

## **PENSION FUND COMMITTEE – 15 SEPTMEBER 2017**

### **SCHEME ADVISORY BOARD CONSULTATIONS**

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

##### **Introduction**

1. The Scheme Advisory Board (SAB) which was set up under the Public Service Pensions Act 2013 to advise the Secretary of State and to act as a co-ordinator for best practice for the individual LGPS pension funds, has recently issued a number of key papers. Two of these are consultation papers with a closing date of 29 September 2017. The third is a template to enable LGPS Funds to seek to opt up to professional status under the new Markets in Financial Instruments Directive (MiFID II).
2. This report invites the Committee to consider the implications of the three papers, and to agree responses to the two consultation documents and a way forward in response to MiFID II.

##### **Consultation on Academies Objectives**

3. In the summer of 2016, the Scheme Advisory Board commissioned a report on the implications for the LGPS of the Department for Education's programme of converting schools to academy status. The work was awarded to PwC who produced a report in early 2017 following consultation with key stakeholders. The report attempted to set out the views and issues raised by the key stakeholders, without setting out any recommendations on the way forward (in line with the instructions from the SAB).
4. The report was considered by the SAB at its meeting in March 2017. At the end of the month, the Chairman of the Board met with Ministers from both the Department for Communities and Local Government and the Department for Education to further discuss the results. The meeting with Ministers agreed that some improvements were required to the current arrangements and that in the first instance it should be considered to what extent these could be delivered by additional guidance notes to LGPS Pension Funds, or by changes within the LGPS Regulations. It was noted that if such measures could not be agreed, Ministers would also consider more radical action outside of the LGPS regulations through the development of primary legislation.
5. The issues identified within the PwC report (which is published on the Scheme Advisory Board's website), were grouped into issues associated with Policy & Governance, Administration and Operations and Contributions and Finance. Many of these issues stem from a lack of guidance to schools contemplating the switch to academy status, the complexity of the LGPS and the lack of

understanding within academies and their payroll providers, the different approaches taken by the LGPS Funds cross England and Wales (a particular concern for those Multi-Academy Trusts with schools in more than one fund), the level of out-sourcing from the academies themselves, concerns about the financial covenant of academies, and the lack of representation of the academy sector within current LGPS governance arrangements.

6. The SAB has currently commissioned additional data from the fund actuaries to provide further information on the issues, and help develop next steps. As part of this exercise, the SAB has launched a consultation exercise to seek stakeholder support for a set of key level objectives against which future proposals can be evaluated.
7. The draft objectives set out by the SAB within the consultation document are as follows:
  - (a) Protect the benefits of scheme members through continued access to the LGPS;
  - (b) Ring fence local tax-payers and other scheme employers from the liabilities of the academy trust sector;
  - (c) Improve the efficiency and effectiveness of administrative practices;
  - (d) Increase the accuracy and reliability of data;
  - (e) Change should not significantly alter cash flows at the fund level; and
  - (f) Change should not significantly alter assets at the pool level.
8. From an administering authority perspective, the draft objectives appear sound and should be supported. The first, fifth and sixth objective all aim to protect the sustainability of individual pension funds, which would be threatened by large scale withdrawal of scheme members of scheme employers, and for Oxfordshire would switch the Fund from cash positive to cash negative. This in turn would require an immediate review of our investment strategy, with potentially a reduction in the level of investment risk and therefore and increase in employer contributions for the non-academy scheme employers.
9. The draft response included at Annex 1 therefore responds to support the draft objectives for the academies project.

### **Cross Pool Information Forum**

10. The second consultation document issued by the SAB covers the proposal to establish a Cross Pool Information Forum (CPIF). The proposal was agreed in principle at the Board meeting in June 2017, to establish an elected member forum to share and disseminate information of the pooling of assets.
11. The proposal for CPIF has been discussed at the Cross Pool Collaboration Group (CPCG), and the Client Group and Oversight Board for Brunel. The CPCG which is an officer group with representations from all 8 pools had a number of concerns regarding the establishment of the Forum. In large part, these concerns were in respect of timing, with the common view that such a

group would have had much greater value if established at the beginning of the pooling process, rather than now as the detailed arrangements for the individual pools are being finalised. CPCG also expressed some concerns about the support arrangements for such a Forum and in particular whether officer time from the pools would need to be diverted from the key work in setting up the new arrangements.

12. The Client Group at Brunel shared the concerns of CPCG and added further concerns including the risk that the new CPIF would cut across the work of the SAB itself and dilute the voice of the LGPS in dealing with the Government. There was no clear added value that was seen to justify the time spent by elected members in attending the Forum and disseminating information back to the fellow members of the pool. The Client Group felt that the objectives set for the CPIF could be better met by holding specific conferences/seminars where members of Pension Committees and Boards could attend and receive presentations from key individuals within each pool and discuss key issues.
13. The Shadow Oversight Board appreciated the concerns of the CPCG and the Client Group. There was though also a view expressed that not all elected members had felt fully engaged in the process, and we should perhaps at least attend the initial meeting of the Forum to assess its value. There was also a view that elected members needed to work closer together across pools to address issues such as seeking Government approval to waive tax charges during the transition of assets to pools.
14. There was no discussion at the Shadow Oversight Board as to how Brunel would choose any representatives to attend the CPIF, nor how these representatives would feed back to the other members of the Oversight Board, and the elected members of the underlying funds themselves. Nor was it discussed how any expenses associated with attending the CPIF would be funded.
15. The consultation document is predicated on the fact that the CPIF has been agreed in principle. The Consultation questions therefore focus on the remit (should it be wider than receiving, sharing and disseminating information), Forum membership – proposed as a maximum of three representatives from each pool with the chair to be selected from within the chosen membership, frequency of meetings – proposed as quarterly, process – the assumption is that there would be no voting policy as the Forum is information only and not decision making, and would be supported by the secretariat of the SAB.
16. The response contained at annex 2 has been drafted on the basis that this Committee wishes to support the establishment of the CPIF and accepts the proposed working model. However, Part 2 of the consultation covers the organisation of an open session along the lines favoured by the Client Group. If it is the view of this Committee that this open session is sufficient to meet the information requirements of elected members, the consultation response can be amended accordingly.

## **Markets in Financial Instruments Directive (MiFID II)**

17. The Markets in Financial Instruments Directive is a piece of EU legislation that regulates firms who provide services to clients linked to financial instruments. Compliance with the directive is overseen by the Financial Conduct Authority who in July 2017 issued their final policy statement covering the implementation of the directive.
18. A key element under MiFID II is the re-classification of all local authorities as retail investors, rather than professional investors as at present. This change will be effective from 3 January 2018. Whilst retail clients receive a number of additional protections in their dealing with financial companies, it is also the case that a number of the fund managers and other service providers who currently provide services to the Pension Fund are prohibited from dealing with retail clients. Even where companies are entitled to deal with retail clients, the additional cost and administration involved in providing the necessary protections could mean that many would refuse to continue to provide existing services. If the Pension Fund remains as a retail investor it is likely to significantly restrict the range of investment options available to the Fund which would impact on the ability of the Fund to deliver its agreed asset allocation. .
19. MiFID II does allow investors defined as retail clients to opt up to professional client status if they meet set criteria. Following the intervention of the Scheme Advisory Board, the Local Government Association, the Department for Communities and Local Government, the Investment Association and the LGPS funds themselves, the FCA agreed criteria to better suit the unique circumstances of local authorities and administering authorities in particular. The tests recognise any authority administering an LGPS as able to meet the quantitative test. The qualitative test is applied to the competency of the authority as a whole including its advisors rather than an individual within the Fund.
20. Institutions covered by the MiFID II regulations will be required, on receipt of an application from a client to be treated as a professional investor, to make an assessment of whether the quantitative and qualitative criteria have been met. The SAB, LGA, Investment Association and others have now produced a standard template to enable funds to apply to be opted up to professional status by the relevant institutions. A copy of this template and the accompanying information template are attached as Annexes 3 and 4 to this report. The letter template includes a full list of the protections lost by opting up to professional client status. Before we start to invest through Brunel Pension Partnership Ltd we will also need to complete the opt up process with the company.
21. Applications can be made in respect of either all of the services offered by the institution (even if not already being accessed) or a particular service only.
22. The opt up process must be completed with each financial institution before the 3 January 2018, or there is a risk to the continuity of the current

arrangements. To that end the committee are recommended to delegate responsibility to the Service Manager (Pensions) for the completion of each of the respective opt up requests.

## **RECOMMENDATION**

**23. The Committee is RECOMMENDED to:**

- (a) agree the consultation response on academies objectives as set down in Annex 1;**
- (b) determine whether they wish to support the establishment of the Cross Pool Information Forum, and agree the consultation response at Annex 2 as amended where appropriate;**
- (c) note the consequences of electing not to opt up to professional client status with all relevant institutions including Brunel Pension Partnership Ltd;**
- (d) agree that the Pension Fund should seek to opt-up to elective professional client status with all relevant institutions and should commence this process as soon as possible;**
- (e) acknowledge and agree, in applying to be treated as a professional client, to forgo the protections afforded to retail clients; and**
- (f) delegate responsibility for completing and submitting all the applications, and whether this is on a full or single service basis, to the Service Manager (Pensions).**

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