

Pensions Committee

22 March 2017

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| Report title | Investment Pooling | |
| Originating service | Pension services | |
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Recommendation(s) for action or decision:

The Committee is recommended to:

- 1.1. To note the progress to date with the implementation of LGPS Central.

1.0 Purpose

- 1.1. West Midlands Pension Fund has been working with seven partner Funds on a proposal which will meet the criteria for pooling laid down by the Secretary of State, by establishing a jointly owned investment management company, to be known as 'LGPS Central Ltd'. This report outlines the progress made with the implementation and set up of LGPS Central in line with the Governments overall timescale of 1 April 2018.

2.0 Background

- 2.1 The revised LGPS Investment Regulations require all administering authorities in England and Wales to enter into joint (pooled) arrangements for the management of their investment assets, with effect from 1st April 2018, in order to achieve scale economies and increase investment capacity.
- 2.2 West Midlands Pension Fund has been working with seven partner Funds on a proposal which will meet the criteria for pooling laid down by the Secretary of State, by establishing a jointly owned investment management company, to be known as 'LGPS Central Ltd'.
- 2.3 In July 2016, the partner Funds submitted a business case to the Department for Communities and Local Government (DCLG) with the proposal for the LGPS Central pool. This was subsequently formally approved in November 2016.
- 2.4 Over the last 12 months, the Pensions Committee and Local Pensions Board have been kept informed of the work of the Fund in meeting Government's criteria. Legal workshops have been organised with representatives from all the Administering Authorities, together with presentations and reports presented to each committee meeting outlining the proposed governance structure and associated implications as submitted to Government in July 2016. A Stakeholders' day was held on 24 January 2017 for both the Pensions Committees and the Local Pensions Boards across the partner Funds.
- 2.5 In readiness for meeting Government's timetable of April 2018, LGPS Central Ltd has been incorporated as a company registered with Companies House. To assist in its creation, and in agreement with all the Administering Authorities, Wolverhampton City Council established the company as the subscriber shareholder with a sole Director. This is a process matter to ensure the creation of the company. The other 7 Authorities will subscribe to the company following finalisation of adoption of agreements.
- 2.6 The Government has also made clear its expectation that pooled entities must be registered with the Financial Conduct Authority (FCA) and regulated under the Financial Services and Markets Act 2000, to ensure appropriate safeguards over the management of client monies. As such, the new LGPS Central company will be subject to on-going oversight by the regulator.

3.0 Progress

- 3.1 The programme continues to progress to schedule, and focus is on the development of the FCA application for submission in July 2017. This application will set out how LGPS Central will operate in line with the regulatory requirements, the organisational structure, and the key policies and procedures for the organisation.
- 3.2 As part of the operator application to the FCA LGPS Central will develop and submit the Strategic Plan for the company. The purpose of this document is to set the overall objectives of the company and enable the partner Funds to understand how the company will be managed and what they can expect. It will detail the key areas including, the operating model, governance and risk management and the financial plans and projections. This document is currently being developed and is scheduled for approval at the Shareholders Forum in June 2017 and Committee will have sight of this later in the year.
- 3.3 The procurement and selection of key systems and suppliers for LGPS Central is underway, with work starting on the procurement of the depository and custodian service, and fund administration supplier in November 2016. The first stage of the process is now complete, and three suppliers were invited to tender in February 2017, with the preferred supplier scheduled to be selected in April 2017. Other procurement processes were initiated in early 2017, which include the selection of an operator and sub fund external auditor, finance system and investment system.
- 3.4 Furthermore, a draft LGPS Central Investment Offering has been developed, which sets out the different sub funds in which Partner Funds will be able to invest. Discussions are underway by each partner Fund with their individual advisors to ensure the proposed structure will enable Fund's to meet their strategic asset allocation.

4.0 Resourcing of LGPS Central

- 4.1 A core programme management team is in place and are supported by colleagues from each of the partner Funds working on the programme on behalf of LGPS Central. To ensure effective governance on the work being undertaken and demonstrate that colleagues working on the programme are carrying out their duties in the interest of LGPS Central, key resources will be seconded into the company. The secondment arrangements do not reference time and payment, it is solely for governance.
- 4.2 To support with the recruitment of the key senior roles for the company, professional recruitment advisors have been appointed. A preliminary list of candidates for the roles of Non Executive Chair and Chief Executive Officer, took place in February 2017, and the shortlisting and interview of candidates by the Shareholder's Forum is scheduled for March. Other key roles, which include the Chief Investment Officer, Chief Operating/Finance Officer and two Non-Executive Directors, were advertised in February with appointments expected late spring/early summer.

5.0 Financial implications

- 5.1 The estimated cost of setting up the jointly owned company is circa £4 million; this will be shared equally between the Partner Funds, with West Midlands' share being around £500,000. There will also be significant transition costs as existing investment mandates are unwound and funds are transferred into new collective investment vehicles. It is not possible to accurately predict these costs, but the initial business case includes an estimate of approximately £50 million. Transition costs will also be shared between the funds on a fair and equitable basis and will be incurred when assets are transitioned from 2018/19.
- 5.2 A document detailing the key cost sharing principles has been produced and provides recommendations for sharing the costs of establishing and running LGPS Central between the Partner Funds. The principles detailed in this document have been agreed by all eight partner Funds.
- 5.3 As the new company will be a regulated entity, under FCA rules, it will likely need to hold regulatory capital to guarantee its solvency. The regulatory capital requirement is expected to be in the region of £10 million, this will be on an agreed split of debt and equity. Due to regulatory requirements, City of Wolverhampton Council as the administering authority will only be able to provide equity.
- 5.4 West Midlands Pension Fund's share of all costs (including the regulatory capital) will be met from the Fund, and there will therefore be no direct impact on the administering authority's revenue or capital budgets.
- 5.5 All cost sharing principles together with financial modelling of the operational costs and fee models are currently being drafted and will be reviewed in the context of direct and indirect tax implications by PWC.
- 5.6 Estimated net total savings for the pool as per the July 2016 submission to Government, are in the region of cumulative £200 million over the period from 2018/19 to 2032/33, with annual savings of around £29 million being achieved by the end of this period
- 5.7 Work is underway to update the initial Business Case submitted in July 2016, which was based on the 2014/15 asset allocation, with the 2015/16 actual assets of the partner Funds against the proposed investment offering for LGPS Central.
- 5.8 Of the overall set up costs of circa £4 million as set out in 5.1, the projected expenditure to the end of March 2017 are estimated to be approximately £750,000, of which West Midlands' share is £94,000 (one eighth). These figures are based on costs incurred up to the middle of February, and are therefore subject to change during the remainder of the financial year. There is budget provision within the Fund's 2016/17 operating budget to meet this forecast cost.

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 achieve the statutory implementation deadline of 1st April 2018
 - 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 is achieved and that costs and savings are managed in accordance with the agreed business case. The S151 officers of each of the Partner Funds sit on the LGPS Central Programme Board and regular joint meetings are held between the Chairs and Vice-Chairs of the respective Pension Fund Committees to ensure effective member oversight of progress and delivery. The West Midlands Pension Fund Committee and Local Pensions Board are also being updated regularly on key developments and decisions, as are the fund employers.
- 6.4 Expert advisers have been appointed to provide support to LGPS Central on legal matters, FCA registration, taxation and overall programme management, and professional recruitment consultants have been appointed to assist and advise on executive recruitment and remuneration.
- 6.5 Browne Jacobson were appointed jointly by the Funds to assist them with their governance arrangements in approving the documents which have been agreed by the Council Solicitor.

7.0 Equalities implications

- 7.1 There are no implications

8.0 Environmental implications

- 8.1 There are no implications

9.0 Human resources implications

- 9.1 It is expected that employees who are currently employed by the partner Funds to manage their investments or perform other related activities will transfer under the Transfer of Undertakings (Protection of Employment) regulations (TUPE) to the new company, subject to detailed consideration of current and future roles.

10.0 Corporate landlord implications

- 10.1 It has been agreed that LGPS Central Ltd will be based at 2 locations. The headquarters will be based in Wolverhampton with a satellite office in Matlock Derbyshire.
- 10.2 Considerations for office space which meet the Pool's requirements are ongoing together with the associated resources. An update will be provided as this progresses.

11.0 Schedule of background papers

- 11.1 Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016
<http://www.legislation.gov.uk/uksi/2016/946/contents/made>
- 11.2 Public Contracts Regulations 2015
<http://www.legislation.gov.uk/uksi/2015/102/contents/made>