

# Pensions Committee

## 6 September 2017

<b>Report title</b>	MiFID II – opt up to professional client	
<b>Originating service</b>	Pension Services	
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### Recommendations for action or decision:

The Committee is recommended to:

1. Approve the opt-up of the Funds to Professional Client status.
2. Authorise the Director of Pensions to request the Funds' existing investment managers treat both the West Midlands Pension Fund and West Midlands Integrated Transport Authority Fund as Professional Clients.
3. Require all future manager appointments (including LGPS Central) are subject to classification of the Fund as a Professional Client.
4. Confirm the delegations in place in relation to investment decisions as summarised in 4.6 of the report.

### Recommendations for noting:

The Committee is asked to note:

1. The greater clarity now available on the criteria local authorities administering LGPS pension funds must meet to "opt-up" and retain Professional Client status.
2. The protections available to Retail Clients which are not available following opt-up to Professional Client.
3. The impact reclassification to Retail Client would have on the Funds' ability to invest.

## **1.0 Purpose**

- 1.1 To update Committee on the final policy statement issued by the FCA in July 2017, confirming the rules for implementation of an EU directive which will (without action) impact on the client categorisation of Local Government Pension Scheme's and the Fund's ability to implement investment strategy.

## **2.0 Background**

- 2.1 The Markets in Financial Instruments Directive (MiFID II) is the EU Legislation that regulates firms who provide services to clients linked to 'financial instruments' (shares, bonds, units in collective investment schemes and derivatives) and the venues where those instruments are traded.
- 2.2 European Commission instigated a review of MiFID due to increasing complexity of financial products and issues related to the 2008 financial crisis. The outcome of the review was a revised Directive, MiFID II, which is to take effect from 3 January 2018.
- 2.3 During 2016 and early 2017, the FCA consulted on the implementation proposals for MiFID II. On 3 July, the FCA published a policy statement setting out the final rules on a number of matters
- 2.4 The key element to the new legislation is the classification of clients (including pension funds) as being Retail or Professional. The proposed rules will re-classify all LGPS pension funds as Retail clients in a change from their current status as Professional client. This will put restrictions on LGPS pension funds investments, could lead to requirement to offload certain assets (for example, private equity funds) and could potentially impact the fee rates funds are charged.

## **3.0 Final policy statement**

- 3.1 Although the FCA reiterates that it is a requirement for local authorities to be reclassified as Retail clients by default it has acknowledged that the LGPS has its own governing regulations and oversight bodies and has amended the opt-up criteria to enable LGPS funds to opt-up to Professional client status.
- 3.2 The final criteria remains a combination of qualitative and quantitative tests but critically specific reference has been added to enable clients who are administering authorities of LGPS funds to meet these.
- 3.3 The statement acknowledges LGPS governance arrangements and role of elected members, enabling investment managers to take a collective view of the expertise, experience and knowledge of committee members, supported by officers and advisers.

#### **4.0 Opt up process and considerations**

- 4.1 The classification of investors (including both the West Midlands Pension Fund and West Midlands Integrated Transport Authority Pension Fund) under MiFID II is determined by each individual investment manager. The Fund will need to approach each one to request “opt-up” and seek confirmation of the manager’s classification of the Fund. With limited transitional arrangements likely to be available, this process will need to be prioritised to ensure the Fund has the status required to continue to implement investment strategy, ahead of the new rules coming into effect from 3 January 2018.
- 4.2 The Fund has prepared a template letter and completed questionnaire ready for issue to all managers, based on a template created by the LGA, in conjunction with Investment Association.
- 4.3 A manager is under no obligation to “opt-up” the Fund and will seek assurance from the Fund that it understands the higher level of regulatory protection offered to Retail client, that will be waived on re-classification to Professional client.
- 4.4 Appendix 1 includes a schedule of warnings in relation to the protections provided to Retail clients which are not in place for Professional clients. A number of these relate to assumed knowledge and disclosure of information. It should be noted that the Fund is currently treated as a Professional client and does not therefore currently have these protections. It should also be noted that other occupational pension funds in the UK will automatically be classified as Professional clients under the new rules.
- 4.5 Subject to confirmation from the Committee that it would like Funds to continue to elect Professional client status and authorisation to the Director of Pensions to proceed with the opt-up process, Fund officers will make the necessary arrangements to ensure managers reclassify the Funds with effect from 3 January 2018. Any new manager appointments will be subject to the manager’s classification of the Fund as a Professional client.
- 4.6 As part of the opt-up process, the Administering Authority is required to confirm delegations in place in relation to investment decisions. These are summarised below for completeness.
- Wolverhampton City Council as the Administering Authority for West Midlands Pension Fund has delegated under Section 101 Local Government Act 1972 the responsibility for the management and administration of the pension fund, including investment management, to its Pension Committee.
  - A copy of the Council’s constitution showing this delegation can be found by following the link at the end of this report.

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- In addition, the Pension Committee under Section 101 Local Government Act 1972 has delegated to its Director of Pensions the responsibility for the administrative and investment management of the Pension Fund, as shown in the Council's constitution (page 183).
- The West Midlands Integrated Transport Authority as Administering Authority for the West Midlands Integrated Transport Authority Pension Fund (ITA Fund), delegated to the Pension Committee of Wolverhampton City Council, responsibility for the management and administration of the ITA Fund. That delegation was accepted and a copy of the report can be found by following the link at the end of this report.

Delegation to the Director of Pensions is governed by Section 101 Local Government Act 1972.

- The creation of the West Midlands Combined Authority, absolved the West Midlands Integrated Transport Authority and the Combined Authority became the Administering Authority for the ITA Fund. The Combined Authority adopted all existing delegations, including the delegation to the Wolverhampton City Council Pension Committee and a copy of the creation order can be found by following the link at the end of this report.

## **5.0 Financial implications**

- 5.1 If opt up is not be achieved before the new rules become effective MiFID II could restrict WMPF's ability to make investments into its current investment strategy and may also impact on fee rates.

## **6.0 Legal implications**

- 6.1 This report contains no direct legal implications.

## **7.0 Equalities implications**

- 7.1 This report contains no equal opportunities implications.

## **8.0 Environmental implications**

- 8.1 This report contains no environmental implications.

## **9.0 Human resources implications**

- 9.1 This report contains no direct human resources implications.

## **10.0 Corporate landlord implications**

- 10.1 This report contains no direct corporate landlord implications.

## **11.0 Schedule of background papers**

11.1 MiFID II Adoption – Pension Committee March 2017

## **12.0 Schedule of appendices**

12.1 Appendix 1 – Warnings – loss of protections for the Local Authority if categorised as a Professional Client.

## **13.0 Schedule of background papers**

13.1 Section 101 Local Government Act 1972 -  
<http://www.legislation.gov.uk/ukpga/1972/70/section/101>

13.2 City of Wolverhampton – The Constitution  
<https://wolverhamptonintranet.moderngov.co.uk/documents/s50871/Constitution%20-%207.4.17.pdf>

13.3 Pensions Committee report, 18 March 2015, Governemce Reform 2014, Delegation of Integrated Transport Authority

<https://wolverhamptonintranet.moderngov.co.uk/documents/s9109/Governance%20Reform%202014%20Delegation%20of%20the%20Integrated%20Transport%20Authority.pdf>

13.4 The West Midlands Combined Authority Order 2016  
<http://www.legislation.gov.uk/uksi/2016/653/contents/made>