Document Pack

Wales Pension Partnership Joint
Governance Committee,
Democratic Services Unit,
Chief Executive's Department,
Carmarthenshire County Council,
County Hall,
Carmarthen SA31 1JP.

WEDNESDAY, 23 JANUARY 2019

TO: ALL MEMBERS OF THE WALES PENSION PARTNERSHIP JOINT GOVERNANCE COMMITTEE

I HEREBY SUMMON YOU TO ATTEND A MEETING OF THE **WALES PENSION PARTNERSHIP JOINT GOVERNANCE COMMITTEE** WHICH WILL BE HELD IN THE **CHAMBER - LLANDRINDOD WELLS, POWYS AT 10.00 AM, ON THURSDAY, 31ST JANUARY, 2019** FOR THE TRANSACTION OF THE BUSINESS OUTLINED ON THE ATTACHED AGENDA

Mark James

CHIEF EXECUTIVE
CARMARTHENSHIRE COUNTY COUNCIL

***PLEASE NOTE**: THIS MEETING WILL BE FILMED FOR LIVE OR SUBSEQUENT BROADCAST. THE IMAGES AND SOUND RECORDING MAY ALSO BE USED FOR TRAINING PURPOSES..*

Democratic Officer:	**Jessica Laimann**
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Webcast Link	**https://powys.public-i.tv/core/portal/home**

WALES PENSION PARTNERSHIP
JOINT GOVERNANCE COMMITTEE
8 MEMBERS
(1 Member from each Constituent Authority)

CARMARTHENSHIRE COUNTY COUNCIL

COUNCILLOR ELWYN WILLIAMS

CITY & COUNTY OF SWANSEA

COUNCILLOR CLIVE LLOYD

CITY OF CARDIFF

COUNCILLOR CHRISTOPHER WEAVER

FLINTSHIRE COUNTY COUNCIL

COUNCILLOR DAVID HUGHES

GWYNEDD COUNTY COUNCIL

COUNCILLOR JOHN PUGHE ROBERTS

POWYS COUNTY COUNCIL

COUNCILLOR PETER LEWIS

RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

COUNCILLOR MARK NORRIS

TORFAEN COUNTY BOROUGH COUNCIL

COUNCILLOR GLYN CARON

A G E N D A

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WALES PENSION PARTNERSHIP JOINT GOVERNANCE COMMITTEE

Tuesday, 25 September 2018

PRESENT: Councillor P. Lewis (Vice-Chair)

Councillors:
Cllr. G. Caron, Cllr. D. Hughes, Cllr. C. Lloyd, Cllr. J.Pugh Roberts, Cllr. R. Smith (In place of Cllr. M Norris), Cllr. C. Weaver and Cllr. D.E. Williams

The following Officers were in attendance:
C. Moore, Joint Committee Section 151 Officer (CCC)
L.R. Jones, Joint Committee Monitoring Officer (CCC)
J. Dong, Chief Treasury & Technical Officer (C&CS)
D. Edwards, Director of Finance (GCC)
C. Salter, Corporate Director of Resources (CoC)
C. Lee, Director Corporate and Frontline Services (RCTCBC)
A. Parnell, Treasury & Pensions Investments Manager (CCC)
D. Powell, Acting Chief Executive (PCC)
D. Fielder, Pensions Finance Manager (FCC)
K. Davies, Head of Corporate Pensions (C&CS)
G. Morgan, Head of Democratic Services (CCC)

Also present:-

Denise Jones- Link Asset Services
Peter Hugh Smith, Link Asset Services
Sasha Mandich, Russell Investments
Jim Leggate, Russell Investments
Eamonn Gough, Link Asset Services
Duncan Lowman, Link Asset Services
Paul Potter, Hymans Robertson

Siambr Dafydd Orwig, - Gwynedd County Council, Council Offices, Caernarfon, Gwynedd, LL55 1SH - 10.00 - 11.00 am

1. APOLOGIES FOR ABSENCE

An Apology for absence was received from the Chair of the Joint Committee, Councillor Mark Norris, of Rhondda Cynon Taf County Borough Council.

Apologies for absence were also received from Nigel Aurelius of Torfaen County Borough Council and of Philip Latham of Flintshire County Council.

2. DECLARATIONS OF INTEREST

Councillor	Nature of Personal Interest
G. Caron	Member of Greater Gwent Pension Fund Wife is deferred Member of the Greater Gwent Pension Fund
D. Hughes	Member of the Clwyd Pension Fund;
P. Lewis	Member of the Powys Pension Fund;
C. Lloyd	Member of the City and County of Swansea Pension Fund;
R. Smith	Member of the Rhondda Cynon Taf Pension Fund;
J. Pugh Roberts	Member of the Gwynedd Pension Fund;
E. Williams	Member of the Dyfed Pension Fund.

(Note: There is an exemption within the Code of Conduct for Members, which allows a member who has been appointed or nominated by their authority to a relevant body to declare that interest but remain and participate in the meeting).

3. TO SIGN AS A CORRECT RECORD THE MINUTES OF THE MEETING HELD ON THE 11TH JUNE 2018

The Chair advised that there was one correction to the minutes as Cllr C. Weaver was not a member of the local government Pension Fund. Cllr Weaver confirmed this was correct.

UNANIMOUSLY RESOLVED that the minutes of the meeting of the Committee held on the 11th June be signed as a correct record, subject to the above amendment.

4. PRESENTATION BY LINK AND HOST AUTHORITY ON MILESTONES AND PROGRESS UPDATE

The Chair welcomed Denise Jones – Head of Change Management of Link Fund Solutions to provide a presentation on Key Milestones and progress in respect of the Wales Pension Partnership.

Ms Jones provided the Joint Committee with a list of the provisional dates for the key milestones, progress to-date on Initial Funds (Global Equity) Tranche 2 (UK and European Equities) and the next steps.

Ms Jones advised that Link were currently working through the reporting templates with a sample pack having been considered by the Officers Working Group in July, it was therefore hoped that agreement on the pack would be received shortly in readiness for the first fund launch.

Ms Jones also informed the Joint Committee that Investment Manager Agreements were underway and it was hoped that all agreements would be signed by the end of September 2018.

In terms of the Global Equity Sub-fund, Link were still targeting mid November 2018 for the launch of the first two funds and it was hoped that agreement would be made within Agenda item 6 for the Tranche 2 funds - UK and European Equities, with approval of the schedule 5 additions to the Fund prospectus by 5th October.

In terms of Transition Manager Appointments for the first two funds (Global Equities), all bids had been received and an initial evaluation had been undertaken, reviewed with officers and final approval was expected within the next week.

In terms of progress to-date, the Joint Committee was advised that:-

- FCA approval was received for the initial funds on the 24th July;
- An Initial Manager engagement day was held on the 5th September with the 3 Global Growth and 3 Global Opportunities Manager in attendance, an additional 4 managers would meet with the Joint Committee later that morning
- Contract negotiations had commenced with Northern Trust for the depositary agreement, as per the report, with the execution copy due for completion later in the week
- Link had reviewed the Administration agreement and fed initial comments back to Northern Trust
- Letters of engagement were now in place for Audit, Legal and Tax advisors.

In terms of Tranche 2 Link had considered UK and European equities, and the fund proposals had been agreed with the investing local authorities of Cardiff and Torfaen, with the schedule 5 additions completed and issued for initial review by the Officers and then approved for submission to the FCA with a view to launch in mid January 2019. It was hoped that Transition Mangers would be appointed by the 11th October 2018. Work had also commenced on fixed income proposals which would hopefully be agreed in November 2018 so that work could commence on the third FCA submission.

Reference was made to the key milestones and dates detailed within the report, and clarification was sought regarding the appointment process for the Transition Manager. The Joint Committee S151 Officer advised that the Transitional Manager would require appointment by each individual authority, and each Authority's appointments process would apply.

In response to a question, Ms Jones advised that the appointment of Global Growth and Global Opportunities Managers would be subject to performance on the first tranche, and it was not therefore guaranteed that the same managers would be appointed to the different funds.

Mr Anthony Parnell provided the Committee with the following update on the host authority's responsibilities:-

- Staffing – following a resource issue, the Host Authority was currently undertaking a recruitment process in respect of the Wales Pension

Partnership Officer and it was hoped that an appointment would be made in the next few months.

- In terms of communications, the first reporting pack had now been produced and discussions were ongoing with another Pension Partnership to ascertain if a consistent approach for reporting could be agreed. The Partnership was also required to provide a progress report to the MHCLG (Ministry of Housing, Communities & Local Government) every season, the Autumn report would shortly be drafted in consultation with Hymans Robertson, and following consultation with the Officer Working Group, the progress report would be circulated for signing off via email by the JGC.
- Governance – Officer Working Groups continued to meet on a regular basis, prospectuses had been approved and the Joint Committee arrangements were working well and compared favourably with other similar pension pools. Work on the development of the website was ongoing. Reporting arrangements continued to be developed in line with CIPFA recommendations and Government expectations.

The Chair congratulated the Partnership on its recent success in being highly commended in the Pool of the Year category at the LAPF Investment Awards 2018 held at the Savoy Hotel, London on Thursday 20th September 2018.

The Committee's Section 151 Officer advised that a request had been received from the Minister for Housing, Communities and Local Government to meet with the Chair of the Committee and officers to discuss the Joint Committee's infrastructure potential proposals, and this meeting would take place shortly.

UNANIMOUSLY RESOLVED that the presentation from Link and the host Authority on milestones and progress update be received.

5. EXCLUSION OF THE PUBLIC

UNANIMOUSLY RESOLVED, pursuant to the Local Government Act 1972, as amended by the Local Government (Access to Information)(Variation) (Wales) Order 2007, that the public be excluded from the meeting during consideration of the following item as the report contained exempt information as defined in paragraph 14 of Part 4 of Schedule 12A to the Act.

6. PRESENTATION BY LINK / RUSSELL ON UK AND EUROPEAN EQUITY SUB-FUNDS

Following the application of the public interest test it was UNANIMOUSLY RESOLVED, pursuant to the Act referred to in minute number 5 above, to consider this matter in private, with the public excluded from the meeting on the basis disclosure of the information detailed in the report would include details of the finer detail of investment opportunities which had yet to be negotiated fully or renegotiated and disclosing the presentation would prejudice those negotiations and impact upon the Funds' costs and returns.

The Committee welcomed Peter Hugh Smith - Managing Director - Link Asset Services and Sasha Mandich - Director, Russell Investments to the meeting.

The Committee proceeded to receive a presentation on the structure of the two regional equity funds namely UK and Europe ex-UK, and considered recommendations in respect of those funds.

Members of the Committee were afforded the opportunity of asking questions on the funds, including fund performance, diversification of investment styles, how funding was split between the two sub-funds, fund manager changes/staffing turnover, and the process for investment./withdrawal.

UNANIMOUSLY RESOLVED:-

1. **That the presentation be noted.**

2. **to invest in two separate sub funds in order to achieve effective diversification, and to employ five specialist managers per fund, namely:-**

    - **UK Equities – Majedie, Lazard Omega, Baillie Gifford, Investec and Liontrust.**

    - **Europe ex-UK equities – Blackrock, Pzena, Invesco, SW Mitchell and Liontrust.**

3. **to reduce trading costs through an 'enhanced implementation' approach, which would involve offsetting overlapping manager trades rather than directing every manager to trade separately with their own brokers.**

CHAIR **DATE**

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WALES PENSION PARTNERSHIP
JOINT GOVERNANCE COMMITTEE

DATE 31 JANUARY 2019

PRESENTATION BY LINK AND THE HOST AUTHORITY ON MILESTONES AND PROGRESS UPDATE

RECOMMENDATIONS / KEY DECISIONS REQUIRED:

To receive a presentation from Link and the host authority on milestones and progress update of the Wales Pension Partnership.

REASONS:

Link and the host authority to provide an update on the milestones and progress of the Wales Pension Partnership.

Report Author:	Designation:	Tel No. 01267 224160
Chris Moore	Director of Corporate Services **Carmarthenshire County Council**	**E. Mail:** **CMoore@carmarthenshire.gov.uk**

EXECUTIVE SUMMARY
JOINT GOVERNANCE COMMITTEE
DATE 31 JANUARY 2019

PRESENTATION BY LINK AND THE HOST AUTHORITY ON MILESTONES AND PROGRESS UPDATE

BRIEF SUMMARY OF PURPOSE OF REPORT

Link and the host authority to present to the Joint Governance Committee an update on the progress and milestones of the Wales Pension Partnership.

DETAILED REPORT ATTACHED?	YES

IMPLICATIONS

Policy, Crime & Disorder and Equalities **NONE**	Legal **NONE**	Finance **NONE**	Risk Management Issues **NONE**	Staffing Implications **NONE**

CONSULTATIONS

Section 100D Local Government Act, 1972 – Access to Information List of Background Papers used in the preparation of this report: THESE ARE DETAILED BELOW		
Title of Document	**File Ref No.**	**Locations that the papers are available for public inspection/WEBSITE LINK**

LINK Asset Services

WPP Joint Governance Committee

Date 31st January 2019

Version 0.1

Key Milestones

Task	Date	RAG	Comment/Responsible
Reporting Template agreed	31/01/19	G	Schedule of reports provided
Investment Manager Agreements	31/12/18	C	Tranche 1 all complete
Approval of Fund Prospectus	11/06/18	C	
FCA Submission	24/06/18	C	
Global Equity Sub Funds Fund Launch	14/01/19	G	Transition on schedule Global Opportunities to Launch 11/01/19
Agree Funds – **Tranche 2**	25/07/18	C	Two funds agreed UK Equity and European ex UK Equity
Approval of Fund Prospectus	05/10/18	C	
FCA Submission – Tranche 2	18/01/19	G	
Fund Launch – Tranche 2	19/03/19	G	
Agree Funds – **Tranche 3**	31/01/19	G	Manager line up approval for third tranche of funds (Fixed Income)
Approval of Fund Prospectus	27/03/19	G	
FCA Submission – Tranche 3	10/04/19	G	
Fund Launch – Tranche 3	11/07/19	G	

Progress to date

Initial Funds (Global Equity)

- Launch and transition of assets completed over 11th and 14th January
- Daily reporting in place, including market commentary
- Restructuring of portfolios scheduled for week commencing 21st January
- First reporting to commence February

Tranche 2 (UK and European Equities)

- Prospectus submitted to FCA week ending 18th January
- Fund launch targeting 19th March, subject to FCA approval
- Transition proposal shared with pool

Tranche 3 (Fixed Income)

- Final fund structure proposal agreed with Officers
- Initial Investment Manager proposals to be agreed

Next Steps

- Tranche 3 agree Investment Managers – **WPP February 2019**
- Agree approach to transition for tranche 2 – **WPP February 2019**
- Agree future tranches – **WPP March 2019**
- Agree Stock Lending requirements – **WPP February 2019**

Host Authority Update

- Staffing
- Communications
- Governance
- Reporting

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WALES PENSION PARTNERSHIP
JOINT GOVERNANCE COMMITTEE

DATE 31 JANUARY 2019

RESPONSIBLE INVESTMENT – DEVELOPMENT OF POLICY

RECOMMENDATIONS / KEY DECISIONS REQUIRED:

To note the draft Responsible Investment policy.

REASONS:

Hymans to develop the first draft of the Responsible Investment policy for the Wales Pension Partnership.

Report Author:	Designation:	Tel No. 01267 224160
Chris Moore	Director of Corporate Services **Carmarthenshire County Council**	**E. Mail:** **CMoore@carmarthenshire.gov.uk**

EXECUTIVE SUMMARY
JOINT GOVERNANCE COMMITTEE
DATE 31 JANUARY 2019

RESPONSIBLE INVESTMENT – DEVELOPMENT OF POLICY

BRIEF SUMMARY OF PURPOSE OF REPORT

Hymans have drafted the development of a Responsible Investment policy which considers how social, environmental and corporate governance considerations are taken into account by individual funds and at Pool level and sets out the actions the Pool should now take.

DETAILED REPORT ATTACHED?	YES

IMPLICATIONS

Policy, Crime & Disorder and Equalities **YES**	Legal **NONE**	Finance **NONE**	Risk Management Issues **NONE**	Staffing Implications **NONE**
Policy New Responsible Investment policy to be developed which will become a formal document for the Wales Pension Partnership.				

CONSULTATIONS

Consultation with all 8 Welsh funds.

Section 100D Local Government Act, 1972 – Access to Information List of Background Papers used in the preparation of this report: THESE ARE DETAILED BELOW		
Title of Document	**File Ref No.**	**Locations that the papers are available for public inspection/WEBSITE LINK**

Responsible Investment: Review of current position and development of policy

Wales Pension Partnership

William Marshall,
Partner, Hymans Robertson

21 January 2019

HYMANS ROBERTSON

Agenda

- Introduction and executive summary
- Regulatory and current issues
- Summary of the Funds' positions
- WPP potential areas of focus

Introduction

- This note is addressed to the Joint Governance Committee ("JGC") of the Wales Pension Partnership ("WPP"). The purpose of this note is to consider how social, environmental and corporate governance considerations are taken into account by individual funds and at Pool level and to set out the actions the Pool should now take. It should not be released or otherwise disclosed to any third party except with our prior written consent, in which case it should be released in its entirety. We accept no liability to any other party unless we have accepted such liability in writing.
- By placing an emphasis on long-term risks, the Pool will need to consider how Environmental, Social and Governance ("ESG") factors are taken into account within strategic decisions, as well as the existing focus on implementation, engagement, stewardship and monitoring. This can be encapsulated in WPP's approach to Responsible Investment.
- Responsible Investment can be broadly defined although we consider it has two elements: *Sustainable Investment* whereby the potential impact of ESG issues on financial outcomes are considered at each stage of the investment process and *Effective Stewardship* whereby investors ensure that they both place a value on and exercise the rights and responsibilities associated with asset ownership.
- This paper provides the following:
  - Review the eight Welsh Funds' responsible investment ("RI") and voting policies, highlighting areas of agreement and differences.
  - Discuss recent industry developments and areas for the Funds to consider when setting their future policies.
  - Set out potential next steps, which will be discussed at the Joint Governance Committee.

We look forward to discussing this paper with you.

Executive summary of the Funds' positions

Fund	Bespoke RI Policy	LAPFF member	PRI signatory	UK SC signatory (3)	Investment Beliefs (4)	Voting	Explicit policy on Climate risk
Fund 1	✓	✓	✗	✗	✓	Delegated to managers	✓
Fund 2	✗	✓	✗	✗	Note 4	Delegated to managers	✗
Fund 3	Note 1	✓	✗	✗	✓	Delegated to managers	✗
Fund 4	✗	✓	✗	✗	✓	Delegated to managers	✗
Fund 5	✓	✓	✗	✓	✓	Delegated to managers	✗
Fund 6	Note 2	✓	✗	✗	Note 4	Delegated to managers	✓
Fund 7	✗	✓	✗	✗	Note 4	Delegated to managers	✗
Fund 8	Note 1	✓	✗	✓	✓	Delegated to managers	✗

1. Policy currently being drafted. 2. Fund has a RI statement on Climate Change in place. 3. All funds support the principles of the codes and expect their managers to be signatories. 4. Some Funds may have documented investment beliefs but these have not been made publically available.

Regulatory overview and current issues

Regulatory requirements/recommendations – a reminder

"The law is generally clear that schemes **should** consider any factors that are financially material to the performance of their investments, including social, environmental and corporate governance factors, and over the long term, dependent on the time horizon over which their liabilities arise. Although schemes **should** make the pursuit of a financial return their predominant concern, they **may** also take purely non-financial considerations into account provided that doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision ." *MHCLG*

"The long-term investment interests of administering authorities are enhanced by the highest standards of corporate governance and corporate responsibility amongst the companies in which they invest. Poor governance can negatively impact shareholder value. Stewardship aims to promote the long term success of companies in such a way that the ultimate providers of capital also prosper." *MHCLG*

"In formulating and maintaining their policy on social, environmental and corporate governance factors, an administering authority:- **Must** take proper advice; **Should** explain the extent to which the views of their local pension board and other interested parties who they consider may have an interest will be taken into account when making an investment decision based on non-financial factors; **Must** explain the extent to which non-financial factors will be taken into account in the selection, retention and realisation of investments; **Should** explain their approach to social investments." *Regulation 7 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016*.

Bolding added by Hymans Robertson for emphasis

Regulatory requirements/recommendations – a reminder

"Pool members **should** ensure that pool companies report in line with the SAB Code of Cost Transparency. They **should** also ensure that pool companies require their internal and external investment managers to do so. *Regulation 7 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016*."

"In formulating their policy on the exercise of rights, administering authorities: **Must** give reasons in their Investment Strategy Statement for not adopting a policy of exercising rights, including voting rights, attaching to investments; **Should**, where appropriate, explain their policy on stewardship with reference to the Stewardship Code; **Should** strongly encourage their fund managers, if any, to vote their company shares in line with their policy under Regulation 7(2)(f); **May** wish to appoint an independent proxy voting agent to exercise their proxy voting and monitor the voting activity of the managers, if any, and for reports on voting activity to be submitted annually to the administering authority; **Should** publish a report of voting activity as part of their pension fund annual report under Regulation 57 of the 2013 Regulations. *Regulation 7 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016*."

Well-being of Future Generations (Wales) Act 2015

"The Act will make the public bodies listed in the Act think more about the long term, work better with people and communities and each other, look to prevent problems and take a more joined-up approach. This new law will mean that, for the first time, public bodies listed in the Act must do what they do in a sustainable way. Public bodies need to make sure that when making their decisions they take into account the impact they could have on people living their lives in Wales in the future."

Bolding added by Hymans Robertson for emphasis

Other developments to consider

FRC UK Stewardship Code.

It is currently expected that the FRC will publish a consultation on the Stewardship Code on 30 January 2019 with a revised Code expected to be introduced around July 2019. As potential signatories, WPP may wish to review the consultation.

Climate risk.

There is increasing scrutiny on the actions being taken by long-term institutional investors in addressing the risks associated with climate change. We set out overleaf some of the major regulatory considerations over recent times suggesting this should be an issue which is explicitly addressed in WPP's RI policy.

Recommendations of the Task Force on Climate-related Financial Disclosures ("TCFD"). The TCFD has proposed a framework within which institutions can report on their approach to climate change. Individual Funds may come under pressure to report in line with the TCFD recommendations and WPP may wish to consider how they can support such Funds.

What are the regulators saying about climate risk?

- Guidance from the **Pensions Regulator** states that climate change is a risk that 'could be financially significant both over the short term and the longer term'. They also tell trustees to **take climate risk factors into account** when making investment decisions and encourage them to become familiar with their managers' stewardship policies.
- The **Environmental Audit Committee** (EAC) recently stated that MPs want to see pension savers be given greater opportunities to engage with decisions about where their money is invested. Mary Creagh MP, Chair of the EAC said, "**We want to see mandatory climate risk reporting** and a clarification in law that pension trustees have a duty to consider long term sustainability, not just short-term returns."
- Following the Department for Work and Pensions' (DWP's) consultation on changes to occupational pension scheme regulations, from 1 October 2019 trustees will be required to set out in their Statement of Investment Principles **how they take account of financially material considerations and stewardship, including climate change**.
- The **Institute and Faculty of Actuaries** released a Risk Alert stating that actuaries should ensure that they understand and are clear in communicating the **extent to which they have taken account of climate-related risks** in any relevant decisions, calculations or advice.

In light of the emerging consensus about the financial materiality of climate risk, regulators are now encouraging asset owners to seriously consider the impact of climate-related risks and opportunities on their pension schemes

Summary of the Funds' positions

Summary of the Funds' positions

Fund	Bespoke RI Policy	LAPFF member	PRI signatory	UK SC signatory (3)	Investment Beliefs (4)	Voting	Explicit policy on Climate risk
Fund 1	✓	✓	✗	✗	✓	Delegated to managers	✓
Fund 2	✗	✓	✗	✗	Note 4	Delegated to managers	✗
Fund 3	Note 1	✓	✗	✗	✓	Delegated to managers	✗
Fund 4	✗	✓	✗	✗	✓	Delegated to managers	✗
Fund 5	✓	✓	✗	✓	✓	Delegated to managers	✗
Fund 6	Note 2	✓	✗	✗	Note 4	Delegated to managers	✓
Fund 7	✗	✓	✗	✗	Note 4	Delegated to managers	✗
Fund 8	Note 1	✓	✗	✓	✓	Delegated to managers	✗

1. Policy currently being drafted. 2. Fund has a RI statement on Climate Change in place. 3. All funds support the principles of the codes and expect their managers to be signatories. 4. Some Funds may have documented investment beliefs but these have not been made publically available.

Observations on the current arrangements

- There are several areas of commonality in that:
  - Voting policy is delegated to investment managers;
  - All funds are members of LAPFF, but unclear how Funds interact with LAPFF;
  - Majority are not signatories of the UK Stewardship Code or UNPRI;
  - Not clear how much reporting each fund receives on ESG issues from their managers.
- One fund is not clear on the financial materiality of ESG factors;
- Several funds have undertaken some action to explicitly address RI issues. In particular, actions that have been taken include:
  - Several funds have worked to develop their own investment beliefs;
  - One fund has undertaken a carbon footprinting exercise and introduced a target to reduce its carbon exposure. One other fund has made a statement of its position on climate change;
  - Two funds are signatories to the UK Stewardship Code;
  - Several funds are in the process of completing RI policies

WPP potential areas of focus

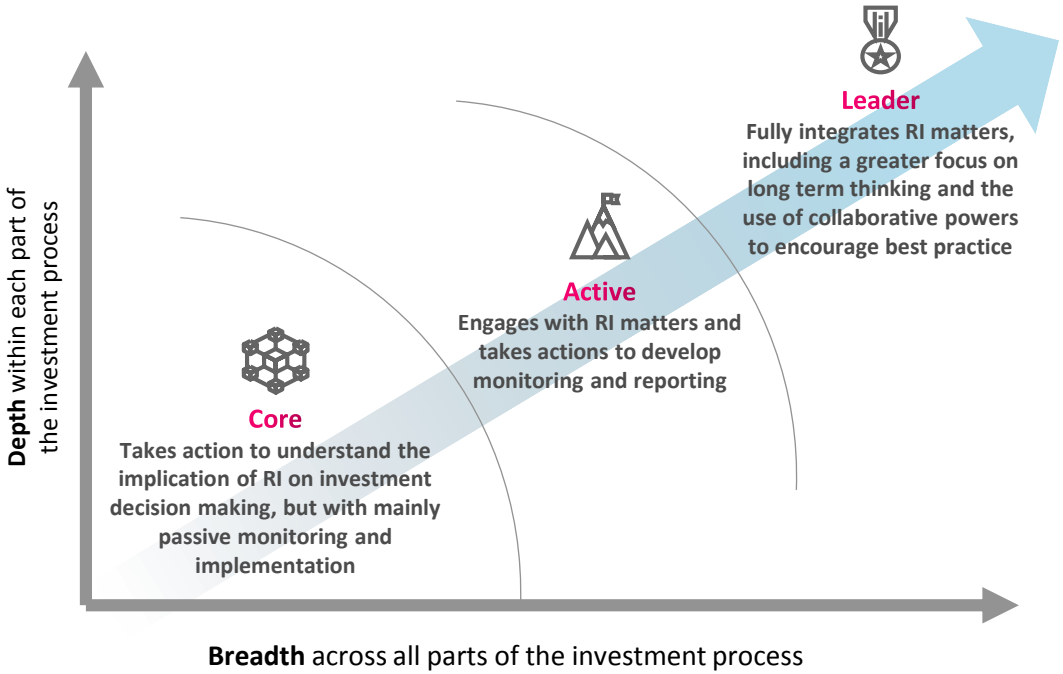
A key question for WPP and the Funds is to consider "what sort of responsible investors they want to be"

There is a spectrum of positions that the pool could take on RI although the position they choose to take should be both proportionate and scheme specific, informed by a number of factors. These factors include:

- Views and investment beliefs;
- The investment time horizon;
- Asset size and the associated complexity of the investment arrangements;
- The means of implementation;
- The overall governance budget;
- Potential scrutiny of the investment arrangements.

To help inform officers discussions, we have developed a framework within which the Pool can consider the position they wish to take

This framework is not intended to be rigid and there may be some elements for which a higher (or lower) level of behaviour is deemed appropriate.



Core position criteria (1)

RI Criteria	Comment on potential actions for WPP to develop RI policy
Beliefs	Several, but not all Funds have developed beliefs. WPP could consider consolidating beliefs at a pool level to reflect common thinking. Still allows Funds to have their own beliefs but should seek to be complementary.
Policies	WPP to consider whether it is appropriate for Stewardship activity (voting and engagement) should continue to be delegated to investment managers or whether to adopt a Pool level policy. Propose developing a pool level policy. Consider a definition of RI that is applicable to the Pool and Funds. WPP to enforce requirements on Cost Transparency.
Training	WPP to consider how it can support education both within the Pool and to Funds.
Strategy	WPP should seek input from Funds on how It can support their strategy requirements.
Structure	WPP should seek input from Funds on how It can support their strategy requirements. Consideration can be given to the introduction of sub-funds that have defined sustainability criteria.

Core position criteria (2)

Criteria	Comment on potential actions to develop RI policy
Manager selection/ appointment	For certain sub-funds funds, WPP has delegated responsibility for the consideration of RI criteria to Russell Investments (initial fund Global Opportunities). WPP should consider any minimum criteria it wishes to reflect in manager selection and agree these with Russell.
Reporting	WPP can consider what metrics it is important to demand be reported by its providers and dictate the format of reporting. WPP needs to ensure that sufficient information is available to fulfil reporting needs e.g. footprinting. WPP to consider its own disclosures and those of Funds and explore how Funds needs are met.
Monitoring	WPP to consider approach to ensuring that managers are meeting policies. What challenge mechanisms exist to ensure that reporting is acted upon. Is there an appropriate governance framework in place.
Adherence	WPP should ensure that it reviews compliance with its own policies.

WPP comparison of RI beliefs

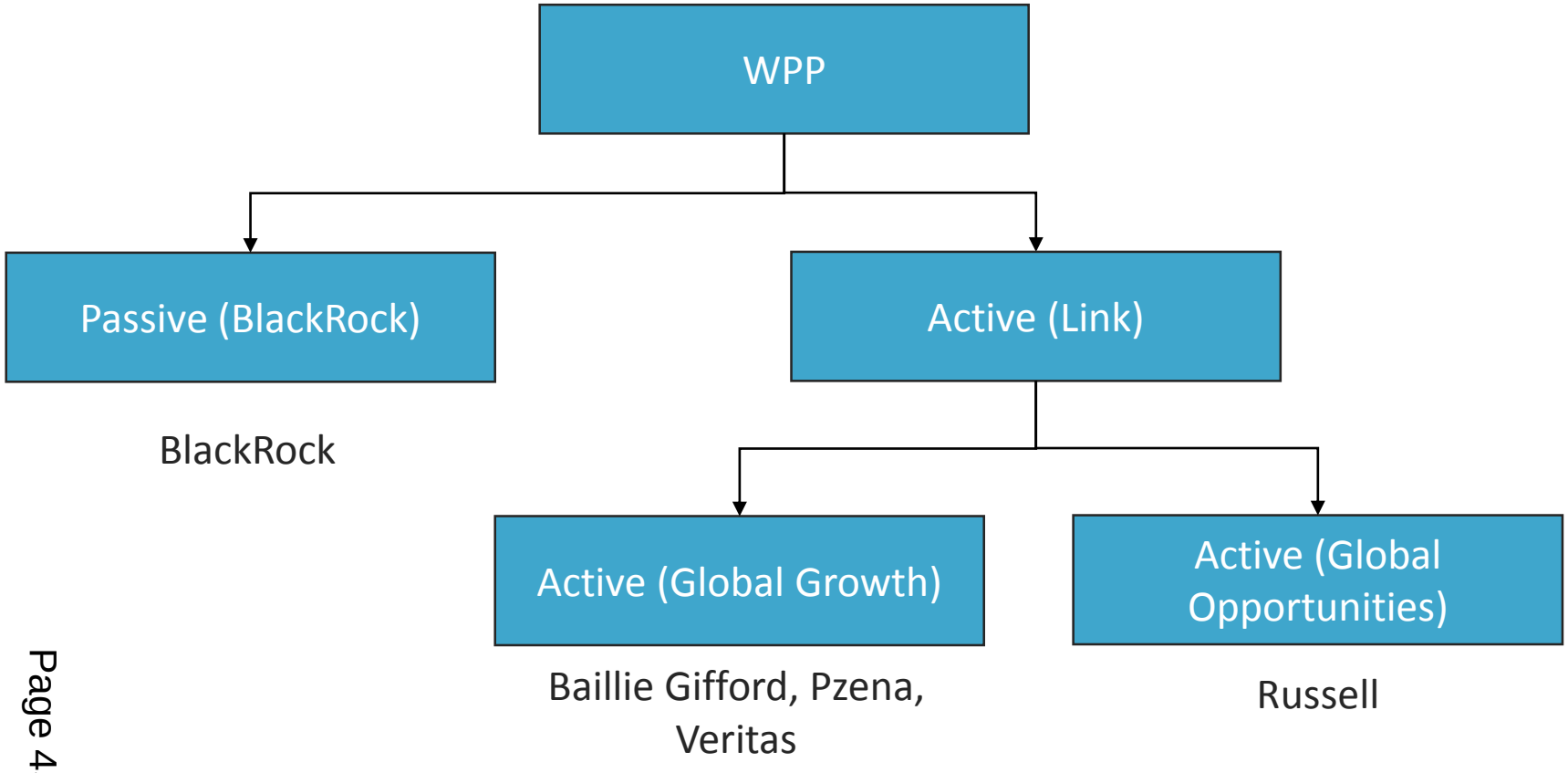
- In the table below we have provided some examples of common areas across the responsible investment beliefs of the funds for which the information was available.
- Further work will be required to establish a set of beliefs and practices that all Funds will subscribe

Areas of Commonality	Observations relating to the Beliefs
Clarity and transparency of the Fund's approach	The Funds should develop a formal responsible investment policy for the Fund. The Funds should publicly disclose its activity on ESG and Stewardship to all stakeholders.
Fully integrated into managers' processes	The Funds' investment managers should embed the consideration of ESG factors into their investment process and decision making.
More information and better reporting	More information is needed to determine the potential financial risk to the Funds of climate change. The Funds would benefit from greater reporting on ESG factors as part of its ongoing monitoring activities.
Engagement with managers where possible	The Funds need to engage more with the Fund's investment managers to better understand ESG risks.

WPP management of climate risk

- Range of approaches amongst the 8 Funds to address this with one fund having set an explicit carbon target.
- The role of the Pool is to facilitate the strategic actions that the Funds may wish to take, but the Pool can support these actions through its RI policy and activities.
- For example, the Pool may have a policy of pushing managers to improve disclosure on climate risk or to vote in favour of climate related resolutions.
- Further, the Pool can lend its support to collaborative actions on behalf of the funds.
- Funds influence sub-fund offering

WPP - which voting policy applies, e.g. Global Equity



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WPP voting arrangements

The current approach to the implementation of voting policy has the potential for inconsistency.

- For active equity funds, Link has set out voting guidelines which are then implemented by the respective managers, subject to a comply or explain approach.
- Managers could interpret the guidelines differently or exercise a different view and hence the possibility remains that managers could vote differently on the same share.
- For passive funds, the voting policy is both framed and implemented by BlackRock.
- There is reporting obligation on Link to WPP, but equally a reporting obligation from each of the underlying managers to Link. This could create operational inconsistencies or delays although the use of a single custodian should limit this.
- Whilst Link has proposed and implemented the voting guidelines to WPP, has there been consultation with WPP on the appropriateness of these guidelines? Has there been any dialogue between Link and the managers on the interpretation of the guidelines?

WPP voting and engagement comments

- Potential areas for discussion and action:
  - Engagement with Link on the voting guidelines to ensure that they are fit for purpose and meet WPP's requirements;
  - Engagement with Link on the reporting requirements and scrutiny of voting;
  - Review consistency of approach between active and passive management and agree how to hold BlackRock to account;
  - Consider
    - potential to use a single voting agent rather than delegating voting to individual managers. This could be a proxy adviser (e.g. ISS) or a third party (e.g. Hermes)
    - If there is flexibility within BlackRock's approach
    - interaction of voting and engagement and whether engagement could be implemented separately. Explore role of LAPFF.
    - Other forms of joint engagement e.g. IIGCC

Goals in the development of RI policy for WPP

For the development of a RI policy, the following criteria are suggested:

- **Clear** – Policy should be unambiguous, particularly under external scrutiny.
- **Proportionate** – Policy should reflect where the Funds and WPP are at in their RI journey. There is no need to try to become a Leader overnight.
- **Consistent** – Policy should reflect the decisions that have already be taken both within WPP and, as far as possible, the Funds.
- **Implementable** – Policy should be able to be put into practice using the structure and resources of the Pool.
- **Reflective of best practice** – Policy should consider current regulatory and best practice requirements but be subject to review and change in future.

WPP - what issues should you include in your policy?

Area	Issues to cover
Policy/Governance	Beliefs Education Divestment Fund engagement Approach to review of policy Delegations
Strategy/Structure	Climate risk Approach to different asset classes
Implementation	Approach to manager selection Fees/costs and transparency
Stewardship	Voting policies and approach to voting Engagement with companies Collaboration Litigation
Monitoring	Information/reporting requirements of third parties Approach to reviewing adherence to policy Disclosure/transparency

Potential next steps

- Discussion with Link and BlackRock on practicalities of current voting and engagement arrangements (March 2019 OWG)
- Initial framework for RI policy (March 2019 OWG)
  - WPP to consider how they want to define “Responsible Investment”
  - Issue short questionnaire to Funds to help develop WPP RI beliefs and policy (January/February 2019)
- Draft RI policy for review by WPP and agreement with Funds (27 March 2019 JGC)
- Consider potential next steps e.g. explicit policies on certain topics subjects (27 March 2019 JGC)

Appendix 1

Industry codes

UK Stewardship Code

Currently 31 LGPS funds and 3 pools are listed as signatories to the Code

MHCLG guidance suggests that Funds should become signatories to the Code

To become a signatory, entities have to produce a statement detailing how they comply with each of the principles. There is no cost.

The Code is due to be reviewed during 2019

The Principles of the Code

So as to protect and enhance the value that accrues to the ultimate beneficiary, institutional investors should:

1. publicly disclose their policy on how they will discharge their stewardship responsibilities.
2. have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed.
3. monitor their investee companies.
4. establish clear guidelines on when and how they will escalate their stewardship activities.
5. be willing to act collectively with other investors where appropriate.
6. have a clear policy on voting and disclosure of voting activity.
7. report periodically on their stewardship and voting activities.

Principles for Responsible Investment

Currently 10 LGPS funds and 4 pools are listed as signatories to the PRI

Signing up to the PRI places an obligation on entities that they will commit to complying with the principles, and to reporting how they comply

There is a cost to signing of circa £10k per annum

Signatories' commitment

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time).

We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes.

Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.

Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.

Principle 4: We will promote acceptance and implementation of the Principles within the investment industry.

Principle 5: We will work together to enhance our effectiveness in implementing the Principles.

Principle 6: We will each report on our activities and progress towards implementing the Principles.

Thank you

This paper is addressed to the JGC of the Wales Pension Partnership ("WPP"). The purpose of this paper is to provide a summary of the Funds' positions on ESG related matters and potential areas for future consideration. The note has not been prepared for use for any other purpose. It should not be released or otherwise disclosed to any third party except as required by law or regulatory obligation or without our prior written consent.

HYMANS ROBERTSON

WALES PENSION PARTNERSHIP
JOINT GOVERNANCE COMMITTEE

DATE 31 JANUARY 2019

MINISTRY OF HOUSING, COMMUNITIES AND LOCAL GOVERNMENT (MHCLG) CONSULTATION ON DRAFT STATUTORY GUIDANCE ON ASSET POOLING IN THE LOCAL GOVERNMENT PENSION SCHEME (LGPS)

RECOMMENDATIONS / KEY DECISIONS REQUIRED:

To note the MHCLG consultation and Hymans paper.

REASONS:

To make the JGC aware of the consultation on draft statutory guidance on asset pooling in the LGPS.

Report Author:	Designation:	Tel No. 01267 224160
Chris Moore	Director of Corporate Services **Carmarthenshire County Council**	**E. Mail:** **CMoore@carmarthenshire.gov.uk**

EXECUTIVE SUMMARY
JOINT GOVERNANCE COMMITTEE

DATE 31 JANUARY 2019

MINISTRY OF HOUSING, COMMUNITIES AND LOCAL GOVERNMENT (MHCLG) CONSULTATION ON DRAFT STATUTORY GUIDANCE ON ASSET POOLING IN THE LOCAL GOVERNMENT PENSION SCHEME (LGPS)

BRIEF SUMMARY OF PURPOSE OF REPORT

MHCLG have issued the consultation on draft statutory guidance on asset pooling in the LGPS to ensure the eight asset pools across England and Wales have guidance on:

- Definitions
- Structure and Scale
- Governance
- Transition of assets to the Pool
- Making new investments outside the Pool
- Infrastructure investment
- Reporting

DETAILED REPORT ATTACHED?	YES

IMPLICATIONS

Policy, Crime & Disorder and Equalities **NONE**	Legal **YES**	Finance **NONE**	Risk Management Issues **NONE**	Staffing Implications **NONE**
Legal Statutory guidance will be issued by MHCLG in due course.				

CONSULTATIONS

Consultation with all 8 Welsh funds.

Section 100D Local Government Act, 1972 – Access to Information List of Background Papers used in the preparation of this report: THESE ARE DETAILED BELOW		
Title of Document	**File Ref No.**	**Locations that the papers are available for public inspection/WEBSITE LINK**

Local Government Pension Scheme

Statutory guidance on asset pooling

Contents

Foreword

The reform of investment management in the Local Government Pension Scheme (LGPS) for England and Wales began in 2015 with the publication of criteria and guidance on pooling of LGPS assets, following extensive consultation with the sector. LGPS administering authorities responded by coming together in groups of their own choosing to form eight asset pools.

Through the hard work and commitment of people across the scheme, those eight pools are now operational. Their scale makes them significant players at European or global level, and significant annual savings have already been delivered, with the pools forecasting savings of up to £2bn by 2033. Along the way many lessons have been learnt and great progress has been made in developing expertise and capacity, including in private markets and infrastructure investment.

This is a considerable achievement in itself, but there is still a long way to go to complete the transition of assets and to deliver the full benefits of scale. In the light of experience to date with pooling and the challenges ahead, authorities have requested guidance on a range of issues. The time is now right for new guidance to support further progress.

1 Introduction

1.1 This guidance sets out the requirements on administering authorities in relation to the pooling of LGPS assets, building on previous Ministerial communications and guidance on investment strategies, and taking account of the current state of progress on pooling. 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.

2 Definitions

2.1 This guidance introduces a set of definitions for use in this and future guidance, as follows:

'Pool' the entity comprising all elements of a Local Government Pension Scheme (LGPS) asset pool
'Pool member' an LGPS administering authority which has committed to invest in an LGPS pool and participates in its governance
'Pool governance body' the body used by pool members to oversee the operation of the pool and ensure that the democratic link to pool members is maintained (for example, Joint Committees and officer committees)
'Pool company' 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
'Pool fund' a regulated unitised fund structure operated by a regulated pool company, such as an Authorised Contractual Scheme (ACS)
'Pool vehicle' an investment vehicle (including pool funds) made available to pool members by a regulated pool company
'Pooled asset' an investment for which the selection, appointment, dismissal and variation of terms for the investment manager is delegated to a regulated pool company, or an investment held in a pool vehicle
'Retained asset' an existing investment retained by a pool member during the transition period
'Local asset' a new investment by a pool member which is not a pooled asset

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 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. Pool members may continue to decide if they wish to invest via in-house or externally managed vehicles.

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. This helps ensure the pools comply with financial services legislation, and provides additional assurance to scheme members and employers. Depending on the structure of the pool, appropriate permissions may include permissions for execution, acting as agent, provision of advice, or such other permissions as required by the FCA. Where regulated funds (e.g. in an ACS) are operated by the pool company it should comply with relevant UK legislation.

Regular review of services and procurement
3.5 Pool governance bodies, working with the pool company, should regularly review the provision of services to the pool, and the process of procurement, to ensure value for money and cost transparency. Where services are procured or shared by pool members, pool members should regularly review the rationale and cost-effectiveness of such arrangements, compared to procurement and management through the pool company. Pool members and pool companies should consider using the national LGPS procurement frameworks (www.nationallgpsframeworks.org) where appropriate.

Regular review of active and passive management
3.6 Pool members, working with the pool company, should regularly review the balance between active and passive management in the light of performance net of total costs. They should consider moving from active to passive management where active management has not generated better net performance over a reasonable period. Pool members should also seek to ensure performance by asset class net of total costs is at least comparable with market performance for similar risk profiles.

4 Governance

4.1 Pool members must establish and maintain a pool governance body in order to set the direction of the pool and to hold the pool company to account. Pool governance bodies should be appropriately democratic and sufficiently resourced to provide for effective decision making and oversight.

4.2 Pool members, through their internal governance structures, are responsible for effective governance and for holding pool companies and other service providers to account. Strategic asset allocation remains the responsibility of pool members, recognising their authority's specific liability and cash-flow forecasts.

4.3 Members of Pension Committees are elected representatives with duties both to LGPS employers and members, and to local taxpayers. Those who serve on Pension Committees and equivalent governance bodies in LGPS administering authorities are, in many ways, required to act in the same way as trustees in terms of their duty of care to scheme employers and members, but are subject to a different legal framework, which derives from public law. In particular while they have legal responsibilities for the prudent and effective stewardship of LGPS funds, LGPS benefits are not dependent on their stewardship but are established and paid under statute in force at the time.

4.4 Those who serve on Pension Committees and equivalent governance bodies in pool members should therefore take a long term view of pooling implementation and costs. They should take account of the benefits across the pool and across the scheme as a whole, in the interests of scheme members, employers and local taxpayers, and should not seek simply to minimise costs in the short term.

4.5 Local Pension Boards of pool members have a key role in pool governance, given their responsibilities under the LGPS Regulations 2013 (regulation 106 (1)) for assisting authorities in securing compliance with legislation, and ensuring effective and efficient governance and administration of the LGPS. They can provide additional scrutiny and challenge to strengthen pool governance and reporting, and improve transparency and accountability for both members and employers.

4.6 Local Pension Boards may also provide a group of knowledgeable and experienced people from which observers may be drawn if pool members wish to include observers on pool governance bodies.

Strategic and tactical asset allocation

4.7 Pool members are responsible for deciding their investment strategy and asset allocation, and remain the beneficial owners of their assets, in accordance with *Guidance for Preparing and Maintaining an Investment Strategy.*

4.8 Pool members collectively through their pool governance bodies should decide the pool's policy on which aspects of asset allocation are strategic and should remain with the administering authority, and which are tactical and best undertaken by the pool company. Pool governance bodies, when determining where such decisions lie, should be mindful of the trade-off between greater choice and lower costs and should involve the pool company to ensure the debate is fully informed on the opportunities and efficiencies available through greater scale.

4.9 Providing pool members with asset allocation choices through an excessively wide range of pool vehicles or investment managers will restrict the pool company's ability to use scale to drive up value. On the other hand maximising scale by significantly limiting asset allocation options may not provide all pool members with the diversification needed to meet their particular liability profile and cash flow requirements. Pool members should set out in their Funding Strategy Statement and Investment Strategy Statement how they, through the pool governance body, have balanced these considerations and how they will keep this under regular review.

4.10 Where necessary to deliver the asset allocation required by pool members, pool companies may provide a range of pool vehicles and in addition arrange and manage segregated mandates or access to external specialist funds. Pool governance bodies should ensure that their regulated pool companies have in place the necessary permissions to enable pool vehicles to be made available where appropriate.

4.11 Determining where asset allocation decisions lie will not be a one-off decision as pool member requirements will change over time. Pool governance bodies should ensure that a regular review process, which involves both pool members and pool companies, is in place.

5 Transition of assets to the pool

5.1 Pool members should transition existing assets into the pool as quickly and cost effectively as possible. Transition of listed assets should take place over a relatively short period.

5.2 Pool governance bodies, working with pool companies and, where appointed, external transition managers, should seek to minimise transition costs to pool members while effectively balancing speed, cost and timing, taking into account exit or penalty costs and opportunities for crossing trades.

5.2 The transition process will incur direct or indirect costs which may fall unevenly across pool members. For example, where the selected managers are used by some pool members but not others. In such cases pool members who are already using the selected manager may incur significantly lower (if any) transition costs than those who do not.

5.3 Inter-authority payments (or other transfers of value) may be desirable in order to share these costs equitably between pool members. The Government's view is that such payments are investment costs within Regulation 4(5) of the 2016 Regulations, and payments made by a pool member to meet its agreed share of costs may be charged to the fund of that pool member, whether the payments are made to other pool members, the pool company, or another body by agreement.

Temporary retention of existing assets

5.4 In exceptional cases, some existing investments may be retained by pool members on a temporary basis. If the cost of moving the existing investment to a pool vehicle exceeds the benefits of doing so, it may be appropriate to continue to hold and manage the existing investment to maturity before reinvesting the funds through a pool vehicle.

5.5 In many cases there will be benefits in such retained assets being managed by the pool company in the interim. However pool members may retain the management of existing long term investment contracts where the penalty for early exit or transfer of management would be significant. These may include life insurance contracts ('life funds') accessed by pool members for the purpose of passive equity investment, and some infrastructure investments. Pool members may also retain existing direct property assets where these may be more effectively managed by pool members.

Regular review of retained assets

5.6 Pool members, working with the pool company, should undertake regular reviews (at least every three years) of retained assets and the rationale for keeping these assets outside the pool. They should review whether management by the pool company would deliver benefits. Pool members should consider the long term costs and benefits across the pool, taking account of the guidance on cost-sharing, and the presumption should be in favour of transition to pool vehicles or moving such assets to the management of the pool company.

6 Making new investments outside the pool

6.1 Pool members should normally make all new investments through the pool company in order to maximise the benefits of scale. Following the 2019 valuation, pool members will review their investment strategies and put revised strategies in place from 2020. From 2020, when new investment strategies are in place, pool members should make new investments outside the pool only in very limited circumstances.

6.2 A small proportion of a pool member's assets may be invested in local initiatives within the geographical area of the pool member or in products tailored to particular liabilities specific to that pool member. Local assets should:

- Not normally exceed an aggregate 5% of the value of the pool member's assets at the point of investment.
- Be subject to a similar assessment of risk, return and fit with investment strategy as any other investment.

6.3 Pool members may invest through pool vehicles in a pool other than their own where collaboration across pools or specialisation by pools can deliver improved net returns.

6.4 During the period of transition, while pool governance bodies and pool companies work together to determine and put in place the agreed range of pool vehicles, a pool member may make new investments outside the pool, if following consultation with the pool company, they consider this is essential to deliver their investment strategy. This exemption only applies until the pool vehicles needed to provide the agreed asset allocation are in place.

7 Infrastructure investment

7.1 Infrastructure investment has the potential to provide secure long term returns with a good fit to pension liabilities, and form part of investment strategies of authorities. The establishment of the pools was intended to provide the scale needed for cost-effective investment in infrastructure, and to increase capacity and capability to invest in infrastructure.

7.2 There is no target for infrastructure investment for pool members or pools, but pool members are expected to set an ambition on investment in this area. Pool companies may provide pool vehicles for investment in UK assets, or overseas assets, or both, as required to provide the risk and return profile to meet pool member investment strategies. However the Government expects pool companies to provide the capability and capacity for pools over time to move towards levels of infrastructure investment similar to overseas pension funds of comparable aggregate size.

7.3 Pool companies may provide pool vehicles for investment in existing (brownfield) or new (greenfield) infrastructure, based on an assessment of the benefits and risks in relation to pool member liabilities, and non-financial factors where relevant. Pool members may invest in their own geographic areas but the asset selection and allocation decisions should normally be taken by the pool company in order to manage any potential conflicts of interest effectively, maintain propriety, and ensure robust evaluation of the case for investment.

7.4 For the purpose of producing annual reports, infrastructure assets are defined in the Chartered Institute of Public Finance and Accountancy (CIPFA) guidance *Preparing the Annual Report* as follows:

Infrastructure assets are the facilities and structures needed for the functioning of communities and to support economic development. When considered as an investment asset class, infrastructure investments are normally expected to have most of the following characteristics:

- *Substantially backed by durable physical assets;*
- *Long life and low risk of obsolescence;*
- *Identifiable and reliable cash flow, preferably either explicitly or implicitly inflation-linked;*
- *Revenues largely isolated from the business cycle and competition, for example, through long term contracts, regulated monopolies or high barriers to entry;*
- *Returns to show limited correlation to other asset classes.*

Key sectors for infrastructure include transportation networks, power generation, energy distribution and storage, water supply and distribution, communications networks, health and education facilities, social accommodation and private sector housing.

Conventional commercial property is not normally included, but where it forms part of a broader infrastructure asset, helps urban regeneration or serves societal needs it may be.

7.5 All residential property is included in this definition of infrastructure. It is not restricted to social accommodation or private sector housing.

7.6 A variety of platforms may be required to implement the infrastructure investment strategies of pool members. Pool companies are expected to provide access to a range of options over time including direct and co-investment opportunities.

8 Reporting

8.1 Pool members are required to report total investment costs and performance against benchmarks publicly and transparently in their annual reports, following the CIPFA guidance *Preparing the Annual Report*, with effect from the 2018-19 report.

8.2 In summary, pool member annual reports should include:

- opening and closing value and proportion of pooled assets by asset class
- opening and closing value and proportion of local assets by asset class
- net and gross performance of pooled assets by asset class
- total costs of pooled assets by asset class
- for actively managed listed assets, net performance by asset class net of total costs compared to appropriate passive indices over a one, three and five year period
- net and gross performance of local assets by asset class
- total costs of local assets by asset class
- asset transition during the reporting year
- transition plans for local assets
- pool set-up and transition costs, presented alongside in-year and cumulative savings from pooling
- ongoing investment management costs by type, with a breakdown between pooled assets and local assets

8.3 Investments should be classed as pool assets on the basis of the definition in the CIPFA guidance *Preparing the Annual Report.*

For the purpose of defining those assets which are classed as being within an asset pool, 'pooled assets' are those for which implementation of the investment strategy – i.e. the selection, appointment, dismissal and variation of terms for the investment managers (including internal managers) – has been contractually, transferred to a third party out with the individual pension fund's control.

8.4 Any investment where a pool member retains the day to day management, or the responsibility for selecting or reappointing an external manager, is not a pool asset.

8.5 Pool members should provide a rationale for all assets continuing to be held outside the pool, including the planned end date and performance net of costs including a comparison which costs of any comparable pool vehicles. They should also set out a high level plan for transition of assets.

8.6 The SAB will publish an annual report on the pools based on aggregated data from the pool member annual reports, in the Scheme Annual Report. Pool members should comply with all reasonable requests for any additional data and information from the SAB to enable it to publish a comprehensive report.

8.7 Pool members should ensure that pool companies report in line with the SAB Code of Cost Transparency. They should also ensure that pool companies require their internal and external investment managers to do so.

8.8 Pool members should also ensure that the annual report of the pool company is broadly consistent with the reports of pool members, and with the Scheme Annual Report, in so far as it relates to their investments, and that the report includes a narrative to explain differences. These may arise for example from reporting periods of pool companies which differ from that of the pool member.

8.9 Pool members are required to report any change which results in failure to meet the requirements of this guidance to the LGPS Scheme Advisory Board (SAB) and to MHCLG.

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Email from Hymans Robertson LLP

In January 2019, the MHCLG published its draft statutory guidance on asset pooling. The consultation is open for 12 weeks (closing on 28 March). It is deemed an informal consultation which is addressed to "*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*".

Some noteworthy features of the consultation document include:

- Guidance will have statutory force
- The definition of "pooled assets" excludes passive investment in life policies held directly by administering authorities
- Pool members *must* appoint a pool company regulated by the FCA (3.2)
- Pool members *should* consider moving from active to passive investment where active management has not generated better net of fees performance over a reasonable period (3.6)
- Pool members *should* take account of benefits across the pool and the scheme as a whole and should not seek simply to minimise costs in the short term (4.4)
- Inter-authority payments *may* be used to share transition costs equitably between pool members (5.4)
- There are tighter definitions of the conditions to justify keeping assets outside of the pool (existing "retained" assets and new investments)
- From 2020 it is expected that pool members "*should* make new investments outside the pool only in very limited circumstances" (6.2)
- Pool members may invest in vehicles provided by other pools where collaboration between pools or specialisation can deliver improved net returns (6.3)
- There is no specific target for infrastructure (7.2)
- All residential property is included in the definition of infrastructure (7.5)
- Extensive reporting requirements on costs and performance relative to relevant indices (8.2) kick in with effect from the 2018-19 report (8.1)

We have prepared the attached note which provides a factual summary of the points raised in the consultation - please feel free to share this summary with your Committee.

We look forward to discussing this note and the consultation with you over the coming weeks.

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Local Government Pension Scheme: Draft Statutory guidance on asset pooling

This note provides factual information relating to the Ministry of Housing, Communities and Local Government's informal consultation on the Draft Statutory guidance on asset pooling. This note is addressed to the Fund's Officers and Committee(s). It is not for public distribution.

Timetable

The consultation was issued on 3 January 2019, it is open for 12 weeks and will close on 28 March. It is deemed an informal consultation which is addressed to *"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".* The SAB secretariat will be assisting MHCLG with the consultation but all responses should be sent to LGPensions@communities.gov.uk.

Background

The guidance sets out the requirements on administering authorities in relation to pooling assets and 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."* As a reminder, we attach links to the replaced documents at the foot of this document[1].

Overview

Further to the introduction the consultation is broken into 7 sections which we set out below. As outlined in the title, the governance is statutory. Throughout the document, there is frequent use of certain words, in particular "must", "should" and "may" in relation to different points being made. Each highlights the extent to which adherence is expected.

Definitions

This section sets out a number of definitions relating to pooling, including,

'Pool governance body' the body used by pool members to oversee the operation of the pool and ensure that the democratic link to pool members is maintained (for example, Joint Committees and officer committees).

'Pool company' 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.

'Pool fund' a regulated unitised fund structure operated by a regulated pool company, such as an Authorised Contractual Scheme (ACS).

'Pool member' an LGPS administering authority which has committed to invest in an LGPS pool and participates in its governance.

It also defines Pool vehicles, retained assets and local assets which are all covered in later sections of the consultation.

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1 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/479925/criteria_and_guidance_for_investment_reform.pdf http://lgpslibrary.org/assets/statgui/ew/201609ISS.pdf http://lgpslibrary.org/assets/statgui/ew/201707ISS.pdf

Structure and scale

This section reiterates the aims of pooling, that a**ll** administering authorities must pool their assets and that pool members must appoint a pool company or companies to implement their investment strategies, stating clearly, *"It is for the pool companies to decide which investment managers to use for pool vehicles"*. It also states that a pool company must be a company regulated by the FCA

It is stated that Pool governance bodies, working with the Pool company, "*should regularly review the provision of services to the pool, and the process of procurement, to ensure value for money and cost transparency*" and *"the balance between active and passive management in the light of performance net of total costs. They should consider moving from active to passive management where active management has not generated better net performance over a reasonable period*".

Governance

It was stated that pool governance bodies must be established in order to "set the direction of the pool and hold the pool company to account" while pool members through their own governance arrangements will be "*responsible for effective governance and for holding pool companies and other service providers to account*". In addition "*Strategic asset allocation remains the responsibility of pool members*". It also states Pension Committees should take a long term view of the potential benefits of pooling, taking into account "*the benefits across the pool and across the scheme as a whole…and should not seek simply to minimise costs in the short term*." It also notes that Pension Boards can have a role in governance arrangements.

It also states that part of pool governance bodies' role is to decide the pool's policy on which aspects of asset allocation are "*strategic*" and which are "*tactical*", with the guidance stating that, "*governance bodies should be mindful of the trade-off between greater choice and lower costs*". It is also noted that the position between what is deemed strategic and what is tactical is something that might change over time. It is also states that, "*Pool members should set out in their FSS and ISS how they, through the pool governance body, have balanced these considerations and how they will keep this under regular review*".

Transition of assets to the pool

There are a number of comments on treatment of costs, including

"Transition of listed assets should take place over a relatively short period." and *"..should see to minimise transition costs to pool members while effectively balancing speed, cost and timing, taking into account exit or penalty costs and opportunities for crossing trades."* And *"Inter-authority payments (or other transfers of value) may be desirable in order to share these costs equitably between pool members. The Government's view is that such payments are investment costs within Regulation 4(5) of the 2016 Regulations, and payments made by a pool member to meet its agreed share of costs may be charged to the fund of that pool member, whether the payments are made to other pool members, the pool company, or another body by agreement."*

It is noted that "*In exceptional cases, some existing investments may be retained by pool members on a temporary basis*" citing assets that need to be held to maturity as an example. It also notes that *"Pool members may also retain existing direct property assets where these may be more effectively managed by pool members"* and *"…pool members may retain the management of existing long term investment contracts where the penalty for early exit or transfer of management would be significant. These may include life insurance contracts ('life funds') accessed by pool members for the purpose of passive equity investment, and some infrastructure investments."*

For assets held outside the pool it is stated that, *"Pool members, working with the pool company, should undertake regular reviews (at least every three years) of retained assets and the rationale for keeping these assets outside the pool."*

Making new investments outside the pool

There is an expectation that new investments will be made through the pool company with 2020 being set as the target timescale and a statement that "*pool members should make new investments outside the pool only in very limited circumstances."*

Exceptions (to pool members investing in their own pool) include,

"A small proportion of a pool member's assets may be invested in local initiatives within the geographical area of the pool member or in products tailored to particular liabilities specific to that pool member", with clarity that Local assets should*, "not normally exceed an aggregate 5% of the value of the pool member's assets at the point of investment and be subject to a similar assessment of risk, return and fit with investment strategy as any other investment.";* or "*may invest ….in a pool other than their own where collaboration across pools or specialism by pools can deliver improved net of fee returns"*

Infrastructure investment

There are a number of infrastructure related aspects noted in the document. Although supportive of the asset class, the consultation states, "*There is no target for infrastructure investment for pool members or pools, but pool members are expected to set an ambition on investment in this area."* "*Government expects pool companies to provide the capability and capacity for pools over time to move towards levels of infrastructure investment similar to overseas pension funds of comparable aggregate size*".

It is explicitly stated that Pools are expected to provide a range of options to accessing the asset class and may offer brown and greenfield exposure to the asset class. There is also comment that, "*Pool members may invest in their own geographic areas but the asset selection and allocation decisions should normally be taken by the pool company in order to manage any potential conflicts of interest effectively, maintain propriety, and ensure robust evaluation of the case for investment*". The consultation states for the purpose of annual accounts CIFPA's definition for the asset class should be used (which includes a comment that conventional property is not normally included). The consultation also makes it clear that residential property is defined as infrastructure.

Reporting

There are a number of cost and pooling related requirements, including stating that, *"Pool members are required to report total investment costs and performance against benchmarks publicly and transparently in their annual reports, following the CIPFA guidance Preparing the Annual Report, with effect from the 2018-19 report."*

The CIPFA guidance is also to be used when it comes to defining which assets are to be deemed pool assets, "*'pooled assets' are those for which implementation of the investment strategy – i.e. the selection, appointment, dismissal and variation of terms for the investment managers (including internal managers) – has been contractually, transferred to a third party out with the individual pension fund's control."* Pool members should *"provide a rationale for all assets continuing to be held outside the pool, including the planned end date and performance net of costs including a comparison which costs of any comparable pool vehicles. They should also set out a high level plan for transition of assets."*

It is stated that the SAB will publish an annual report on the pools based on data from the pool member annual reports. It is also stated that pool companies should report in line with the SAB Code of Cost Transparency, with pool companies requiring their internal and external investment managers to do likewise. The final point on the consultation is to state that *"Pool members are required to report any change which results in failure to meet the requirements of this guidance to the LGPS Scheme Advisory Board (SAB) and to MHCLG."*

Prepared, for and on behalf of Hymans Robertson LLP, by:-

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