

COMMITTEE: Pensions Committee	DATE: 24 February 2015	CLASSIFICATION: Unrestricted	REPORT NO.	AGENDA NO.
REPORT OF: Acting Corporate Director of Resources ORIGINATING OFFICER(S): Kevin Miles – Chief Accountant		TITLE: Investment in London LGPS Collective Investment Vehicle – Joint Committee Meeting 17th December 2014 Ward(s) affected: N/A		

1. SUMMARY

- 1.1 In an attempt to reduce pension fund administration costs, the creation of a London wide collective investment vehicle is being created through London Councils. The fund would allow pension fund investments to be pooled for the purpose of reducing fund manager's fees as a lower fee is charged the larger the investment.
- 1.2 At the moment, the scheme is in its early stages of development. This report summarises the business of a Pensions CIV Sectoral Joint Committee meeting on the 17th December 2014.
- 1.3 At the meeting, a further investment of £50,000 (in two instalments of £25,000) was requested to cover the set up costs of the CIV, plus an element of initial running costs. If the scheme is created as expected, the reduced management fees would more than offset these costs.
- 1.4 Any decisions to transfer pension fund investments to the Collective Investment Vehicle would need to be approved by this committee. The investments available within the Investment Vehicle would need to match the council's investment strategy.

2. DECISIONS REQUIRED

- 2.1 Members are recommended to agree the further investment of £50,000 into the CIV that will be used to contribute towards the setup and initial running costs of the fund.
- 2.2 Note the progress made to date in the creation of the CIV as outlined at the Pensions CIV Sectoral Joint Committee.

3. REASONS FOR DECISIONS

- 3.1 Members are being asked to agree that the Council continues to participate into the CIV scheme as it is expected that the improved bargaining power of the larger scheme will mean management fees for CIV investments will be significantly lower for the Council's pension scheme than at present. All but three London Boroughs have agreed to participate in the scheme. The three Boroughs that are not participating yet may join at a later date. The current CIV members would need to decide if late investors would be asked to pay a fee for late investing.

4. ALTERNATIVE OPTIONS

- 4.1 The theory of the CIV is that fund managers will charge a lower management fee on pooled investments managed. If the CIV investment proves to be a popular fund, then if the Tower Hamlets fund was outside the scheme it would not have the potential to benefit from economies of scale.
- 4.2 If the Pensions Committee did not approve the further payments totalling £50,000, this could mean that other Councils who have contributed £50,000 will question this Council's participation in the CIV.

5. BACKGROUND

- 5.1 A joint London Borough Pension Working Group initiative is looking at ways in which pension schemes can work together to get financial benefits and efficiencies of scale from joint working.
- 5.2 A pensions working group led by London Councils launched a Collective investment vehicle to enable London Boroughs to participate in a scheme of joint pension fund investing. It will be an Authorised Contractual Scheme (ACS). This scheme will require FCA (Financial Conduct Authority) approval – this approval is being sought. It is currently planned that the scheme will be launched in February 2015, though this date may slip to later in the year. Details of the proposed scheme are shown in the attached London Councils report.
- 5.3 This work is partly in response to the Government's review of Local Government Pension Schemes. Further Government announcements may be made to request more joint working by councils to reduce administration costs.
- 5.4 Tower Hamlets Council agreed to participate in the CIV at Full Council in 2014 following recommendation by Pension Committee and Cabinet. The Council has invested £1 capital in the scheme. If the investments available are in line with the pension investment strategy and will offer reduced costs to the fund. So far the organisers are interviewing potential fund managers. At least one of the pension fund managers, Legal and General is likely to be involved in the scheme from inception. Northern Trust has been appointed as the fund's custodian.
- 5.5 In theory, the Council could move an unlimited amount of its investments into the scheme if they were in line with the investment strategy and offered reduced fees. The Council pension scheme has around £1 billion of investments with annual management fees total around £2.3 million. Investments within the fund are likely to be unitised fund type investments.
- 5.6 To maximise the value of pension schemes, ways to reduce the volume of management fees charged to pension schemes are being explored. This Collective Investment Vehicle approach has been designed by London Councils as a way in which similar investment types within different London Boroughs can be combined to benefit from smaller fee charges. Fund manager's fees are based on the size of the fund and are based on a percentage of the amount managed. The larger the fund, the lower the percentage fee charged.

6 **PENSIONS CIV SECTORAL JOINT COMMITTEE**

- 6.1 London Councils held the first Pensions CIV Sectoral Joint Committee on 17th December 2014. Councillor Harrison attended on behalf of the Council following Pension Committee agreement that Cllr Harrison was to be the Council's first representative at these meetings.
- 6.2 The papers for the meeting are enclosed as an appendix. The initial business concerned the election of meeting Chairs, agreeing the terms of reference, an update on progress made in creating the CIV, a fund manager analysis of current London Borough funds, the procurement of managers to the CIV and the dates of future meetings.
- 6.3 **Terms of Reference** – draft terms of reference were tabled, they are included as the appendix to this report). The Pensions CIV Joint Committee will meet at least once a year and will appoint directors, auditors, agree the Articles of Association, Accounts and Annual Report. The report included the appointed Member representatives from each participating Borough.
- 6.4 **Background and Progress Update** - So far 30 London Councils have signed up to participate. Those London Boroughs who are not participating might sign up in future, but the terms will need to be agreed. The scheme might also admit non London based Councils in the future. If the non-participating authorities wish to invest in the future the terms of their admission would need to be agreed by the group.
- 6.5 **Governance** - The governance of the scheme was outlined – the intention is that the wishes and needs of the Boroughs are fulfilled (probably through an investment committee structure featuring experts from across the Boroughs), however the governance arrangements will need to be practical and follow best practice – the operation of these will need to be determined (i.e. how many representatives be at participating investment managers performance review meetings?). Robust systems of management will need to be put into place.
- 6.5 **FCA Regulated** - The scheme will be a Financial Conduct Authority (FCA) regulated UK domiciled Authorised Contractual Scheme (ACS). This requires the scheme to operate in a transparent manner and is likely to provide some international tax advantages (i.e. to increase recoverable tax where possible).
- 6.6 **Procurement arrangements** – Counsel advice is being sought to see if investment manager procurement can be conducted outside the OJEU procurement regime. Procurement arrangements will be critical to the operation of the scheme. The final legal advice will be reported back to this committee once known.
- 6.7 **CIV Budget** – So far, each participating Council has contributed £25,000 towards costs exploring the CIV proposal. Two further contributions totalling £50,000 for set up and initial business as usual costs have been proposed to contribute towards £1.73m of costs of the scheme up to April. At the time of writing, the request for the first £25,000 has been received. Committee members expressed some concerns on the escalation of the costs of setting up and running the CIV, but the organisers commented that costs would be more than offset by reductions in manager fees (likely to be in excess of £2.8m per paragraph 6.9). Organisers commented that investment manager fees were being negotiated

Comment [NA]: I think you need to state the year – is it April 2015?

down below those currently being charged. This Committee is asked to approve the further payment of £50,000 towards the CIV.

- 6.8 **Investment Manager Review** – The technical sub-group are reviewing existing London Borough pension fund investments to see if there are common investments, strategies and fund managers between funds.
- 6.9 The sub-group are liaising with 14 investment managers who control over £14.5bn of Borough assets. This will include Legal & General. An initial review has identified up to £9.9bn of investments with eleven managers that could potentially be combined by the launch of the CIV. Though still subject to negotiation, the management fee could on average be reduced by 20% (£2.8m per annum across the fund). LBTH's level of benefit will depend on how its current fee compares to the new fees proposed. There is an expectation of fund managers that they will publish full information on investments held to participating investors.
- 6.10 More precise estimates of savings will be known as the technical group continue discussions with fund managers. As active manager fees are higher than passive managers, active manager fees are likely to have savings potential. The CIV committee will report back as discussions continue. Any infrastructure investments will be considered later in the CIV establishment process after more straightforward asset mandates have been combined.
- 6.11 **Asset Services Procurement** – a report outlining how the CIV was procuring a custodian for the fund. Since the meeting in December, the appointment of Northern Trust has been announced. Northern Trust is an established custodian for Local Authority pension investments.
- 6.12 **Future meeting dates.** A list of proposed future meeting dates was circulated. The next meeting was planned for 25th February 2015.

7. COMMENTS OF THE CHIEF FINANCIAL OFFICER

- 7.1. The comments of the Corporate Director Resources have been incorporated into the report.

8. LEGAL COMMENTS

- 8.1 Regulation 11(3) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 requires the Council, as an administering authority, to invest fund money that is not needed immediately to make payments from the Pensions Fund. Regulation 11(1) requires the Council to have a policy in relation to its investments. The investment policy must be formulated with a view –
 - (a) to the advisability of investing money in a wide variety of investments; and
 - (b) to the suitability of particular investments and types of investments. The Council is also required to have a Statement of Investment Principles in accordance with regulation 12 (1) which covers the following matters:
 - (a) the types of investment to be held;
 - (b) the balance between different types of investments;
 - (c) risk, including the ways in which risks are to be measured and managed;
 - (d) the expected return on investments;
 - (e) the realisation of investments;

(f) the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments;

(g) the exercise of the rights (including voting rights) attaching to investments, if the authority has any such policy; and

(h) stock lending.

In accordance with Regulation 11(5), The Council is required to take proper advice at reasonable intervals about its investments and must consider such advice when taking any steps in relation to its investments.

8.2 It is desirable for the Council to take steps to reduce the costs of administering its pension fund. The proposal to create a Collective Investment Vehicle appears to be a viable way to achieve savings.

8.3 When deciding whether or not to proceed with the project, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty).

9. ONE TOWER HAMLETS CONSIDERATIONS

9.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance or reduction in management fees will reduce the contribution and increase the funds available for other corporate priorities.

9.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

10. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

10.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

11. RISK MANAGEMENT IMPLICATIONS

11.1 Any form of investment inevitably involves a degree of risk.

11.2 To minimise risk the Investment Panel attempts to achieve a diversified portfolio. Diversification relates to asset classes and management styles.

12. CRIME AND DISORDER REDUCTION IMPLICATIONS

12.1 There are no crime and disorder reduction implications arising from this report.

13. EFFICIENCY STATEMENT

13.1 The monitoring arrangement for the Pension Fund and the work of the Pension Fund Investment Panel should ensure that the Fund optimises the use of its resources in achieving the best returns for the Council and members of the Fund.

LOCAL GOVERNMENT ACT 1972 (AS AMENDED) SECTION 100D

LIST OF "BACKGROUND PAPERS" USED IN THE PREPARATION OF THIS REPORT

Brief description of "background papers"

***Name and telephone number of holder
And address where open to inspection***

Pensions CIV Sectoral Joint Committee agenda papers