

COLLABORATIVE WORKING WITH OTHER LOCAL GOVERNMENT PENSION FUNDS

Responsible Officer Justin Bridges

e-mail: justin.bridges@shropshire.gov.uk

Tel: (01743)
252072

Fax (01743)
255901

1. Summary

- 1.1 This report informs the Committee of discussions that have been taking place with other Local Government Pension Scheme (LGPS) Administering Authorities, and to seek delegated authority to continue this work.
- 1.2 The report also provides an update to Members on the wider national position in respect of collaboration within the LGPS, and in particular the potential impact of an announcement contained within the Summer Budget.

2. Recommendations

- 2.1 Members note the position as set out in the report.
- 2.2 Members delegate authority to the Head of Finance Governance & Assurance in consultation with the Chairman if necessary to conclude the matter of joint procurement of a passive investment manager with other LGPS administering authorities.

REPORT

3. Risk Assessment and Opportunities Appraisal

- 3.1 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998.
- 3.2 There are no direct environmental, equalities or climate change consequences arising from this report.

4. Financial Implications

- 4.1 There are no financial implications to consider in this report at this stage but it is expected that the procurement exercise will result in investment management fee savings to the Fund.

5. Background

- 5.1 Members will be aware that in May 2013 the Local Government Minister made clear in a speech that the structure of the LGPS was being considered, with Fund mergers a possibility for consideration. This speech was followed by a 'Call for Evidence' consultation that focused on the management of deficits and investment efficiency.
- 5.2 In May 2014, and following analysis of the responses received from the Call for Evidence, a further round of consultation was launched. This consultation ruled out forced Fund mergers in the near term and focussed on the possibility of asset pooling (possible via the formation of a small number of Common Investment Vehicles) and the increased use of passive management, both of which were thought to offer potentially significant savings in investment management fees across the LGPS.
- 5.3 The Summer Budget of July 2015 contained the following announcement:
- “The government will work with the Local Government Pension Scheme administering authorities to ensure that they pool investments to significantly reduce costs, while maintaining overall investment performance. The government will invite local authorities to come forward with their own proposals to meet common criteria for delivering savings. A consultation to be published later this year will set out those detailed criteria as well as backstop legislation which will ensure that those administering authorities that do not come forward with sufficiently ambitious proposals are required to pool investments.”
- 5.4 The consultation referred to in the Budget has not yet been issued, and there is no set date for when it will be issued but it is likely to be expected in mid-November 2015. What is clear is that the Government will need to see significant efforts by the LGPS to reduce running costs (and especially investment management fees), or it will legislate to ensure that this happens.

6 Current collaborative working with other Funds

- 6.1 For a number of months now, and preceding the Summer Budget announcement, the Shropshire County Pension Fund has been in discussions with 6 other Administering Authorities about the possibility of a joint procurement of passive investment management. This work was started by the Cheshire and Staffordshire Funds and the 7 Funds now involved appear to have sufficient 'critical mass' to be able to jointly procure passive investment management services at a cost that is significantly lower than the individual Funds are currently paying.

- 6.2 When it became apparent that the discussions had reached a point at which action seemed the likely outcome, the Head of Finance Governance & Assurance (Scheme Administrator) was involved on a conference call with all the other Funds involved. The Chairman of the Pension Committee has also recently been advised of the discussions which have taken place to date.
- 6.3 A meeting of 6 of the Funds was held on 14 August 2015 (the 7th Fund was unavailable due to other commitments), and the discussions were extremely encouraging. There was a clear common goal and willingness to proceed in a timely manner and the group was able to agree every point of importance. There was agreement of the need to appoint an investment consultant to carry out work in respect of the optimal outcome for the group, and five consultants have been approached to put forward submissions for how they would carry out this work. By the date of this meeting the investment consultant will either have been selected by the group, or the appointment will be very close.
- 6.4 The 7 Funds believe that they have sufficient assets to ensure that the investment management fees achieved will be extremely attractive. Other Funds will be welcomed if they want to join and do not slow down the timetable, but having more assets is likely to have almost insignificant impact onto the level of fees that can be achieved. It is hoped that the whole process, including restructuring any assets that will require transferring between investment managers, will be completed before the end of October 2015. This timetable is ambitious but it is believed that it can be achieved.
- 6.5 The outcome of the joint procurement will almost undoubtedly be that all Funds involved will have the same passive investment manager, as opposed to the four different ones that are currently used. It is expected that the appointed manager will be able to provide pooled funds that replicate the indices that are already used by the individual funds, although there is a willingness on the part of the Funds to make slight revisions to their benchmarks if this is beneficial.
- 6.6 It is difficult to be specific about the likely fee savings in advance of the procurement, but informal discussions between Cheshire, Staffordshire and Shropshire and some of the potential managers suggest that they will be worthwhile. Passive management fees are low in comparison to those charged by active managers, but it seems likely that a reduction of fees will be achievable for all Funds involved.
- 6.7 In reality if like-minded LGPS Funds cannot work collaboratively on a joint procurement for a passive manager, there is little hope for collaboration in other areas. In order to allow smooth progress towards the joint appointment I believe that it is impractical to seek the approval of the Committee of the appointment of a passive investment manager within this exercise. As a result, it is recommended that this matter is delegated to the Head of Finance Governance & Assurance, who will consult with the Chairman on all

matters of importance. There is the possibility that the successful investment manager will be the Shropshire Fund's incumbent passive manager (Legal & General), in which case no action other than the signing of a new fee agreement will be necessary.

7 National Collaboration

- 7.1 The Summer Budget announcement made it clear that the Government wants to see clear action on the part of the LGPS to bring about lower running costs, whilst maintaining investment management performance. It has been clearly articulated by and to those who are closest to the process that the savings are expected to be significant. A couple of Funds working together to negotiate better fees with their managers will save money, but does not get close to the 'sufficiently ambitious' requirement of the announcement.
- 7.2 On the 21 August a meeting was held at the Local Government Association headquarters to which all LGPS Funds were invited to attend. The meeting was held under Chatham House Rules, so it is difficult to be overly detailed about the discussions that took place but it does appear highly likely that an outcome that involves a number of formal asset pools (involving potential geographical or asset class groupings) will be the Government's favoured option. The expectation is that these asset pools will have to be significant in size, with £20 billion - £40 billion being mentioned as the optimal size. There is a probability that there will be limited ability for Funds to invest outside these asset pools.
- 7.3 There is an expectation of action within the terms of this Parliament, but an acceptance that it is necessary to get an optimal (rather than speedy) outcome. A period of 3 years before the asset pools become active appears to be likely. There appears to be a broad consensus amongst the Funds that collaborative working and leveraging the size of the LGPS is sensible, but there are differing views about how best to do this. Bringing together the disparate views into a workable solution that is a better option for everyone rather than the 'backstop legislation' referred to in the Budget Announcement will be challenging.
- 7.4 It is expected that the forthcoming consultation will account for each LGPS Fund being able to decide its own asset allocation, however it does seem likely that some freedoms will have to be sacrificed by individual Funds if the scale of savings is likely to be sufficient to satisfy the Government. What is clear is that the Government see the LGPS as a single entity, and not 89 individual Funds, and that it will not be left to individual Funds to produce savings on a stand-alone basis.
- 7.5 It remains clear that changes need to be implemented at an LGPS wide level, and that resources need to be made available in order to ensure that suitable progress is made. Although with limited resources Shropshire intends to play an active role in this process and it is considered important that the Fund's views are heard and

taken into account. Members will be updated further on any other developments when they become clearer over the coming months.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

Call For Evidence Response September 2013 & LGPS Consultation Response July 2014.

Cabinet Member

N/A

Local Member

N/A

Appendices

N/A