

Report of the Director, West Yorkshire Pension Fund, to the meeting of Joint Advisory Group to be held on 25 July 2019

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Subject:

Northern LGPS

Summary statement:

In accordance with the guidance from Government, West Yorkshire Pension Fund (WYPF) together with Greater Manchester and Merseyside are working towards the creation of an investment pool, Northern LGPS (NLGPS).

This report sets out the progress in establishing the Northern LGPS (formerly the Northern Pool), covering:-

- Drafting the Northern LGPS Operating Agreement, including the Terms of Reference for the Joint Committee
- Procuring a joint custodian for all the assets of NLGPS
- Developing the GLIL Infrastructure vehicle (including FCA regulation to facilitate it becoming the national LGPS vehicle for infrastructure investment)
- Developing a joint private equity vehicle.

Recommendation and Reason for Recommendation

It is recommended that the Joint Advisory Group note the progress to date, and the response to the Ministry of Housing, Communities and Local Government on the limited informal consultation in respect of revised statutory guidance on investment pooling.

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1 Background

- 1.1 The Northern LGPS (NLGPS) partners are Merseyside, Greater Manchester and West Yorkshire Pension Funds, three large, cost effective Metropolitan funds. Individual funds will retain their current role of setting asset allocation and investment policy, and will delegate the implementation of that policy to the Joint Committee.
- 1.2 A Joint Committee will be formed which will have responsibility for ensuring the appropriate structure and resources are in place to implement the policy required by each fund, those resources to be provided by the three Funds. Staff will be employed by one fund, but will be seconded to act for the other funds where that is required.
- 1.3 The Joint Committee will consist of two Members appointed by each Fund plus a total of three trade union representatives. It will not have any direct involvement in the appointment of managers, or selection of investments. These matters will be fully delegated to professional officers. Its role will be to determine the asset class and risk profile, as well as whether management is internal or external, in accordance with the investment policy set by each fund.
- 1.4 The long term vision for the pool is to provide access to
 - a range of internal and externally managed listed assets at low cost
 - collective investment in alternatives, while building skill to enable cost reduction by increasing direct access
 - working arrangements with other pools where greater size may add value.
- 1.5 The investment philosophy is to maintain simple arrangements, with a relatively low number of managers, low manager and portfolio turnover, an increasing proportion of assets managed internally within the pool, with individual funds retaining the ability to select asset class, territory, and active or passive management.

2. Progress to Date

- 2.1 The programme for establishing the NLGPS consists of
 - Drafting the NLGPS Operating Agreement, including the Terms of Reference for the Joint Committee
 - Procuring a joint custodian for all the assets of the Pool
 - Developing the GLIL Infrastructure vehicle, including FCA regulation to facilitate it becoming the national LGPS vehicle for infrastructure investment
 - Developing a joint private equity vehicle.
- 2.2 The draft Operating Agreement was approved by the February Council meeting.
- 1.1 The NLGPS Shadow Joint Committee approved the appointment of a common custodian bank, Northern Trust, to provide custodial services for all funds in the pool. The appointment of a common custodian is a key strategic milestone in

setting up the NLGPS. It is anticipated that the assets of the Fund will be transferred to Northern Trust over the summer.

- 1.2 GLIL, a vehicle established to invest in infrastructure, is fully operational, regulated by the FCA, and is available to other Pools or individual funds to invest, thereby establishing a national solution for LGPS funds to increase commitments to infrastructure, the fourth pooling criterion.
- 1.3 A joint venture, NPEP, has been established to make private equity investments on a collective basis. The governance of this vehicle operates in a similar manner to the GLIL infrastructure vehicle, although there are no plans to obtain FCA approval, as we do not expect the demand from other funds for private equity.
- 1.4 Between the January and March meetings the decision was taken to change the name to Northern LGPS, which identifies the pool more clearly with the LGPS, and avoids any confusion which may derive from the use of pool in the name. None of the other seven have pool in their name.
- 1.5 At the Shadow Joint Committee meeting on 28 March Councillor Doughty (Merseyside Pension Fund) stood down as Chair, as he was not standing in the elections in May, and Councillor Ged Cooney (Greater Manchester Pension Fund) was elected Chair.
- 1.6 The latest report on performance and cost for the NLGPS from CEM Benchmarking was presented. CEM's universe of funds comprised 327 funds with total assets of £7.3 trillion (average £22 billion, median £6 billion). Analysis of the 2017/18 data indicates that the Northern LGPS remains low cost, and is in the lowest cost 25% of its peer group (which consists of 21 global pension funds ranging from £16 billion to £65 billion).
- 1.7 CEM noted that the NLGPS 5-year net value added was 0.7%. This was above the U.K. median of 0.3% and above the global median of 0.3%. On cost they reported that NLGPS investment cost was 45.4 bps [0.45%], below our benchmark cost of 50.6 bps [0.51%]. This demonstrates that NLGPS is low cost compared to its peers.
- 1.8 At the meeting on 16 May the Shadow NLGPS Committee received a pooling update report, a further report on performance and cost covering the appointment of Performance Evaluation Ltd as the common performance measurement provider, and a report on Responsible Investment.
- 1.9 The NLGPS website is now operational, and has current information on the pool (www.northernlgps.org).

3. Meeting the Four Criteria

- 3.1 Asset pools are required to achieve the benefits of scale, deliver strong governance and decision making, achieve reduced costs and excellent value for money, and achieve an improved capacity to invest in infrastructure. The Northern Pool has a clear plan to deliver on these criteria.

3.2 As reported at the last meeting, NLGPS submitted a report on progress to the Ministry for Housing, Communities and Local Government on 22 October. A formal response has not been received.

4. **Informal Consultation on Statutory Guidance on Pooling**

4.1 On 3 January 2019 MHCLG began an informal consultation on statutory guidance on pooling. This guidance differs considerably from the current guidance, and, if implemented, removes the criteria set in 2015, in particular the requirement to deliver improved value for money and lower costs. The NLGPS has submitted a response to the consultation, making it clear that while it fully supports the criteria set in 2015, many aspects of the revised guidance are at odds with elected Members' duties to local council tax payers, and would not achieve the policy objectives of asset pooling.

4.2 The key concerns raised in the response, Appendix A, are as follows:

- The removal of the Value For Money criterion from the latest draft guidance, seen as the whole point of LGPS investment reform
- The assertion that individual funds should be prepared to suffer an increase in their costs in order to benefit other funds in the pool, or the wider LGPS. This is clearly at odds with authorities' fiduciary duty in managing their fund
- In the same vein, the assertion that elected members owe duties to parties other than their own funds and relevant stakeholders (employers and scheme members) is also contrary to their fiduciary duties.
- The requirement for all pools to have a FCA regulated company. We view this as unnecessarily prescriptive and believe the guidance should instead make clear that FCA regulated activities should not be carried out without either authorisation or an appropriate exemption from authorisation; and
- More generally, there is no evidence given in the consultation as to why the prescriptive requirements of the new guidance are beneficial to stakeholders.

4.3 As the issues raised are so wide and far reaching, the opinion of Jason Coppel QC was obtained, and this was also submitted as part of the response on 28 March. The covering letter is attached as Appendix B, and the opinion as Appendix C.

4.4 Mr Coppel's conclusions are:-

- The draft guidance, if it were to be implemented, would be ultra vires the relevant statutory powers of the Secretary of State for Housing, Communities and Local Government ("the Secretary of State") as a result of it purporting to require administering authorities to appoint an FCA-regulated company to implement their investment strategy, and potentially to act contrary to their fiduciary and quasi-fiduciary duties.
- If implemented, the draft guidance would be open to challenge on grounds of having been preceded by an unlawful consultation.

- The additional costs purportedly required by the draft guidance fall within the so-called New Burdens Doctrine, and administering authorities have an enforceable legitimate expectation that these will be considered at the policy formulation stage, and met by the Secretary of State
- 4.5 The Chair of NLGPS, together with the two Vice Chairs met with the Minister on 3 April to discuss the issues raised. While the meeting was positive in tone, the Minister was not prepared to make any specific comments until the civil servants have considered the responses received, of which there are over 90.
- 4.6 Civil servants, who are meeting with all pools, met officers on 16 May. Discussions covered the NLGPS response to the consultation, the progress in developing performance and cost benchmarking for the NLGPS, and pool implementation to date.

Appendices

Appendix A	Northern Pool response to MHCLG
Appendix B	Covering letter to QC Opinion
Appendix C	QC Opinion