Brent	**Brent Pension Fund Sub-Committee** 18 November 2014 **Report from the Chief Finance Officer**
For Action	Wards Affected: ALL
London pension fund collaboration	

1. SUMMARY

1.1 This is an update on the voluntary collective investment vehicle (CIV) which is being developed by the London Leaders. The CIV aims both to achieve lower investment management fees and potentially improve investment performance without the loss of operational independence in terms of asset allocation policy (which a merger of funds would imply). The London CIV has moved from an exploratory stage into the technical process of deciding upon, and creating, the most appropriate structure.

1.2 Some 30 out of 33 London boroughs and councils are participating. They have each paid £25,000 for the exploratory stage, and most of this money has been spent on external technical services, to tackle the legal, regulatory, and other aspects of the CIV.

2. RECOMMENDATION

2.1 Members are asked to support the ongoing establishment of a collective investment vehicle (CIV) and delegate authority to the Chief Finance Officer to approve a further £50,000 expenditure relating to the set up costs of the CIV, with one tarnche of £25,000 being requested now, and one more in April 2016.

3. DETAIL

3.1 A CIV is a structure which would harness the joint purchasing power of the participating boroughs. It should be stressed that participation by boroughs in the CIV will be voluntary and boroughs would retain their autonomy in asset allocation and funding strategy. The CIV is built entirely on attraction. The CIV will provide boroughs with cheaper access to high quality funds within each asset class, and also do the “heavy lifting” in terms of monitoring and compliance, thus eliminating widely duplicated efforts across London boroughs. Fund managers are attracted by having “one client” in terms of reporting and hence save marketing resources. The prospect of economies of scale for both the providers and customers of fund management services sells itself.

3.2 The vast majority of authorities are in favour of creating a CIV. Some 30 of the 33 London schemes have contributed £25,000 towards meeting the cost of creating such a London-wide vehicle. In the longer term, costs incurred in operating the CIV would be recoverable from participating boroughs which would be more than paid for from reduced fees.

3.3 Fund managers (without whom the CIV could not function) are keen to be put onto the CIV structure, as they see the benefits accruing to them. The firm levels of indicated demand provide reassurance that the projected fee reductions will be realised.

3.4 It is possible to estimate the recurring cost savings from participation in the CIV, on account of the reduction in fund management fees. The working assumption, based on initial indications, is that fees will be some 20% lower once funds are migrated to the CIV, although the first wave of formal interviews has yet to commence. For the sake of calculations, it is assumed that index trackers (passive) investments will be in the first wave to go on to the CIV. The Baillie Gifford Diversified Growth fund is also likely to go onto the CIV. Lastly, the example also includes the Henderson Total Return Bond Fund. The data shows the projected cost saving both including and excluding Henderson:

Savings excluding Henderson TR Bond Fund				
Fund Manager	**Product**	**AMC (Fee) £**	**Estimated Savings (%)**	**Estimated Savings (£)**
Baillie Gifford	Diversified Growth	220,316	20%	44,063
L&G	Global Equity Tracker	130,640	20%	26,128
L&G	UK Equity Tracker	45,461	20%	9,092
Total Savings per annum				**79,283**
Savings excluding Henderson TR Bond Fund				
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Hendersons	Total Return Bond Fund	325,181	20%	65,036
Total Savings per annum				**100,256**

3.5 It is anticipated that the reduction in fees will be greater as more asset classes and fund managers come onto the CIV, and as the Brent Pension Fund portfolio changes, provided that the desired fund managers are on the CIV.

3.6 The benefits of participating in the CIV are extended to non-pecuniary issues. Better monitoring and oversight will reduce the (duplicated) workload of Pension Fund officers, and in time, give access to new opportunities in unlisted investments, such as infrastructure. Overall governance is expected to be boosted from the outset.

3.7 The development of the CIV structure has gone far beyond the original idea of "exploring the proposal", as Mayor Jules Pipe's letter put it. The ongoing development of the operating model has required the use of outside expertise. Although simple in concept, there is a raft of issues to consider and work through, before the final structure is submitted to the FCA.

3.8 The first payment of £25,000 paid by the 30 participating boroughs has enabled many of the conceptual issues to be resolved. Some £479,000 of the £750,000 raised has been spent. Boroughs are requested to submit another payment of £25,000, in order to pay for the ongoing technical and legal advice which must be outsourced, as well as to pay for the recruitment and remuneration of the CIV's management and non-executive board members, who must be *in situ* before the final version of the structure is submitted to the FCA. The costs for the CIV are therefore front-loaded. The next payment is not anticipated until April 2016, one year after the current projected launch date in April 2015. (The launch date is subject to FCA approval and other external factors).

4. BACKGROUND

4.1 The London Leaders and Society of London Treasurers have been comparing a range of options for closer pension fund collaboration in terms of their impact and practicality. The preferred option is a CIV that operates on a voluntary basis. The proposal is that the CIV will be a bridge between individual schemes and fund managers. The CIV will identify and monitor one or more fund managers for each asset class, agreeing fees. Individual schemes such as Brent would then be able to opt into those arrangements.

4.2 The advantage of a CIV compared with merger is that there will be no change to the Brent fund structure and the Sub-Committee will retain local decision making in the setting of investment and funding strategies. The additional available choice will be that when it comes to manager selection, Brent will be able to use the managers selected to manage the CIV. Monitoring of fund managers and decisions to de-select would continue to be undertaken by Brent. With additional resources and a larger mandate, the hope is that a CIV would result in improved investment performance (which is debatable) and lower fees (a more reasonable expectation).

4.3 London pension funds have collected information on individual fund performance compared with the larger county councils and concluded that while there is a wide distribution of returns across London, which might indicate poor management by some councils, on average the larger county councils generated returns that were no higher than the London average. The research did suggest that there is scope for fee savings, but not to the extent suggested by earlier commentators.

4.4 It is clear that the Government seeks change, possibly by compulsion if not achieved voluntarily. The CIV route addresses many of the concerns raised in previous discussions on compulsory merger, and should achieve many of the benefits of scale. The merits of the CIV route are listed as follows:

- It leaves unchanged the structure of the scheme, the setting of strategy and the determination of manager mandate (active versus passive);
- By operating at asset class level, it allows choice as to which asset classes should be collectively managed and which excluded;
- Greater scale would enable investments to be managed in a different way – an example would be avoiding use of 'fund of funds' approaches because the CIV pool would be large enough to diversify adequately;
- There is no compulsion to use the CIV, although there needs to be adequate support from a sufficient number of funds to ensure its success;
- The CIV will have running costs (staff, accommodation and advisers), although these should be wholly offset by reduced management fees through larger pools of assets;
- Individual schemes may save on adviser fees;
- By acting to achieve the fee savings and improved performance the Government expects from the pooling of assets, the establishment and use of a CIV may avoid more drastic action being imposed.

5. FINANCIAL IMPLICATIONS

5.1 These are included within the report.

6. DIVERSITY IMPLICATIONS

6.1 None.

7. STAFFING IMPLICATIONS

7.1 None.

8. LEGAL IMPLICATIONS

8.1 None.

9. BACKGROUND

9.1 None.

10. CONTACT OFFICERS

10.1 Persons wishing to discuss the above should contact the Treasury and Pension Investment Section, Governance and Corporate Services, on 020 8937 7633 or 07884 997 633 at Brent Civic Centre.

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