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| Brent | **Pension Board**<br>13 December 2016<br><br>**Report from the Chief Finance Officer** |
| For Information Purposes | Wards affected:<br>ALL |

## Breach of Internal Regulations

**1.0 Summary**

1.1 The purpose of this report is to notify Board Members of a breach of internal regulations.

**2.0 Recommendations**

2.1 To note the report.

**3.0 Detail**

3.1 The Pension Fund Sub-Committee of November 8th were informed of a breach of internal regulations. The Pension Fund had added to its tracker funds in Quarter 1 2016, beyond the amount allowable (35%) with an individual body, due to the expectation that for appropriate investments within the CIV would soon become available. During the February Pension Fund Sub-Committee meeting, it should have been explicitly noted in the minutes that it would temporarily breach the internal regulations.

3.2 Since then, investment outperformance in passive equity has caused this element to grow to almost 45%. Furthermore, delays within the CIV have prevented the planned allocation of these monies to investments. It isn't practical to correct this anomaly immediately, given delays in the on-boarding timetable so the Pension Fund Sub-Committee were content with the position and any implied risk, which is minimal.

3.3 In February 2016, Pension Fund Sub-Committee were notified of the temporary £34m additional investment into two different mandates with Legal & General Tracker Funds. This cash came from the divestment of the Dimensional investment. The cash was placed with the Tracker Funds solely for holding purposes till appropriate investments became available. Passive equity was the appropriate choice because they are very low cost and because they track the markets rather than specific investments. The risk is therefore limited to the innate risk of equity in the UK and globally and to LGIM's ability to maintain the appropriate share allocation within the tracker fund.

3.4 Delays in the CIV (collective Investment Vehicle) have caused problems for cash allocation and investment decisions. The Pension Fund Sub-Committee were also told about the officer intent to bring investment decisions to meetings in early to mid-2017. These decisions would arrive with the clear intent of both investing excess cash and reducing the passive equity closer to 30%, in-line with the Pension Fund's strategic investment allocation objectives.

3.5 LGIM UK Tracker Fund shrank by 0.41% in Quarter 1 but then rebounded to grow by 4.74% in Quarter 2 and 7.81% in Quarter 3. LGIM World Ex-UK Dev Equity grew by 2.62%, 8.89% and 8.26% in the same quarters. This growth led to the passive equity share of the Pension Fund rising close to 45%.

3.6 The London CIV was also recently very successful in reducing fees and charges on LGIM tracker fund products. Therefore, there was a clear benefit from the investment decision and the Government generally promotes use of tracker funds and low fee-based investment options to LGPS schemes, wherever possible.

3.7 The LGPS regulatory framework refers to not having more than 35% in one mandate established the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 has the effect of requirement not more than 35% of Unit Trust managed in one mandate. There are currently two different mandates as passive equity is split into the UK portion and the World-wide portion that does not include the UK. These mandates represent different policy objectives within the fund. The scheme is UK based and hence benefits from a UK-centred tracker fund. However, the Pension Fund also needs access to the potential for global sources of growth. Therefore, having two separate passive equity mandates de-risks the Pension Fund. Nonetheless, the Pension Fund has an internal policy of not having more than 35% of Unit trusts managed by any one body so there has been a breach of this internal requirement.

3.8 The new regulatory framework (The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 came into force on 1 November 2016. It requires a new investment strategy and a statement of that strategy to be published no later than April 1st 2017. The regulations transfer investment decisions and their consideration more fully to administering authorities within a new prudential framework. A paper on the new regulatory framework will go to the Pensions Board meeting in the New Year, as the detailed analysis is still taking place.

## 4.0 Financial Implications

4.1 There are no direct financial implications.

## 5.0 Legal Implications

5.1 The Pension Fund must have regard to its internal policies. These are contained within the council's current statutory Statement of Investment Principles under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 ("the 2009 Regulations"). The current statement must be replaced by April 1st 2017 by the new Investment Strategy Statement under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 ("the 2016 Regulations"). There has been a breach of the current statutory report, as the Pension Fund invested more than 35% of Unit trusts managed by a single body.

5.2 The Pension Fund must also have regard to the Schedule 1 to the the 2009 Regulations" until such time as the new Investment Strategy Statement is in place. As set out in the body of the report, the effect of the 2009 Regulations and the schedule is that no single mandate can be more than 35% of the Fund. No single mandate can be more than 35% of the Fund. The passive equity referred to in this report is split into two mandates, which are following two separate policy objectives, one to track the UK market and the other to track the World-wide market. If either of these mandates individually was to breach 35%, this would require the Pension Fund to contact the LGPS regulatory function. As set out in the report, this is the position.

5.3 The 2016 Regulations will give Pension Fund Sub-Committees greater flexibility over matters such as these but they must still have regard to the regulatory oversight that will remain to protect the LGPS schemes from imprudent decision-making.

**6.0 Diversity Implications**

6.1 Not Applicable

**7.0 Staffing/Accommodation Implications (if appropriate)**

7.1 Not Applicable

**Background Papers**

**Contact Officers**

Persons wishing to discuss the above should contact Gareth Robinson, Investment and Pensions Section, Finance, on 020 8937 6567, gareth.robinson@brent.gov.uk at Brent Civic Centre

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