Brent	**Pension Fund Sub-Committee** 19 November 2013 **Report from the Chief Finance Officer**
For Action	Wards Affected: ALL

London pension fund collaboration

1. SUMMARY

1.1 Further to the recent public debate regarding the potential merger of LGPS funds, collaboration is high on the agenda and proposals to set up a voluntary collective investment vehicle (CIV) are being developed by the London Leaders 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.

1.2 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 would be voluntary and boroughs would retain their autonomy in asset allocation and funding strategy. The CIV would provide the boroughs with a wide choice of funds within each asset class, would select the "best of breed" fund managers and negotiate and monitor fee and service levels.

1.3 A summary of the Government's 'Call for Evidence' on the future structure of the LGPS is attached at Appendix A to provide Members with some contextual background. The vast majority of LGPS funds (including Brent) have responded by asserting that the Government's objectives can be achieved through greater collaboration between funds without structural change that would reduce local accountability, point to the lack of correlation between size and performance across LGPS funds and highlight the value of current collaborative initiatives already taking place between funds.

1.4 The majority of authorities are in favour of exploring the scope for collaboration and each of the 33 London schemes are expected to commit up to £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.

1.5 Wandsworth Council has offered to act as a lead borough for a CIV for the London pension funds. The lead authority would procure an investment adviser followed by a transition manager and investment funds/fund managers within each asset class, including alternatives like infrastructure. The CIV would operate by maintaining a “best of breed” selection of funds/managers for each asset class, with the CIV using its buying power to secure lower investment manager fees.

1.6 Such a scheme would counter the argument for a single London pension fund and mitigate against the imposition of other, unwelcome initiatives given that the maintenance of the status quo is not a viable option.

2. RECOMMENDATION

2.1 Members are asked to support the investigation and establishment of a collective investment vehicle (CIV) and delegate authority to the Chief Finance Officer to approve expenditure relating to the investigation and set up costs of the CIV up to a limit of £25,000.

3. DETAIL

3.1 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.

3.2 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).

3.3 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.

3.4 It is clear that the Government seeks change, possibly by compulsion if not achieved voluntarily. The CIV route now being investigated 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.

3.5 It is suggested that the Sub-Committee supports further investigation of the CIV option and remain open-minded about using the CIV. It is possible that Brent will be asked to contribute to the investigation and set-up costs of the CIV, and it is suggested that authority be delegated to the Chief Finance Officer to approve such expenditure up to a limit of £25,000. It is considered that if London councils refuse to explore the potential for a CIV that the Government is more likely to force change, such as a merger.

3.6 The report on the 'Annual review of fund managers' fees' included in the exempt section of this particular meeting agenda highlights the significant progress which has been made by the Brent Pension Fund in reducing its fund management costs over the past 12 months. Therefore, whilst the scope to achieve further savings on fees is considered to be limited a reduction of a single basis point, i.e., 0.01%, which equates to £50,000 on a £0.5bn fund would more than offset the proposed £25,000 contribution towards meeting the costs of creating a CIV.

4. FINANCIAL IMPLICATIONS

4.1 These are included within the report.

5. DIVERSITY IMPLICATIONS

5.1 None.

6. STAFFING IMPLICATIONS

6.1 None.

7. LEGAL IMPLICATIONS

7.1 None.

8. BACKGROUND

8.1 None.

9. CONTACT OFFICERS

9.1 Persons wishing to discuss the above should contact the Treasury and Pension Investment Section, Governance and Corporate Services, on 020 8937 1472 at Brent Town Hall.

CONRAD HALL **Chief Finance Officer**	**ANTHONY DODRIDGE** **Head of Exchequer and Investment**

Appendix A

CALL FOR EVIDENCE ON THE FUTURE STRUCTURE OF THE LOCAL GOVERNMENT PENSION SCHEME

The Department for Communities and Local Government (DCLG) has launched an informal 'Call for Evidence' on the question of LGPS Fund sizes, potential mergers and cost management.

The Call for Evidence had been announced by Local Government Minister Brandon Lewis at the National Association of Pension Funds' annual local government conference in May. The Minister stated *"I am neither ruling anything in nor ruling anything out at this stage. However, the clear message from me this morning is that I am not wedded to the existing number of 89 funds in England and Wales. If it takes a smaller number of funds to improve the efficiency and cost-effectiveness of the scheme, I shall not shy away from pursuing that goal."*

The call for evidence sets out two high level objectives and six secondary objectives. These are as follows:

<u>High level objectives</u>

1. Dealing with deficits

2. Improving investment returns

<u>Secondary objectives</u>

1. To reduce investment fees

2. To improve the flexibility of investment strategies

3. To provide for greater investment in infrastructure

4. To improve the cost effectiveness of administration

5. To provide access to higher quality staffing resources

6. To provide more in-house investment resource

There is also the suggestion that, although there is a wide range of data available on Local Government Pension Scheme funds, it is currently widely dispersed and would benefit from enhancement, collation and further analysis. The call for evidence also asks for views on how best to achieve a high level of accountability to local taxpayers, particularly if services are to be shared or funds merged.