NORTHERN LGPS POOL

DRAFT STATUTORY GUIDANCE ON ASSET POOLING

JOINT ADVICE

The advice sought

1. We are instructed by Tameside Metropolitan Borough Council ("**Tameside**") to advise it and City of Bradford Borough Council ("**Bradford**") and Wirral Metropolitan Borough Council ("**Wirral**") on the legality of draft guidance - "*Local Government Pension Scheme: Statutory guidance on asset pooling*" ("**the draft guidance**") - issued by the Ministry of Housing, Communities and Local Government ("**MHLG**") for "*informal"* consultation on 3rd January 2019.

2. Our principal conclusions are as follows:

   (1) The draft guidance, if it were to be implemented, would be *ultra vires* the relevant statutory powers of the Secretary of State for Housing, Communities and Local Government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.

   (2) If implemented, the draft guidance would be open to challenge on grounds of having been preceded by an unlawful consultation.

   (3) The additional costs purportedly required by the draft guidance fall within the so-called New Burdens Doctrine, and administering authorities have an enforceable legitimate expectation that these will be considered at the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.

Background

3. Tameside is the administering authority for the Greater Manchester Pension Scheme; Bradford and Wirral are the administering authorities for, respectively, the West Yorkshire Pension Fund and the Merseyside Pension Fund. The three authorities have together established pooling arrangements as the Northern LGPS, pursuant to reforms introduced by central Government with a view to requiring pension funds within the Local Government Pension Scheme ("**LGPS**") to come together to create so-called British Wealth Funds, thereby reducing administrative costs and encouraging greater investment in infrastructure in the UK. Regulation 7(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (SI 2016/946) ("**the 2016 Regulations**") requires an LGPS administering authority to "*formulate an investment strategy which must be in accordance with guidance issued from time to time by the Secretary of State*" and this strategy must include, *inter alia*, the authority's approach to pooling investments (reg. 7(2)(d) - see further below).

4. The relevant guidance is the "*Local Government Pension Scheme: Investment Reform Criteria and Guidance"* (November 2015) ("**the 2015 Guidance**"), which laid down four criteria which pooling arrangements should satisfy. First, asset pools should achieve the benefits of scale, being at least £25bn in size - the Northern LGPS comfortably satisfies that criterion with funds of c.£45bn. Second, they should have strong governance and decision-making. Third, they should bring about reduced costs and excellent value for money. We understand that the three funds making up the Northern LGPS perform extremely well in keeping costs down, in comparison with their peers. Fourth, pooling arrangements should have an improved capacity to invest in infrastructure. Again, the Northern LGPS is a "*market leader*" in this regard.

5. Further guidance was issued by the Secretary of State in September 2016 pursuant to reg. 7(1) of the 2016 Regulations, namely, *Local Government Pension Scheme: Guidance on Preparing and Maintaining an Investment Strategy Statement (September 2016)* ("**the 2016 Guidance**").[1] The 2016 Guidance gave guidance on each of the elements of reg. 7(2) of the 2016 Regulations, including, at pp.7-8, on reg. 7(2)(d), where the pooling criteria in the 2015 Guidance were expressly incorporated by reference.

[1] The 2016 Guidance was replaced by *Local Government Pension Scheme: Guidance on Preparing and Maintaining an Investment Strategy Statement (July 2017)* ("**the 2017 Guidance**") following the Government's defeat in a judicial review (subsequently overturned by the Court of Appeal). The changes made by the 2017 Guidance are not material for present purposes.

6. The Department for Communities and Local Government (as it then was) required each LGPS administering authority to submit initial pooling proposals by February 2016 and refined proposals by July 2016, requirements with which the Northern LGPS complied. Since then, there has been regular correspondence between the Northern LGPS and what is now the MHCLG regarding the progress of implementation of the Northern LGPS's proposals. The Northern LGPS initially proposed that it would create an investment management company, wholly owned by the three funds, and compliant with the Alternative Investment Fund Manager Directive (Directive 2011/61/EU), which would be regulated by the Financial Conduct Authority ("**FCA**") and would manage all pool assets. However, further work led the Northern LGPS to conclude that the additional expense entailed by this option could not be justified and that the Northern LGPS would be better served by: (1) appointing an FCA-regulated common custodian for the funds in the Northern LGPS, thereby facilitating collective investments, and (2) establishing pooled vehicles for alternative (i.e. non-listed) assets, also FCA-regulated, as and when appropriate.

7. We note that to date the move towards the operation of a small number of LGPS pools, rather than c.90 individual LGPS funds, has been achieved almost entirely through Ministerial guidance and the voluntary exercise by administering authorities of the discretions conferred on them by legislation to give effect to the Secretary of State's aims. Although "*pooling*" is referred to in reg. 7(2)(d) of the 2016 Regulations, the term has no statutory definition.

8. Northern LGPS take the view that forming an FCA-regulated company is undesirable in its circumstances because, *inter alia*:

    (1) Under its current governance and investment structures, all of the funds held within the Northern LGPS are managed in accordance with all relevant financial services law (including, in particular, the Financial Services and Markets Act 2000 ("**FSMA**")).

    (2) As the Pool consists of only three funds, the existing professional staff of each investor are directly involved in all investment decision-making and this allows collective investments to be made via non-FCA regulated vehicles whilst remaining FSMA-compliant. Strategic oversight of the vehicles is provided via a joint committee structure. We are instructed that this approach has worked successfully for the Northern LGPS's private equity vehicle (NPEP) and its infrastructure vehicle (GLIL). Northern LGPS has

been advised that a similar structure could also be adopted for monitoring, appointing and removing managers of listed securities.

(3) The costs of establishing a new investment management company to hold funds, and obtaining the required FCA permissions for that company, are likely to be several million pounds, with an increase in annual management costs of as much as 0.03% p.a. (i.e. £10m to £15m p.a.). Northern LGPS considers that incurring these additional costs would be inconsistent with the fiduciary duty of its constituent administering authorities to manage the assets of members, employers and taxpayers in the most cost-effective way.

9. With submissions dated 22 October 2018, the Northern LGPS supplied MHCLG with an advice from Jason Coppel QC confirming that its approach to the establishment of an FCA-approved company was lawful and compliant with the 2015 Guidance.

10. Under cover of an email of 3 January 2019 from Teresa Clay, a MHCLG official, the Secretary of State has purported to consult on the draft guidance. The covering email stated, *inter alia*:

> *"…. we have been preparing new statutory guidance on LGPS asset pooling. This will set out the requirements on administering authorities, replacing previous guidance, and builds on previous Ministerial communications and guidance on investment strategies.*
>
> *We are now inviting views on the attached draft guidance…"*

11. The draft guidance states (so far as is material for present purposes):

> *"1.1 This guidance sets out the requirements on administering authorities in relation to the pooling of LGPS assets… It is made under the powers conferred on the Secretary of State by Regulation 7(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the 2016 Regulations). Administering authorities are required to act in accordance with it.*
>
> *1.2 This guidance replaces the section at pages 7 to 8 of Part 2 of Guidance for Preparing and Maintaining an Investment Strategy, issued in September 2016 and revised in July 2017, which deals with regulation 7(2)(d) of the 2016 Regulations. It also replaces Local Government Pension Scheme: Investment Reform Criteria and Guidance, issued in November 2015.*
> *…*
>
> ***3 Structure and scale***
> *3.1 All administering authorities must pool their assets in order to deliver the benefits of scale and collaboration. These include:*
> - *reduced investment costs without affecting gross risk-adjusted returns*

- *reduced costs for services such as custody, and for procurement*
- *strengthened governance and stewardship and dissemination of good practice*
- *greater investment management capacity and capability in the pool companies, including in private markets*
- *increased transparency on total investment management costs*
- *diversification of risk through providing access to a wider range of asset classes, including infrastructure investments*

3.2 In order to maximise the benefits of scale, pool members must appoint a pool company[2] *or companies to implement their investment strategies. This includes:*

- *the selection, appointment, dismissal and variation of terms of investment managers, whether internal or external*
- *the management of internally managed investments*
- *the provision and management of pool vehicles including pool funds*

It is for the pool companies to decide which investment managers to use for pool vehicles, including whether to use in-house or external management. …

3.3 Pool companies may be wholly owned by pool members as shareholders or may be procured and appointed by the pool members as clients.

3.4 A pool company must be a company regulated by the Financial Conduct Authority (FCA) with appropriate FCA permissions for regulated activities….
…" (emphasis added)

The legality of the draft guidance

Legal principles

12. The LGPS is established by regulations made pursuant to the Superannuation Act 1972 ("**the 1972 Act**") and now the Public Service Pensions Act 2013 ("**the 2013 Act**"). The principal regulations governing the current LGPS are the Local Government Pension Scheme Regulations 2013 (SI 2013/2356), made under the 1972 Act. The 2016 Regulations are made under s.1 of the 2013 Act.

13. Section 3(1) of the 2013 Act provides that Scheme regulations (i.e. those made under s. 1) "*may, subject to this Act, make such provision in relation to a scheme under section 1 as the responsible authority* [i.e. the Secretary of State] *considers appropriate*". The provision that may be made in regulations includes, in particular, provision as to any of the matters specified in Sch. 3 (s. 3(2)(a)). The matters listed in Sch. 3 to the 2013 Act include:

[2] Defined in §2.1 as: "*the Financial Conduct Authority (FCA) regulated company which undertakes selection, appointment, dismissal and variation of terms of investment managers, and provides and operates pool vehicles for pool members*".

"11 Pension funds (for schemes which have them).

This includes the administration, management … of any pension funds.

12 The administration and management of the scheme, including—

(a) the giving of guidance or directions by the responsible authority to the scheme manager (where those persons are different); …"

14. Section 21 of the 2013 Act makes provision in relation to consultation before scheme regulations are made and provides that:

"(1) Before making scheme regulations the responsible authority must consult such persons (or representatives of such persons) as appear to the authority likely to be affected by them.

(2) The responsible authority must publish a statement indicating the persons that the authority would normally expect to consult under subsection (1) (and keep the statement up-to-date)."

15. Regulation 7 of the 2016 Regulations provides, in material part, that:

*"**7. Investment strategy statement***
(1) An authority must, after taking proper advice, formulate an investment strategy which must be in accordance with guidance issued from time to time by the Secretary of State.

(2) The authority's investment strategy must include—

(a) a requirement to invest fund money in a wide variety of investments;

(b) the authority's assessment of the suitability of particular investments and types of investments;

(c) the authority's approach to risk, including the ways in which risks are to be assessed and managed;

(d) the authority's approach to pooling investments, including the use of collective investment vehicles and shared services;

(e) the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and

(f) the authority's policy on the exercise of the rights (including voting rights) attaching to investments.

(5) The authority must consult such persons as it considers appropriate as to the proposed contents of its investment strategy. …." (emphasis added)

16. Regulation 8(1) gives the Secretary of State power to impose directions on an administering authority. It provides, in material part, that:

> *"**8. Directions by the Secretary of State***
> *(1) This regulation applies in relation to an authority's investment functions under these Regulations and the 2013 Regulations if the Secretary of State is satisfied that the authority is failing to act in accordance with guidance issued under regulation 7(1)."*

17. Before exercising the power under reg. 8(1) the Secretary of State must consult with the administering authority (reg. 8(3)). The directions that the Secretary of State may make are set out in reg. 8(2) and range from requiring the authority to change its investment strategy to directing that its investment functions be exercised by the Secretary of State or a person nominated by him.

18. The relevant principles in relation to guidance issued by a Secretary of State may be summarised as follows. *First*, guidance is different from a direction. Guidance that amounts to a direction will be unlawful. Thus in ***Laker Airways Ltd v Department of Trade*** [1977] QB 643, 714 at 724-725 Lawton LJ held that:

> *"The Secretary of State was empowered to give guidance with respect to the performance of its functions. The Authority had a statutory duty to perform its functions in such manner as it considered was in accordance with the guidance for the time being given to it. The statutory word is "guidance," not "direction." The Secretary of State can point out the way to be followed. He can tell the Authority what policy is to be applied in the performance of its functions. The Authority is left to decide how to carry out the policy. … The two words are so different. The word "guidance" has the implication of leading, pointing the way, whereas "direction" even today echoes its Latin root of regere, to rule. When the Secretary of State exercises his statutory powers to direct he does indeed rule. He is in command: he is more than a guide."*

In that case the Civil Aviation Authority ("**CAA**") was required by s. 3(1) of the Civil Aviation Act 1971 ("**the CAA 1971**") to perform its functions in the manner best calculated to secure the general objectives set out in s. 3(1)(a)-(d), subject to any current "*guidance*" given by the Secretary of State (ss .3(2)-(3)). Pursuant to s. 4 the Secretary of State had wide powers to "*give directions*" to the CAA in the national interest in circumstances specified in the section. The Secretary of State issued "*guidance*" that effectively amounted to an instruction to the CAA. The Court of Appeal held that the Secretary of State had acted *ultra vires* in issuing the purported guidance. He was entitled to reverse the policy embodied in s. 3(1)(b) of the CAA 1971, but could only do so by legislation.

19. More recently in ***R (Alvi) v Secretary of State for the Home Department*** [2012] UKSC 33, [2012] 1 WLR 2208, Lord Clarke at [120] held that:

> *"It seems to me that, as a matter of ordinary language, there is a clear distinction between guidance and a rule. Guidance is advisory in character; it assists the decision maker but does not compel a particular outcome. By contrast a rule is mandatory in nature; it compels the decision maker to reach a particular result."*

Section 3(2) of the Immigration Act 1971 requires to be laid before Parliament statements of the rules and of any changes to the rules as to the practice to be followed in the administration of the Act for regulating entry into, and stay in, the UK. The principal issue in that case was whether a code of practice that was referred to in the Immigration Rules as setting out criteria that were to be satisfied itself constituted rules. The code had not been laid before Parliament. The Supreme Court held that s. 3(2) applied to the code and that its requirements had not been satisfied.

20. *Second*, guidance issued by a government department (just as with any statement of policy) may not be over-rigid – it must retain sufficient flexibility (see, e.g., ***R v Secretary of State for the Home Department, ex p Venables*** [1998] AC 407, per Lord Browne-Wilkinson at 496-497). Courts are likely to construe strictly and narrowly a purported power to make rigid guidance (see ***R v Herrod, ex p Leeds City DC*** [1976] QB 540, per Lord Denning MR at 559-560). *Third,* statements of policy or guidance may not reverse or contradict the purpose of the relevant statute (see, e.g., ***R (Girling) v Parole Board*** [2006] EWCA Civ 1779, [2007] QB 783, per Sir Anthony Clarke MR at [20-23]).

Analysis

21. In our view, there are a number of respects in which the draft guidance, were it to be implemented, would be *ultra vires* the Secretary of State's powers under the 2013 Act and the 2016 Regulations. *First*, the draft guidance purports to be guidance but it contains, in key respects particularly in relation to the need for a FCA-regulated company, *directions* as to how administering authorities are to engage in pooling. We have set out above a number of passages from the draft guidance, which are couched in plainly mandatory terms using the word "*must*" and being stated to be "*requirements*". It is very hard to read these passages as doing anything other than purporting to *direct* administering authorities to do a particular thing, namely appoint an FCA-regulated company.

22. In our view, the requirement in reg. 7(1) of the 2016 Regulations that a local authority must formulate an investment strategy which is in accordance with guidance issued by the Secretary of State does not justify guidance which purports to instruct rather than to guide. An authority acts in accordance with guidance where it has due regard to that guidance and carefully considers whether or not to follow the guidance given, but an authority does not act in accordance with guidance only if it rigidly complies with what is stated in that guidance. That must be correct because otherwise the Secretary of State would be arrogating a power to make what would be, in effect, mandatory regulations by means of issuing guidance, but without the procedural safeguards which apply to the making of regulations.

23. Nor can the issuing of guidance purport to replicate or supersede the power of the Secretary of State in reg. 8 of the 2016 Regulations to give directions to administering authorities. That power can only be exercised if there has been a failure to act in accordance with guidance. That is not, of course, what has happened in the present case, but the very existence of the power to give directions tends against any attempt by the Secretary of State to compel action by administering authorities through the issuance of guidance.

24. *Second*, applying the principles set out at §20 above, to the extent that the guidance requiring the formation or appointment of an FCA-approved company could be said to be guidance rather than a direction, it is overly rigid. The draft guidance does not suggest any flexibility in this respect (even if the desiderata set out in, e.g., §3.1 can (in a particular case) be achieved by other means (as Northern LGPS contend is the case)). If the Secretary of State's concern is with pools containing a number of members resulting in either inefficient decision-making or else members unlawfully engaging in regulated investment activity in respect of each other, then there is an obvious way of addressing those issues in a flexible and proportionate way (for example, to impose an FCA-approved company requirement if there are more than, say, 5 members of the pool, where it can realistically be said that the membership is too large for effective joint control).

25. *Third*, the draft guidance cuts across the statutory scheme. The LGPS operates on the basis that is for administering authorities to administer their pension funds. This is clear from the 2013 Regulations. Further, reg. 7 of the 2016 Regulations does not contradict that principle - the regulation concerns the investment strategy *of the administering authority*. Regulation 7(2) sets out what the administering authority much include in *its* investment strategy. The discretion as to how to set that strategy compliant with reg.7(2) remains with the administering authority,

albeit acting in accordance with the Secretary of State's guidance. Such guidance cannot purport to remove the discretion of the administering authority.

26. This analysis is supported by consideration of the policy behind the 2016 Regulations and 2015 Guidance. There is nothing in the explanatory note or explanatory memorandum that suggests that the 2016 Regulations were intended to allow the Secretary of State to place prescriptive requirements on administering authorities as to how they exercise their powers. Indeed, the DCLG's consultation response document on the 2016 Regulations and the 2015 Guidance (*Local Government Pension Scheme: Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009: Government response to the Consultation (September 2016))* makes clear that this package was intended to introduce a *less* prescriptive, deregulated regime (see, e.g., at §§2, 5, 7 (response to Qs.1, 7 and on Part C)).

27. *Fourth*, the draft guidance has the effect of potentially requiring an administering authority to act contrary to what it reasonably considers to be its fiduciary duty. It is generally accepted that an administering authority has a fiduciary duty to the members and beneficiaries of its pension fund. A local authority also has a quasi-fiduciary duty to Council Tax-payers when spending public money (see ***Roberts v Hopwood*** [1925] AC 578, per Lord Atkinson at 595-596). In the present case Northern LGPS has come to the considered view that, in the circumstances of <u>its</u> case, the formation or appointment of a FCA-regulated company would involve unnecessary and unjustified expenditure that would be in breach of its fiduciary or quasi-fiduciary duties. The draft guidance, however, purports nonetheless to require the appointment or formation of such a company. Whilst the Secretary of State may by legislation override such non-statutory duties, it would be unlawful for him to issue guidance that purported to require administering authorities to act contrary to such duties.[3]

28. In our view, the Courts would conclude that, if issued in its current form, the draft guidance was *ultra vires* the Secretary of State's powers. To achieve what the Secretary of State appears to wish to achieve, it would be necessary for him to do so by making regulations (with the attendant requirements in terms of consultation and Parliamentary scrutiny).

<u>The legality of the consultation</u>

[3] We also note, as an aside, that other aspects of the draft guidance can be said to be contrary to the fiduciary and/or quasi-fiduciary duties of administering authorities. In particular, the suggestion at §4.4 that members of Pension Committees and equivalent governance bodies have a duty to "*take account of the benefits … across the scheme as a whole*" is misconceived – there is no such duty beyond their own fund and the Secretary of State would need legislation to impose one.

29. The Secretary of State has chosen to consult with "*interested parties only, including the Scheme Advisory Board, Pensions Committees, Local Pension Boards, the pool Joint Committees or equivalent, the Cross Pool Collaboration Group, the pool operating companies where owned by participating funds, CIPFA and ALATS*".

30. A duty on a decision-maker to consult certain persons may arise where: (1) there is an express or implied statutory obligation to do so: (2) where there is a legitimate expectation arising either from an express representation to do so or past practice of consulting; or (3) where the individuals concerned have an interest in the benefit in question that is sufficient to found a legitimate expectation of consultation (see ***R (Bhatt Murphy) v Independent Assessor*** [2008] EWCA Civ 755, per Laws LJ at [49-50]). Even if there is no legal requirement to conduct a consultation, "*if it is embarked upon it must be carried out properly*" (***R v North and East Devon Health Authority, ex p Coughlan*** [2001] QB 213, per Lord Woolf MR at [108]). In other words, if the choice is made to consult, the consultation must be fair (see ***R (Capenhurst) v Leicester City Council*** [2004] EWHC 2124 (Admin), (2004) 7 CCL Rep 557, per Silber J at [44]).

31. In the present case there is no express statutory duty to consult any particular person before issuing guidance, nor (as far as we are aware) has there been any express promise to consult any particular persons before doing so. Nor do we consider that this a case falling within the third, exceptional category where a duty to consult may arise. However, in our view, the Secretary of State's "*informal*" consultation is open to challenge on two related bases.

32. *First*, during the development of policy on pooling the Secretary of State has previously consulted widely through formal, public consultation. The 2015 Guidance was issued following the May 2014 consultation, *Local Government Pension Scheme: Opportunities for collaboration, cost savings and efficiencies*. That in turn led to the consultation in November 2015, *Local Government Pension Scheme: Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009*, on the draft 2016 Regulations and the 2016 Guidance (which the Secretary of State has accepted were consulted upon together as a package – see ***R (Palestine Solidarity Campaign Ltd) v Secretary of State for Communities and Local Government*** [2018] EWCA Civ 1284, [2019] 1 WLR 376, per Sir Stephen Richards at [11]). Again, the Secretary of State conducted a public consultation (which, indeed, received over 23,000 responses).

33. The draft guidance involves a significant departure from the 2015 Guidance (and the 2016 Guidance) and, in our view, the Secretary of State's past practice in respect of consultation is sufficient to found a legitimate expectation that significant changes of approach would be subject to consultation on a similar basis. We note that there would be no need for a challenger to demonstrate a uniform practice of public consultation: "*While a practice does not have to be unbroken, it has to be sufficiently consistent to be regarded as more than an occasional voluntary act*" (***R (BAPIO Action Ltd) v Secretary of State for the Home Department*** [2007] EWCA Civ 1139, per Sedley LJ at [39]). Applying that test, we consider that the past practice in this case is sufficiently consistent.

34. *Second*, whether or not the Secretary of State was under a legal obligation to consult on the draft guidance, he chose to do so but – unfairly it would be argued – failed to consult with, *inter alia*: (1) individual administering authorities (although we recognise that they may have been alerted to the consultation by their pool Joint Committees); (2) employing authorities; (3) local government trades unions; (4) active, deferred or pensioner members of the LGPS; or (5) council taxpayers (i.e. the general public). Given, in particular, the potential costs involved in setting up and operating an FCA-regulated company, all of the above groups may be affected by the implementation of the draft guidance to varying degrees. Even if (contrary to our analysis above) the draft guidance would not be *ultra vires*, it is at the most prescriptive fringes of what could properly be regarded as guidance. Were the Secretary of State to implement the proposals by way of regulation there would be a statutory duty on him to consult with those that appear to him may be affected. Those factors support the view that the consultation which the Secretary of State chose to undertake was unfairly narrow.

35. We would also note that should judicial review proceedings be commenced, it would also be for the Secretary of State to demonstrate through evidence that his consultation was conducted whilst his policy was at a formative stage (in circumstances where the MHCLG appears to have been committed to this course for some time) and that adequate reasons for the proposal were advanced (in circumstances where no explanation at all was provided for the draft guidance). These well-known conditions of a lawful consultation (see ***R (Moseley) v London Borough of Haringey*** [2014] UKSC 56, [2014] 1 WLR 3947, per Lord Wilson at [25]) might also provide fertile grounds for challenge.

Compliance with the New Burdens Doctrine

36. "*New burdens doctrine: Guidance for government departments*" ("**NBD**") was promulgated by the Coalition Government in June 2011. It states, *inter alia*:

> *"1.2… [T]he Cabinet has agreed that* ***all new burdens on local authorities must be properly assessed and fully funded by the relevant department****…*
> *…*
> *2.1 To ensure that* ***the pressure on council tax is kept down****, the* ***net additional cost*** *of all new burdens placed on local authorities … by central Government must be assessed and* ***fully and properly funded****.*
> *…*
> *2.5 Broadly, a new burden is defined as* ***any policy or initiative which increases the cost of providing local authority services****. This includes duties, powers, or any other changes which may place an expectation on local authorities, <u>including new guidance</u>.*
> *…*
> *2.7 The new burdens doctrine* ***only applies where central government requires or exhorts authorities*** *to do something new or additional...*
> *…*
> *3.1 A burden will arise where* ***new powers/duties/<u>expectations</u>*** *could lead to authorities having to increase spending. …*
>
> *3.2 Nor do new burdens result only from new legislation: they can arise from authorities being asked to* ***exercise existing powers and functions in new ways****, e.g. in new guidance. If it is the Government's policy that authorities should do something and that this will cost them more money, the department responsible for the policy must ensure that the necessary funding is provided….*
> *…*
> *5.14* ***It is important to remember that these rules concern the impact of policies on council tax in each individual year****. Departments cannot argue that short term costs will be offset against long term savings. Short term costs are generally quantifiable, as is the impact on council budgets once implementation begins. The savings are often longer term.* ***Only specific identified cost savings (rather than vague, non-specific, or unquantifiable savings) can be offset against identified costs*** *and this should be on a year-by-year basis (so longer term cost savings could reduce a new burden over time)."* (bold emphasis in the original; underlined emphasis added)

37. A legitimate expectation will arise where there has been a clear promise or a settled practice which engenders an expected (procedural or substantive) advantage. A promise must be "*clear, unambiguous and devoid of relevant qualifications"* (see ***R v Inland Revenue Commissioners, ex p MFK Underwriting Agents Ltd*** [1990] 1 WLR 1545, per Bingham LJ at 1569; ***R (Bancoult) v Secretary of State for Foreign and Commonwealth Affairs (No.2)*** [2008] UKHL 61, [2009] 1 AC 453, per Lord Hoffmann at [60]).

38. In ***R (Liverpool City Council & others) v Secretary of State for Health*** [2017] EWHC 986 (Admin), [2017] PTSR 1564, local authorities challenged the Secretary of State's failure to provide sufficient funds to enable them to meet the costs of complying with their statutory

responsibilities under the Mental Capacity Act 2005 following the Supreme Court's judgment in ***Cheshire West and Chester Council v P*** [2014] UKSC 19, [2014] AC 896. They claimed that that failure was in breach of their legitimate expectations created by the NBD. Garnham J dismissed the challenge on grounds of delay but also held that the NBD established no legitimate expectation that local authorities would receive funding to meet extra costs resulting from a court judgment because there was no clear and unambiguous representation to that effect (see at [74-76]). However, where an additional financial burden upon a local authority does fall within the scope of the NBD, the ***Liverpool*** case is consistent with the proposition that the NBD will create enforceable substantive legitimate expectations on the part of local authorities that it will be complied with.

39. In the present case the draft guidance purports to require the establishment of an FCA-regulated company. That clearly carries with it a significant one-off start-up cost and additional ongoing costs. The Northern LGPS authorities estimate these costs as running to several million pounds. Benefits under the LGPS are fixed by legislation (i.e. the 2013 Regulations). Ultimately, the only sustainable basis on which ongoing increases in the cost of administering the LGPS can be met is by increasing employer contributions, at direct cost to local authorities. In our view, the FCA-regulated company requirement in the draft guidance would engage the NBD. That is notwithstanding that these additional costs would be incurred as a result of mere guidance, rather than legislation (see at §§2.5 and 2.7). Nor is it any answer to say that there may be offsetting benefits in the future (see at §5.14).

40. In our view, the draft guidance falls squarely within the scope of the NBD and, if that guidance were to be implemented there would be an enforceable legitimate expectation on the part of administering authorities that the MHCLG would fund the extra costs of the requirement for an FCA-regulated company. Indeed, there may already have been a breach of the NBD as a result of the requirement that such costs will be considered at the policy formulation stage (see NBD, chapter 5).

Conclusions

41. In summary, therefore, our conclusions are:

    (1) The draft guidance, if it were to be implemented, would be *ultra vires* the relevant statutory powers of 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.

(2) If implemented, the draft guidance would be open to challenge on grounds of having been preceded by an unlawful consultation.

(3) The additional costs purportedly required by the draft guidance fall within the NBD, and administering authorities have an enforceable legitimate expectation that they will be considered at the policy formulation stage, and met by the Secretary of State.

42. If we can be of any further assistance, our Instructing Solicitors should not hesitate to contact us.

JASON COPPEL QC

JAMES CORNWELL

11KBW,
11 King's Bench Walk,
Temple,
London EC4Y 7EQ

28th March 2019