

## **PENSION FUND COMMITTEE – 23 JUNE 2017**

### **BRUNEL PENSION PARTNERSHIP - UPDATE**

#### **Report by the Director of Finance**

##### **Introduction**

1. Under The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, all LGPS Funds in England and Wales are required to enter into pooling arrangements for the management of their investment assets. The previous Committee alongside the Fund's officers undertook a significant amount of work since the initial Government announcement of the pooling requirement in July 2015.
2. This work led to an initial decision to notify Government in February 2016 that the Oxfordshire LGPS Fund was minded to join the Brunel Pension Partnership. This Partnership comprised 9 other LGPS Funds, being Avon, Buckinghamshire, Cornwall, Devon, Dorset, the Environment Agency, Gloucestershire, Somerset and Wiltshire. This decision was re-confirmed in a second return to Government in July 2016, and then endorsed by the full Council in December 2016 after consideration of the full business case for the establishment of the partnership.
3. A key element of the business case was the setting up of a Financial Conduct Authority (FCA) regulated company to be named Brunel Pension Partnership Limited (BPP Ltd.). The project has now reached the key point at which the company needs to be formally established to allow work to continue to meet the Government's timetable for the new pooled arrangements to be operational by April 2018.

##### **Establishment of Brunel Pension Partnership Limited**

4. The Business Case envisaged the creation of Brunel Pension Partnership Limited ("BPP Ltd" or the "Company"), which is the company to be set up to manage the pooling of the assets of the 10 BPP Administering Authorities. The structure and constitution of the company was to be determined to meet the needs of the 10 authorities in terms of their pooling responsibilities, as well as meeting the requirements of the Financial Conduct Authority.
5. As would be expected given the complexity of the project and the involvement of the 10 Funds, the documents have been subject to a considerable level of review and comment. This includes review by the s151 officers / chief finance officers, monitoring officers / legal directors, heads of pensions, the pension committee representatives of each of the Funds, and BPP Ltd through its chair and interim managing director.

6. The legal documents have mostly been prepared by Osborne Clarke (legal advisers to the project), with input from PricewaterhouseCoopers (PwC – commercial advisers to the project) and Alpha Financial Markets Consulting (specialist financial advisers, including support for the FCA application).
7. BPP Ltd will be a private company limited by shares, registered in England and Wales and with its registered office in Bristol. The Company will be one tenth owned by each of the 10 Funds and each of the Funds will be responsible for providing one tenth of the capital required by the Company to be set up. Once operational, each Fund will be charged a service fee depending on the services taken up and assets under management.
8. The key documents required for the creation of BPP Ltd are as follows:
  - Articles of Association
  - Shareholders' Agreement
  - Services Agreement
  - Business plan
  - Terms of reference of the Oversight Board
  - Terms of reference of the Client Group
  - Terms of reference of the Audit, Risk and Compliance Committee
  - Terms of reference of the Remuneration Committee
  - Remuneration Policy
  - Pricing Policy

Further detail of each of these is given below. The full documents are available to Members of the Committee on request to Sean Collins, Service Manager (Pensions).

#### Articles of Association

9. This document is required by company law, and will set out the Company's constitution and regulate the relationship between the Administering Authorities and BPP Ltd. It sets out the Company's powers and procedures and will be filed at Companies House. It is mostly procedural and mechanical, with the vast majority of the substance in the Shareholders' Agreement.

#### Shareholders' Agreement

10. This regulates key aspects of the relationship between the Administering Authorities as shareholders of the Company as well as with the Company itself. BPP Ltd will be a party to this agreement and it will define contractually the manner in which the shareholders will control BPP Ltd, and include contractual restrictions on what the company can do rather than limiting the power of the Company itself. Key provisions are:
  - Reserved matters and special reserved matters: The Shareholders' Agreement sets out certain matters which cannot be undertaken by the Company without first obtaining the approval of shareholders. There are two lists – "special reserved matters" which cannot be undertaken without the approval of all shareholders (including approval of the

business plan/budget and other matters considered fundamental to the structure and rationale of the project) and other matters which require the approval of 80% of the shareholders (i.e. eight out of the ten) (matters which are considered less significant but over which some measure of control is considered desirable without the ability for any one (or two) Funds to veto). It is worth noting that if any action is included in the business plan (which must be unanimously approved) then it is considered approved for the purposes of the reserved/special reserved matters. A full list of the Special Reserved Matters and Reserved Matters is included in exempt Annex 1 (which is confidential until such time as all legal negotiations are concluded).

- Initial funding: The Shareholders' Agreement sets out the requirement for each Administering Authority to provide the capital required for the Company to be set up and become operational, which is to be provided one tenth each by each Administering Authority. This may be payable in tranches rather than all up front.
- Exit charge: One of the matters subject to the most debate has been the proposal for there to be an exit charge. This would be a charge payable by an Administering Authority which exits from the pool operated by BPP Ltd. The proposal is intended to model an estimate of the loss incurred by the Company in the event that an Administering Authority was to exit. This covers both direct costs of disinvestment together with a formula for calculating the anticipated loss resulting from loss of scale and the operating costs / overheads of the Company (which will then fall to be borne by the remaining authorities). This would be expressed as a maximum or default amount, which would be subject to a duty to mitigate by BPP Ltd and would be reduced to reflect any such mitigation and to the extent otherwise agreed by the remaining Administering Authorities. This approach should provide certainty of a maximum outcome upon exit for any exiting authority together with a reasonable degree of protection for the remaining pool members that the economics of the model should not be disadvantaged too significantly by any exit.
- Directors: The Shareholders' Agreement sets out the agreed structure of the board of the Company, being four executive directors, one non-executive chair, two non-executive directors and a shareholder representative non-executive director. Directors must be approved by shareholders by 80% majority.

#### Services Agreement

11. The Services Agreement will be entered into between the 10 Funds and BPP Ltd when the pool becomes operational in April 2018 (or shortly before).
12. This is a comprehensive document which sets out in detail the key operational and technical aspects. It covers such matters as the following: definition of services to be provided, duty of care obligations, the portfolio construction terms, FCA authorisation obligations, pricing terms, managing conflicts of interest, reporting and valuation provisions. Key provisions are:

- Investment Objectives and Portfolios: The Services Agreement sets out the portfolios into which the Administering Authorities' assets will be invested and the procedure whereby new portfolios can be created (at the request of Administering Authorities) and portfolios can be deleted if no longer required. There has been a level of debate around whether Administering Authorities will be able to continue holding segregated mandates – i.e. investments which cannot themselves be pooled (for example closed-ended private equity funds). The agreed position is that the Services Agreement will not prohibit such holdings, and the Client Group will have the ability to approve these on a case-by-case basis, after undertaking appropriate cost/benefit analysis.
- Services: Schedules to the Services Agreement set out the Core Services and the Elective Services to be provided by BPP Ltd. The Core Services will be provided to all Administering Authorities and these cover the design of portfolios, transitioning of assets, asset management and reporting. Administering Authorities may separately agree with BPP Ltd. to be provided with Elective Services for an additional fee. Elective Services include reviewing an Administering Authority's investment strategy statement, project support, and additional levels of reporting.
- Reporting: BPP Ltd. will provide each Administering Authority with quarterly and annual reports containing financial information, investment performance analysis and written commentary. An example form of report will be attached to the Services Agreement.
- Liability: There has been debate around whether Administering Authorities should be able to bring a claim against BPP Ltd. should it be in breach of its obligations under the Services Agreement (in the same way that would be seen in a usual investment management agreement). The position has been agreed where a claim can be brought, but subject to the terms of the Shareholders' Agreement (under which there is a duty to keep all other Administering Authorities informed of any such claim).

#### Business Plan

13. The Business Plan is not a legal document but is important in that it defines the purpose and freedom of the Company to operate. As noted above, to the extent that an action is included within the Business Plan, the Company need not come back to the Administering Authorities to request permission to undertake the relevant action.

#### Terms of reference for Oversight Board

14. These set out the procedures and responsibilities of the Oversight Board, which is intended to have a supervisory function. It will include representatives of each of the Funds, together with two representatives of fund members. It will not be a joint committee and does not have formal decision making powers.

#### Terms of reference for Client Group

15. These set out the procedures and responsibilities for the Client Group, which will provide practical and technical support, guidance and assistance to the

Oversight Board. It will comprise one representative of each of the 10 Funds. As with the Oversight Board, the Client Group has no formal decision-making powers.

#### Terms of reference for the Audit, Risk and Compliance Committee

16. These set out the procedures and responsibilities of the Audit, Risk and Compliance Committee, which is a committee of the board of directors of the Company. This committee will be comprised of at least three members all of whom must be non-executive directors of the Company (including the Shareholder non-executive director).

#### Terms of reference of the Remuneration Committee

17. These set out the procedures and responsibilities of the Remuneration Committee, which is a committee of the board of directors of the Company. This committee will be comprised of at least three members all of whom must be non-executive directors of the Company (including the Shareholder non-executive director) and shall be chaired by the chair of the Company.

#### Remuneration policy

18. The remuneration policy defines the key elements of remuneration, particularly for senior executives. Changes to that policy (or remuneration which is inconsistent with that policy) will be a special reserved matter, and hence will require unanimous express shareholder approval. Key provisions are:
  - Remuneration caps: Remuneration caps will be included for different levels of employees, reflecting a consistency with the approach for the public sector.
  - Performance related pay: There will be no performance related pay (though with the ability to give recognition awards).
  - LGPS membership: Membership of the LGPS will be offered as part of the remuneration package for new employees. The LGPS is to be open for the first three years, and revisited thereafter.

#### Pricing Policy

19. The pricing policy sets out the basis on which the company will charge the 10 administering authorities. The initial pricing policy is seen as an interim document to cover the transition period. As the partnership will still be very much in development as the new portfolios are created, and assets transitioned, costs will continue to be re-charged on an equal tenth basis where general overheads, and on a pro-rata to total assets under management for those costs deemed to vary on the basis of size of investments. Only exception will be those staff specifically employed to develop in-house capacity for managing private market investments which will be recharged based on private market allocations. All elective services will be charged at cost.
20. The Pricing Policy includes a built in review to move as many costs as possible to a portfolio specific charge, with portfolio costs then recharged to the administering authorities' pro-rata to their allocation to each portfolio.

## Decisions required

21. As noted above, the legal documents have been subject to considerable discussion over recent months, and it is understood that all key issues have now been resolved, and final versions of the documents were being drafted at the time this report was written. The Finance and Legal Officers Assurance Group (FLAG) and the Shadow Oversight Board are both due to meet once more before the Committee meeting on 23 June, and any significant issues will be raised with the Committee.
22. The Company needs to be in place by 17 July 2017 if the project is to stick with the current timetable. It is therefore necessary for the Committee to delegate the final decision to execute the legal documents to the Director of Finance and the Director of Law and Governance in consultation with the Committee Chairman, Vice Chairman and Opposition Spokesperson.
23. On the assumption that the legal documents are agreed by all 10 administering authorities, it will then be necessary to appoint a representative to attend the Oversight Board and any Shareholders meetings on behalf of Oxfordshire. As noted above, the Oversight Board is not a formal decision making body, so no additional delegations need to be assigned to the individual representing Oxfordshire there. However, the Shareholder Representative will be required to exercise a vote and the Committee therefore need to determine the extent of any delegations.
24. It is envisaged that Shareholders will meet for the Annual General Meeting which will involve a number of routine and non-contentious resolutions plus approval of the annual business plan and budget. This last item is seen as a Special Reserved Matter. .
25. For the AGM, it is likely that the date will be known well in advance, and papers made available in advance, which would allow the Pension Committee to meet to discuss and approve any resolutions in advance. In the case of any unplanned reserved matters raised during the year, these will, if the timings permit, either be brought before the next scheduled Pension Fund Committee meeting or before an extraordinary Pension Fund Committee meeting.
26. Having approved the relevant resolutions, it is proposed that, in the case of the AGM, the Pension Fund Committee appoint and delegate responsibility to a Shareholder representative to attend the AGM and cast Oxfordshire's vote.
27. , As noted above, the legal documents include a proposal for the initial funding of the company through all 10 administering authorities making a payment for their share. Following advice from our commercial advisers, the proposal differs from that assumed in producing the business case, as the latest option is deemed to offer greater tax advantages in the future.
28. As a consequence, the payment due from Oxfordshire will be structured differently to that assumed when the budget was approved by Committee in March 2017, with a contribution to the share capital of c£900,000 required to be made, alongside a c£300,000 reimbursement from the Company in respect of development costs incurred in establishing the Company. Whilst this matches the net figure of £600,000 included in the budget, the Committee are recommended to agree the necessary amendment to the budget to reflect the new structure of the payments.

## **Other Updates**

29. The reasons for the Company to be established by 17 July relate to progress on other elements of the project. In particular, the tender for the Administrator/Custodian for the Partnership closed on 5 June 2017, and responses are currently being evaluated with a view to selecting a preferred supplier by 17 July 2017. The issue of the standstill notice to confirm the preferred supplier, and allow unsuccessful tenderers to raise any objections to the process, will require the Company to be formally constituted as the notice is published in their name.
30. Interviews for the three remaining non-executive positions, including the Shareholder non-executive director were held on 1 and 2 June. Appointments are subject to ratification by the Shadow Oversight Board at their meeting on 20 June 2017, and again the company needs to exist to enable contracts to be issued. Similarly, the advertisements for the four executive posts have been issued with a closing date of 9 June 2017. Interviews for all roles are planned for the first two weeks in July, and again require the establishment of the company for contracts to be issued.
31. A third key area of focus over recent months has been the identification of suitable office accommodation for the new company. Unfortunately, the space initially identified is no longer available as the main leaseholder has determined to expand into the space once ear-marked. However, a second site identified in the initial trawl of properties is still available, and this is being progressed. The site is within Bristol, in very close proximity to Temple Meads Railway Station.

## **RECOMMENDATION**

32. **The Committee is RECOMMENDED to:**
  - (a) delegate to the Director of Finance and the Director of Law and Governance, in consultation with the Committee Chairman, Deputy Chairman and Opposition Spokesperson the decision to execute the legal documents for the establishment of the Brunel Pension Partnership Limited;**
  - (b) agree an individual to represent the Committee on the Oversight Board;**
  - (c) agree an individual to act as the Shareholder's representative to attend the Shareholders' annual general meeting and to cast Oxfordshire's vote in accordance with the Committee's decision;**
  - (d) agree a virement to the annual budget to allow for the latest proposal for the initial funding of the company as set out in paragraph 28 above; and**
  - (e) note the progress set out in the other updates above.**

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