

NORTH YORKSHIRE COUNTY COUNCIL**PENSION FUND COMMITTEE****24 NOVEMBER 2016****LGPS POOLING ARRANGEMENTS****Report of the Treasurer****1.0 PURPOSE OF REPORT**

- 1.1 The Committee has previously considered the Government's proposal to pool the Local Government Pension Scheme's investments in England and Wales.
- 1.2 This report updates the Committee on the position.

2.0 BACKGROUND

- 2.1 On 7 July 2015 the Chancellor announced a consultation on legislation for delivering savings via the use of pooled investment vehicles for Scheme assets.
- 2.2 On 25 November 2015 the Government released a set of documents that took this policy forward.
- 2.3 These documents state that the pools should take the form of up to six "British Wealth Funds", each with assets of at least £25bn, which are able to invest in infrastructure and drive local growth.
- 2.4 The local Section 101 committees, in the Council's case the Pension Fund Committee, will remain responsible for setting the funding strategy and the high level investment strategy, e.g. the appropriate asset allocation for their fund. This has been confirmed in answers to Parliamentary questions and by civil servants during the consultation process.
- 2.5 Valuations, the setting of employer contributions and pensions administration will also remain at the local level.

3.0 POOLING PROPOSALS

- 3.1 At the Pension Fund Committee meeting on 25 February 2016, Members considered the pooling options open to the Fund and resolved that it should join the Border to Coast Pensions Partnership (BCPP), a non-regional pool of funds with a like-minded approach to investment. The BCPP members are:

- Bedfordshire
- Cumbria
- Durham
- East Riding
- Lincolnshire
- Northumberland
- North Yorkshire
- South Yorkshire
- South Yorkshire Transport Fund
- Surrey
- Teesside
- Tyne and Wear
- Warwickshire

3.2 As at 31 March 2015, the assets of BCPP were around £36bn, significantly in excess of the Government's threshold of £25bn.

3.3 The initial response to Government from the BCPP was submitted on 19 February 2016. In addition, the Fund made an individual response to provide the context of its own position in relation to pooling.

3.4 At the end of March, the Chair of each fund in the Pool received a supportive letter from Marcus Jones MP, the Minister for Local Government, which also reiterated the requirement for a more detailed submission in July 2016.

3.5 On the deadline date of 15 July 2016 the BCPP submitted this more detailed response, using the Government's template and addressing the guidance, which asked for information on

- asset pool(s) that achieve the benefits of scale
- strong governance and decision making
- reduced costs and excellent value for money
- an improved capacity to invest in infrastructure

- 3.6 Due to the size of the document this response is not included in this report but is available on the Fund's website, <https://www.nypf.org.uk/Documents/BCPPProposalforAssetPoolingJuly20160715FINAL.PDF>. Responses from individual funds were not required.
- 3.7 There were eight pooling proposals submitted in February and July 2016. The other seven pools are as follows:
- Central - a group of funds in the Midlands, with assets of £34bn
 - Brunel - a group of funds in the South West, with assets of £22bn
 - ACCESS - a South East based group of funds, with assets of £36bn
 - Wales - all 8 funds in Wales, with assets of £12bn
 - Northern - Merseyside, Greater Manchester and West Yorkshire, with assets of £36bn
 - London - all 33 London boroughs, with assets of £25bn
 - Local Pensions Partnership - Lancashire, London Pension Fund Authority and Berkshire, with assets of £14bn
- 3.8 As a reminder to the Committee, the BCPP received a cost benefit analysis from Deloitte and legal advice from Squire Patton Boggs. The range of potential legal structures was reviewed and a recommendation made of which structures to adopt.
- 3.9 In broad terms the following structures were recommended and formed the basis of the July 2016 proposal.
- Funds – Members, through the individual Pension Fund Committees retain asset allocation decisions, control over the investment strategy and the funding strategy.
 - Supervisory Entity - a Joint Committee to oversee the operation of the FCA regulated BCPP company. This Joint Committee would be made up of representatives from each fund, and operate on the basis of one fund one vote. The Joint Committee would not engage in FCA regulated activities. It would exercise significant control over the Board in matters such as appointments of key personnel, remuneration and approval of the business plan.
 - Executive Body – the wholly owned company controlling all investment decision making (e.g. hiring, firing and monitoring of managers and investment products; FCA compliance; tax monitoring; etc.). These functions would be performed by employees of the newly created FCA regulated investment management company. Some of these employees will also be required to have FCA authorisation, separate from the company authorisation. Advice recommended against anyone

sitting on both the Joint Committee and the Board of this company to avoid conflicts of interest.

- Sub-Funds – assets are to be held in the most operationally and tax efficient manner, which, following the detailed advice above, at a high level is deemed to be
 - liquid quoted assets should be held in an Authorised Contractual Scheme (ACS). This is a structure regulated by the FCA and as such will provide strong controls over the operation
 - assets held in life funds can continue to be held in the name of the individual fund, but future monitoring and tender exercises will be undertaken by the Pool
 - a mix of other structures for illiquid assets such as property, private equity, and infrastructure is still to be determined. They are complex in terms of tax and legal ownership. This is recognised by Government and the current assets in these categories which are held by funds will be allowed to go into run off over an extended period. New investments will be made in the new Pool structures, when they are available.

3.10 The proposed governance and investment structures are shown diagrammatically below:



4.0 INTERIM GOVERNANCE ARRANGEMENTS

4.1 In order to provide some structure around the work being undertaken by the funds in the Pool it was considered appropriate to establish some interim governance arrangements until the formal structures and arrangements are finalised.

4.2 In summary, the following groups have been established:

- Member Steering Group - this consists of the Chairs of each individual fund or a representative nominated by the administering authority. This Group provided input and guidance into the submission in July and will be the decision making body going forward. It is expected that members of this group will report back to, and take soundings from, their respective committees and administering authorities.
- Officer Operations Group - this is accountable to the Member Steering Group. It undertook and co-ordinated the work on the July submission and beyond, and will perform the same role on work going forward.

4.3 Both of these groups will continue to exist to take the pooling initiative forward until the final formal governance structures are established. There have been three meetings of the Members Steering Group so far, on 6 June, 24 June and on 30 September 2016.

4.4 The Member Steering Group has decided that a new Chair will be chosen for each meeting. The fourth meeting of the Member Steering Group is due to take place in York, on 18 November 2016. As this meeting is after the publication deadline for these papers, a verbal update will be provided to Members at the meeting.

4.5 On 5 September 2016 a meeting took place with Section 151 Officers and the Heads of Legal Services of the BCPP administering authorities to go through the proposal in detail.

5.0 PROGRESS TOWARDS THE LONGER TERM ARRANGEMENTS

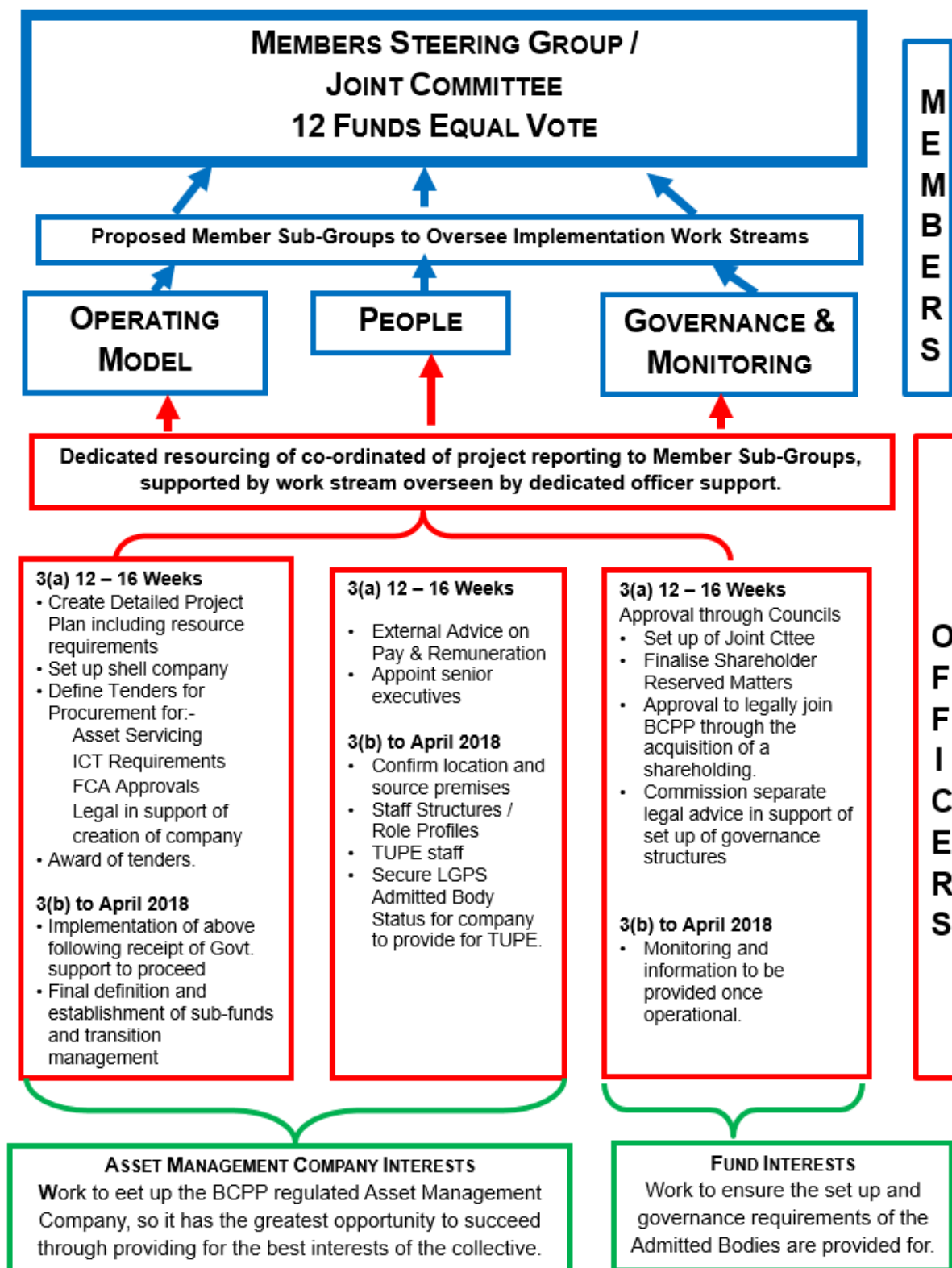
5.1 The Government has stated an expectation that formal pooling arrangements will be in effect by April 2018. The BCPP response submitted in July 2016 suggested that this was possible as long as the Government replied positively by the end of September. The view was that BCPP member funds would not be prepared to spend significant money until it was clear the Government supported the approach. So far, no reply has been received.

5.2 A meeting has however been arranged with Marcus Jones MP on 24 November 2016. Attending will be three Chairs, three officers and one Section 151 Officer, providing wide representation from the BCPP administering authorities. This meeting represents an opportunity to

respond to any questions the Minister may have. A formal reply to the consultation response is expected once the Minister has met with representatives from all eight pools.

- 5.3 The pooling proposal referred to in paragraph 3.6 above includes a section 4a (page 38) on implementation costs, based on two scenarios. Each BCPP member has agreed to bear an equal share of implementation costs, which equates to £350k per Fund based on scenario B, the high estimate. Although every effort will be made to keep costs down, the Member Steering Group agreed to seek approval from their respective Pension Fund Committees to approve expenditure up to this amount. Members are therefore recommended to approve a budget allocation of £350k to facilitate pooling arrangements. It was considered appropriate to get this approval now, to ensure that the BCPP can move quickly to engage the various organisations providing the services, advice and support that will be required to make this happen, once Government has agreed the pooling proposal is acceptable.
- 5.4 Anticipating the work that will be required to set up complex arrangements, the Member Steering Group also decided to set up three specific workstreams. Each would include one or more Chairs from the Member Steering Group to provide direction for the workstream, and officers from the Officer Operations Group who would progress the work.
- 5.5 A procurement process has been initiated to seek further legal advice. This is in two strands, the first being advice that the FCA regulated investment company will need on its arrangements and its relationship with the twelve administering authorities as both investors and owners. The second is advice that the administering authorities themselves will need as investors in and owners of the company. The investors/owners need to have separate legal advice from the company to ensure the interests of both are fully protected. Legal advice will be required to support the work of all three workstreams.

5.6 A diagram providing some details of the areas these three workstreams will cover is shown below:



- 5.7 The Operating Model workstream is focussed on the creation of the FCA regulated investment company and all of the requirements that need to go with it. The initial work includes the creation of a shell company so that it can be a contracting party, rather than advice be commissioned by one of the BCPP Funds on behalf of the other eleven. It also includes more clearly defining the sub-funds which may be available. Meetings with the investment advisers of all twelve BCPP funds are planned in November and December to assist with this.
- 5.8 The People workstream is focussed on the arrangements for everyone who will be employed by the company. This ranges from the Board executive and non-executive director remuneration packages to the accommodation requirements for all staff. Initial work will include consulting with advisers and recruitment agencies to assess the market rates for investment professionals, and establishing the approach to recruitments as required.
- 5.9 The Governance and Monitoring workstream is focussed on the governance arrangements between the administering authorities as investors and owners and the company, and the appropriate monitoring arrangements once pooling is underway. The initial work will be on the terms of reference of the Joint Committee, and the Shareholder Agreement between each administering authority and the company they will own. It is believed that these documents will require approval by the Full Council of each of the administering authorities so a significant lead-in time is expected. Section 151 Officers and the Heads of Legal have all been contacted to alert them to this requirement.
- 5.10 It was initially anticipated that formal approval from each administering authority be sought early in 2017. However, the delays in getting the final approval from Government and the volume of work required to get approval from Full Council of all twelve administering authorities may mean that this is not possible. Any delay would impact on the proposed start date of April 2018.
- 5.11 The completed Joint Committee terms of reference and the Shareholder Agreement are required to be approved by NYCC's Full Council. At this stage it is highly unlikely that these documents will be finalised in time for the Full Council meeting in February 2017. Due to the local elections in May 2017 and the potential Member and committee representative changes, seeking approval at the Full Council meeting in July 2017 may be a more pragmatic approach than May 2017.
- 5.12 One alternative suggested by the Officer Operations Group is whether each administering authorities' Full Council could be asked to approve draft documents at the February 2017 meetings. Final approval could be delegated to the S151 Officer and Head of Legal Services.

5.13 Whichever route is decided upon, there will be a role for this Committee in terms of approval to recommend to Full Council.

5.14 Significant progress on all three workstreams is therefore dependent upon:

- the legal adviser appointments referred to in paragraph 5.5 being in place, expected by early December
- the approval process required by each of the BCPP administering authorities
- approval being received from Government.

6.0 CONCLUSIONS

6.1 The response to the initial pooling submission in February 2016 was well received by Government. The detailed response was submitted by the deadline of 15 July 2016 but a reply from Government has not yet been received.

6.2 Despite the lack of reply from Government, it is expected that it will still want pooling arrangements to be delivered. Workstreams have been created to progress arrangements, but activity has been limited due to the wish to avoid what may be unnecessary expenditure. In this context, the Member Steering Group and the Officer Operations Group continue to meet to progress matters.

6.3 A significant amount of work was undertaken on pulling together the submission for July, however a much greater amount of work lies ahead.

6.4 An update on any further progress will be provided to the Committee at its next meeting.

7.0 RECOMMENDATION

7.1 Members to note the contents of this report.

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14 November 2016

Background documents: None