Local Government Pension Scheme (LGPS) reform.

## **1.0 Purpose**

1.1 This report sets out the Fund's response to the DCLG's May 2014 consultation on LGPS reform.

## **2.0 Background**

2.1 With assets of £178 billion as at 31 March 2013, the LGPS is one of the largest funded pension schemes in Europe. Several thousand employers participate in the Scheme, which has a total of 4.68 million active, deferred and pensioner members. The Department for Communities and Local Government (DCLG) is responsible for the regulatory framework governing the Scheme in England and Wales.

2.2 In 2013, the Government ran a call for evidence on the structural reform of the Local Government Pension Scheme (LGPS). The call for evidence was developed around the primary objectives of reducing fund deficits and improving investment returns but in the light of the responses made, the Government has focussed on the scope for saving costs.

2.3 Following the call for evidence, the Shadow Scheme Advisory Board also reviewed the responses to the call for evidence and submitted recommendations to the Minister for Local Government. Furthermore, the Minister for Local Government and the Minister for the Cabinet Office commissioned additional analysis using the Contestable Policy Fund. Following a competitive tender process, Hymans Robertson were selected to establish the aggregate performance of the Scheme by asset class and to provide a detailed cost-benefit analysis of three potential options for reform:

- Establishing one common investment vehicle for all funds;
- Creating five to ten common investment vehicles for fund assets
- Merging the existing structure into five to ten funds.

## **3.0 The Consultation**

3.1 On 1 May 2014 the Government launched a consultation in response to the call for evidence into the structure of the LGPS. This consultation represents the next step in reform of the LGPS and is the culmination of three sources of evidence, the public call for evidence into the future structure of the Scheme; the recommendations of the Shadow Scheme Advisory Board, based on the responses to that call for evidence; and the detailed cost-benefit analysis provided by Hymans Robertson.

3.2 The consultation sets out how the LGPS could achieve significant savings of £660 million a year. It outlines proposals to use common investment vehicles (CIVs) for both listed and alternative asset classes, to help funds achieve economies of scale and deliver savings. In particular, it proposes a move to low cost passive (index tracking) management of listed assets away from higher cost active (value added seeking) management.

- 3.3 The consultation sets out the government's preferred approach to reform, seeks views on the proposals and asks respondents to consider how if adopted, these reforms might be implemented most effectively.

The proposals set out in the consultation include:

- Establishing CIVs to provide funds with a mechanism to access economies of scale, helping them to invest more efficiently in listed and alternative assets and to reduce investment costs.
- Significantly reducing investment fees and other costs of investment by using passive management for listed assets, since the aggregate fund performance has been shown to replicate the market.
- Keeping asset allocation with the local fund authorities, and making available more transparent and comparable data to help identify the true cost of investment and drive further efficiencies in the Scheme.
- A proposal not to pursue fund mergers at this time.

#### **4.0 The questions in the consultation**

- 4.1 The five questions raised in the consultation are as follows –

Q1. Do you agree that CIVs would allow funds to achieve economies of scale and deliver cost savings for listed and alternative investments?

Q2. Do you agree with the proposal to keep decisions about asset allocation with local fund authorities?

Q3. How many CIVs should be established and which asset classes do you think should be represented in each of the listed asset and alternative asset CIVs?

Q4. What type of CIV would offer the most beneficial structure? What governance arrangements should be established?

Q5. Four options relating to the use of passive management in listed assets are put forward, ranging from compulsion to invest some or all assets in this way, to a comply or explain regime. Which of these offers best value for taxpayers, Scheme members and employers?

- 4.2 A copy of the DCLG's May 2014 consultation on LGPS reform can be found at [www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies](http://www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies)

- 4.3 At the Pensions Committee's training session, Hymans Robertson will present on the DCLG consultation and we will present on our response. We will also make a present at our forthcoming employer summer briefing.

## **5.0 Summary of WMPF's Position and Response**

5.1 As one of the largest LGPS funds, WMPF has substantial internal investment management resources. These are not available to all 89 LGPS funds in England and Wales. Further, WMPF deploys passive management of its listed assets with £3.6 billion so deployed. WMPF's views can be summarised as follows –

- LGPS internal investment management arrangements deliver good investment performance cost effectively as is evidenced in Hymans Robertson's report. They should be encouraged and supported as far as practicable;
- Decisions regarding asset allocation and portfolio objectives should be made locally;
- All forms of collaboration should be actively explored. There may be a role for a CIV or CIVs (ie in alternative investments) but we would not support the mandatory use of CIVs and the potential complexities associated in setting up such a vehicle should not be underestimated;
- The 'comply and explain' option would be best so far as passive management is concerned. WMPF believes that passive investment management has a crucial role to play in listed assets, but in conjunction with targeted active investment management. WMPF does not favour compulsion to invest passively (in whole or in part) as an optimal solution.

5.2 A copy of WMPF's draft response (with an accompanying covering letter) is set out in Appendix A. The Committee is requested to endorse the draft response and once finalised, the response will be sent to the DCLG ahead of the response deadline of 11 July 2014.

5.3 The Committee will be appraised of further developments both regarding the consultation and LGPS reform more widely.

## **6.0 Financial implications**

6.1 This report contains no direct financial implications but the changes proposed in the paper could impact on both cost and investment return.

## **7.0 Legal implications**

7.1 This report contains no direct legal implications.

## **8.0 Equalities implications**

8.1 This report has no direct equal opportunities implications.

## **9.0 Environmental implications**

9.1 This report has no direct environmental implications.

**10.0 Human resources implications**

10.1 The report contains no direct human resource implications.

**11.0 Corporate landlord implications**

11.1 The report contains no direct corporate landlord implications.

**12.0 Schedule of background papers**

12.1 There were no preceding background papers.