

# Pensions CIV Sectoral Joint Committee

17 December 2014: 14:30 – 16:30

Conference Suite (1<sup>st</sup> Floor)

At London Councils offices, 59½ Southwark St., London SE1 0AL

Refreshments will be provided

London Councils offices are wheelchair accessible

**Labour Group pre-meeting:** Room 4 (1<sup>st</sup> Floor) 14:00

(Political Adviser: 07977 401955)

**Conservative Group pre-meeting:** Room 1 (1<sup>st</sup> Floor) 14:00

(Political Adviser: 07903 492195)

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### **\*Declarations of Interests**

If you are present at a meeting of London Councils' or any of its associated joint committees or their sub-committees and you have a disclosable pecuniary interest\* relating to any business that is or will be considered at the meeting you must not:

- participate in any discussion of the business at the meeting, or if you become aware of your disclosable pecuniary interest during the meeting, participate further in any discussion of the business, or
- participate in any vote taken on the matter at the meeting.

These prohibitions apply to any form of participation, including speaking as a member of the public.

It is a matter for each member to decide whether they should leave the room while an item that they have an interest in is being discussed. In arriving at a decision as to whether to leave the room they may wish to have regard to their home authority's code of conduct and/or the Seven (Nolan) Principles of Public Life.

\*as defined by the Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012

# Pensions CIV Sectoral Joint Committee

## Terms of Reference and Notification of Membership

Item no 5

**Report by:** Hugh Grover      **Job title:** Programme Director London LGPS CIV

**Date:** 17 December 2014

**Contact Officer:**

**Telephone:** 020 7934 9942      **Email:** [hugh.grover@londoncouncils.gov.uk](mailto:hugh.grover@londoncouncils.gov.uk)

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### Summary

The Pensions CIV Sectoral Joint Committee has been established in accordance with recommendations made to London Councils' Leaders' Committee on 11 February 2014 and decisions taken by participating London boroughs and the City of London Corporation in accordance with those recommendations.

This report presents the committee with its current Terms of Reference as agreed, in principle, by London Councils Leaders' Committee at its meeting of 11 March 2014.

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**Recommendations** The committee is recommended to:

- i. Note the contents of this report; and
  - ii. Note the provisional Terms of Reference at Annex
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## Terms of Reference and Notification of Membership

1. The Pensions CIV Sectoral Joint Committee has been established in accordance with recommendations made to London Councils' Leaders' Committee on 11 February 2014 and decisions taken by participating London boroughs and the City of London Corporation in accordance with those recommendations.
2. The committee will take decisions in accordance with the functions which have been delegated to it by the participating local authorities. The committee will collectively act as the shareholder of the ACS Operator and each shareholder (i.e. the participating local authorities) will nominate a representative to the Pensions CIV Joint Committee to act for it.
3. The committee will operate under London Councils governance arrangements<sup>1</sup> and in practice will fulfil two roles:
  - i. To act as the shareholder body for general meetings of the ACS Operator for those London local authorities that have chosen to take a shareholding in the Authorised Contractual Scheme (ACS) Operator company established for the purposes of a London Pensions Collective Investment Vehicle (CIV). This would relate to usual shareholder powers such as appointing the directors (subject to FCA approval of the appointees) and auditors of the ACS Operator, changing the articles of association of the ACS Operator, and the ability to wind up the ACS Operator; and
  - ii. To act as a forum for the participating authorities to consider and provide guidance on the direction and performance of the CIV as an investment vehicle.
4. The committee will be guided by a set of Terms of Reference (ToR). Attached at Annex A are the current ToR as agreed, in principle, by Leaders' Committee at its meeting of 11 March 2014. These were agreed in anticipation of sufficient boroughs agreeing the recommendations of 11 February, and the incorporation of the ACS operating company (London LGPS CIV Ltd.), which would predicate the need for the establishment of this committee.
5. This set of ToR are subject to revision in the light of on-going work to settle the detail of the CIV's governance arrangements, revision of the 'model' Articles of Association that have been adopted by the company on incorporation, the drafting of a shareholder

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<sup>1</sup> The London Councils' Governing Agreement dated 13 December 2001 (as amended), London Councils' Standing Orders, Financial Regulations and other policies and procedures as relevant.

agreement, and in light of changes made to London Councils' Standing Orders. A revised ToR will be brought to a future meeting of the committee for approval before going to Leaders' Committee for agreement.

6. The committee will note that the current nominated members of the committee are set out in section 3 of the ToR at Annex A.

### **Recommendations**

7. The committee is recommended to note the contents of this report.

### **Legal implications**

8. As noted above, the committee will have two different reasons for convening, one as shareholders in a Private Limited Company and the other as members with a common interest in the pensions issues and the operation of the CIV. Annex B provides some clarity about the legal distinction.

### **Financial implications**

9. The administration costs of running the PSJC will be met by the participating authorities. The board of the ACS operator company is considering suitable models for recovering the costs of running the CIV which will include the costs of the PSJC.

### **Equalities implications**

10. There are no equalities implications for London Councils

### **Attachments**

- |         |   |
|---------|---|
| Annex A | Pensions CIV Joint Committee Terms of Reference       |
| Annex B | Brief guidance note on the dual role of the committee |

**1. Pensions CIV Joint Committee**

**Constitution**

- 1.a.1 The Pensions CIV Joint Committee is a sectoral joint committee operating under the London Councils governance arrangements.<sup>2</sup>
- 1.a.2 Each London local authority participating in the arrangements shall appoint a representative to the Pensions CIV Joint Committee being either the Leader of the local authority or the elected mayor as applicable or a deputy appointed for these purposes.<sup>3</sup>
- 1.a.3 The Pensions CIV Joint Committee shall appoint a Chair and Vice-Chair.
- 1.a.4 The Pensions CIV Joint Committee shall meet at least once each year to act as a forum for the participating authorities to consider and provide guidance on the direction and performance of the CIV, In addition, members of the Pensions CIV Joint Committee shall meet at least once each year at an Annual General Meeting of the ACS Operator in their capacity as representing shareholders of the ACS Operator.
- 1.a.5 Subject to Clause 1.1.4 above, meetings of the Pensions CIV Joint Committee shall be called in accordance with London Councils' Standing Orders and the procedure to be adopted at such meetings shall be determined in accordance with those Standing Orders.
- 1.a.6 If the Pensions CIV Joint Committee is required to make decisions on specialist matters in which the members of the Pensions CIV Joint Committee do not have expertise the Pensions CIV Joint Committee shall arrange for an adviser(s) to attend the relevant meeting to provide specialist advice to members of the Pensions CIV Joint Committee.

**Quorum**

- 1.a.7 The requirements of the Standing Orders of London Councils regarding quorum and voting shall apply to meetings of the Pensions CIV Joint Committee.

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<sup>2</sup> The London Councils' Governing Agreement dated 13 December 2001 (as amended), London Councils' Standing Orders, Financial Regulations and other policies and procedures as relevant.

<sup>3</sup> Clause 4.5 of the London Councils' Governing Agreement dated 13 December 2001 (as amended).

## Membership

Borough	Representative	Party
City of London	Mark Boleat	-
Barking & Dagenham	Dominic Twomey	Labour
Barnet	Mark Shooter	Conservative
Bexley	John Waters	Conservative
Brent	Shafique Choudhary	Labour
Camden	Peter Brayshaw	Labour
Croydon	Simon Hall	Labour
Ealing	Yvonne Johnson	Labour
Enfield	Toby Simon	Labour
Greenwich	Don Austen	Labour
Hackney	Robert Chapman	Labour
Hammersmith & Fulham	Iain Cassidy	Labour
Haringey	Jason Arthur	Labour
Harrow	Keith Ferry	Labour
Hounslow	Mukesh Malhotra	Labour
Islington	Richard Greening	Labour
Kensington & Chelsea	Quentin Marshall	Conservative
Kingston upon Thames	Eric Humphrey	Conservative
Lambeth	Adrian Garden	Labour
Lewisham	Mark Ingleby	Labour
Merton	Imran Uddin	Labour
Newham	Forhad Hussain	Labour
Redbridge	Elaine Norman	Labour
Richmond upon Thames	Thomas O'Malley	Conservative
Southwark	Fiona Colley	Labour
Sutton	Sunita Gordon	Liberal Democrat
Tower Hamlets	Clare Harrisson	Labour
Waltham Forest	Simon Miller	Labour
Wandsworth	Maurice Heaster	Conservative
Westminster	Suhail Rahuja	Conservative

## Terms of Reference

1.a.8 To act as a representative body for those London local authorities that have chosen to take a shareholding in the Authorised Contractual Scheme (ACS) Operator company established for the purposes of a London Pensions Common Investment Vehicle (CIV).

1.a.9 To exercise functions of the participating London local authorities involving the exercise of sections 1 and 4 of the Localism Act 2011 where that relates to the actions of the participating London local authorities as shareholders of the ACS Operator company.

To act as a forum for the participating authorities to consider and provide guidance on the direction and performance of the CIV and, in particular,



to receive and consider reports and information from the ACS Operator particularly performance information and to provide comment and guidance in response (in so far as required and permitted by Companies Act 2006 requirements and FCA regulations).

1.a.10 In addition, members of the Pensions CIV Joint Committee will meet at least once each year at an Annual General Meeting of the ACS Operator to take decisions on behalf of the participating London local authorities in their capacity as shareholders exercising the shareholder rights in relation to the Pensions CIV Authorised Contractual Scheme operator (as provided in the Companies Act 2006 and the Articles of Association of the ACS Operator company) and to communicate these decisions to the Board of the ACS Operator company. These include:

1.a.10.1 the appointment of directors to the ACS Operator board of directors;

1.a.10.2 the appointment and removal of auditors of the company;

1.a.10.3 agreeing the Articles of Association of the company and consenting to any amendments to these;

1.a.10.4 receiving the Accounts and Annual Report of the company;

1.a.10.5 exercising rights to require the directors of the ACS Operator company to call a general meeting of the company;

## Guidance note on the dual role of the committee

### 1. Overview

The Pensions CIV Joint Committee will in practice be fulfilling two roles:

- a) To consider and provide guidance on the direction and performance of the CIV (“**Joint Committee Meetings**”). Decisions can be taken at the committee relating to the operation and business of the ACS Operator but they will not be formal decisions of the ACS Operator unless either a general meeting of the ACS Operator (and not the committee) has been formally convened or a Board meeting of the ACS operator adopts the recommendations of the Joint Committee
- b) The formal shareholder meetings of the ACS Operator to take decisions on behalf of the participating London local authorities in their capacity as shareholders exercising the shareholder rights in relation to the ACS Operator (“**Shareholder Meetings**”).

There are various differences between the Committee meetings and the Shareholder Meetings, both in terms of how they are convened and who can attend. These differences are summarised below. In practice, the best way to conduct business is for a meeting of shareholders to be convened at the rising of the Joint Committee so that shareholders business can be transacted including any necessary formalising of any business of the joint committee:

### 2. Committee Meetings

The conduct of London Councils committee meetings are governed by London Councils’ Standing Orders which are contained in Schedule 6 of the Leaders’ Committee Governing Agreement.

### 3. Shareholder Meetings

The Shareholder Meetings are private meetings of the shareholders of the ACS Operator and only shareholders or their appointed representative may attend.

The conduct of the shareholder meetings will also be governed by London Councils’ Standing Orders as far as these are compatible with company law, or by company law where the requirements are different e.g. notice periods are longer under company law and there are rules around proxies which must be followed.

# Pensions CIV Sectoral Joint Committee

## Background and Progress Update

Item no: 6

**Report by:** Hugh Grover      **Job title:** Programme Director London LGPS CIV

**Date:** 17 December 2014

**Contact Officer:**

**Telephone:** 020 7934 9942      **Email:** [hugh.grover@londoncouncils.gov.uk](mailto:hugh.grover@londoncouncils.gov.uk)

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**Summary**      This report provides the committee with an update on progress towards establishing a Collective Investment Vehicle for those London boroughs that wish to participate in such arrangements.

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**Recommendations**      The committee is recommended to consider and note the contents of this report.

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# Progress report and proposed next steps towards a London LGPS CIV

## Introduction

1. The question of whether and if so how the Local Government Pension Schemes (LGPS) across London might work more closely together has been the subject of a number of reports to London Councils' Leaders' Committee and Executive since March 2012 (see 'Background Papers' below for a complete list of all reports). To provide leadership and direction to this consideration Leaders' Committee resolved to establish a Pensions Working Group (PWG) comprised of the then three London Councils' Party Group Leaders (Mayor Jules Pipe and Cllrs. Teresa O'Neill and Ruth Dombey) and three representatives from the Society of London Treasurers, supported by the then Director of Fair Funding, Performance & Procurement.
2. In response to a Pensions Working Group (PWG) update to its December 2013 meeting, Leaders' Committee resolved that London Councils should establish a designated fund with contributions from those boroughs interested in further exploration of proposals for the establishment of a London LGPS Collective Investment Vehicle (CIV) and that the funds collected should be used to pay for the professional costs associated with that exploration.
3. Since that meeting 30 London local authorities have become active participants in the CIV programme and have each contributed £25,000 to the designated fund. Three boroughs have decided not to participate at this time.
4. The fund is being used to commission specialist expert professional advice associated with the development of the proposed CIV. At this point £470,000 of the fund has been committed to cover the costs of expert advisors (Eversheds, Deloitte, Northern Trust (on a short contract leading to the February 2014 report to Leaders' Committee), and Mercer), and the engagement of a Programme Manager on a one year fixed-term contract.
5. At its February 2014 meeting, Leaders' Committee considered a report from the PWG, which presented a more detailed business case and proposals in respect of establishing a CIV with the underlying structure of a UK Authorised Contractual Scheme (ACS).
6. Leaders' Committee agreed the recommendations of the PWG, and resolved to endorse and recommend to each local authority which decides to participate that, in addition to matters connected to the establishment of an ACS operating company, a representative

body, in the form of a new Sectoral Joint Committee (the “Pensions CIV Joint Committee” (PCJC)), be established (pursuant to the existing London Councils Governing Agreement, dated 13 December 2001 (as amended)). That committee has now been formed and is meeting today for the first time.

7. This report provides an update to the PCJC on progress since the February meeting of Leaders’ Committee and sets out plans leading towards the eventual launch of the CIV.

### **Borough engagement**

8. The February 2014 report asked that Leaders’ Committee endorse and recommend to each local authority which decides to participate, that they make decisions based on a number of recommendations that would be necessary to the establishment of the CIV. Since then 30 boroughs have given formal notification (in the form of a letter to London Councils’ Chief Executive) that such resolutions have been made. Three have decided that they will not be participating at this time.

### **Programme Structure**

9. With such weight of support being demonstrated by the boroughs the initial exploratory project has quickly moved to being an implementation programme. Within the programme there are three projects:
  - i. **Establishing the company that will be the ACS Operator with all the underlying systems, processes and policies required of an organisation that will conduct business and employ staff**, which includes all the areas associated with setting up a new company from the ground up including (as examples) incorporating the company as a company limited by shares (London LGPS CIV Ltd. has been incorporated and each participating borough holds a £1 share), agreeing a licence to occupy with London Councils (it is proposed that the company will be accommodated within 59½ Southwark Street), and setting up finance, HR and IT systems and policies;
  - ii. **Establishing the company as a financial services organisation regulated by the Financial Conduct Authority (FCA)**, which includes defining the company’s operating model, writing policies and procedures, completing a significant amount of paperwork to support the authorisation application to the FCA, and procuring relationships with key partners such as the Asset Servicer (covering custodian, depository and fund administration);
  - iii. **Establishing the fund structure for launch**, which includes analysing the current pattern of investments across the boroughs, engaging with the

Investment Managers (IMs) to gather detailed data about assets under management, mandate types and fee structures, discussing with the IMs which mandates may be suitable to transition to the CIV, putting the proposed structure to each borough for consideration by their relevant committee and, later, agreeing a transition strategy for launch.

10. To support the delivery of this programme a Technical Sub-Group (TSG) was set up at the beginning of 2014. This is an officer group, constituted of the core programme team of two officers from London Councils and a number of LGPS experts from across the boroughs, under the leadership of the Director of Finance from LB Wandsworth. The input from these borough colleagues has been vital to the progress made so far.

### **Governance and structures**

11. The CIV is being developed for and on behalf of the London boroughs and the City of London, and each will participate on an entirely voluntary basis. As such, considerable attention is being given to ensuring that the proposed governance and operational structures of the CIV reflect the wishes and needs of the boroughs, both on day one and into the future.

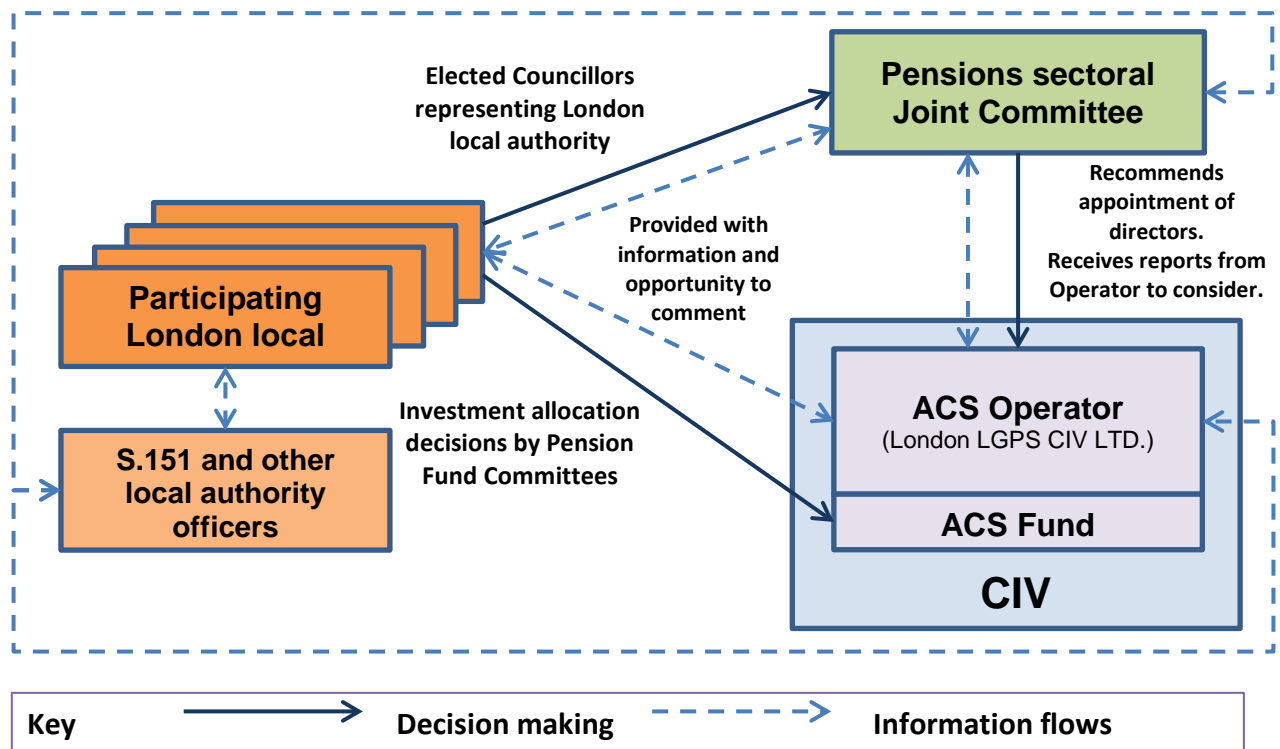
12. It is noteworthy that from advice to date the governance and structures described below are considered to give sufficient ownership and control for the participating boroughs such that there is no requirement for a borough to procure either the services of the Operator nor entry in the Fund (procurement professionals would recognise the arrangements are "Teckal compliant"). Some initial thought has been given to the possibility that the CIV might be open to investments from other LGPS funds (Administering Authorities from outside of London). This is something that members will be asked to decide upon at a later stage, but the question does have some bearing on the relationship between participating London LGPS funds and the CIV which could lead to the Teckal rules being breached, this is explored in more detail in the 'Relationship between the London boroughs, the CIV and other LGPS funds' section below.

13. Figure 1 below illustrates the overarching governance structure that is being established. A key element of that structure is the Pensions CIV Joint Committee. The committee will act as a representative body comprised of elected members from those local authorities that resolve to participate in the arrangements. At its March 2014 meeting, Leaders' Committee agreed, in principle, the Pensions CIV Joint Committee terms of reference, which are the subject of a separate report to today's meeting (see agenda item 5).

14. The CIV will be a Financial Conduct Authority (FCA) regulated UK domiciled Authorised Contractual Scheme (ACS). The ACS structure has been adopted because it brings with it significant international tax advantages and a high degree of data transparency. There are primarily two separate regulated elements to the structure, which are an ACS Operator and the ACS Fund.

15. The ACS Operator is a limited liability company (London LGPS CIV Ltd.), which is wholly owned by the 30 participating boroughs. At this stage it has interim directors, as proposed in the February report to Leaders' Committee, with final directors to be recruited and appointed ahead of the company being authorised and operational. The interim directors are Mayor Jules Pipe, Cllrs. Teresa O'Neill and Ruth Dombey, Mr Chris Buss (Treasurer, LB Wandsworth), Mr Ian Williams (Treasurer, LB Hackney), Mr Peter Kane (Chamberlain, City of London) and Mr John O'Brien (CEO, London Councils).

Figure 1



16. Detailed work is about to begin of define the company's operating model. Deloitte LLP have been selected through a procurement process to give expert advice to this work and to assist in taking the company through to authorisation and launch.

17. It is anticipated that, initially, the Operator will be based on a model that has as many roles and functions outsourced as possible – accepting that the FCA will have strong views in this area so total outsourcing is unlikely to be acceptable. As such it will have a



limited number of directly employed staff, with most functions being provided through outsourced partners. Over time, it is likely that a number of the outsourced functions could be brought in-house, but this will depend on establishing the necessary level of skills, knowledge and expertise, either through recruitment or training.

18. Procuring the outsourced partners is a complex and time consuming exercise and the Technical Sub-Group (TSG, set up to support the PWG) has begun the process of drawing up specifications and engaging with the market. It is hoped to have the first key partner, the Asset Servicer, in place by the end of 2014.
19. For expediency it was agreed that the London LGPS CIV Ltd. would adopt 'model' Articles of Association for its initial incorporation and that these would be revised to reflect the final governance structures and operating model as the detail became clearer. Over recent weeks Eversheds has been working on a draft 'Head of Terms' (HoT) document to inform the revision of the Articles and the drafting of a Shareholder Agreement. It is proposed that the draft HoT will be circulated to officers in participating boroughs for consideration and comment before bringing a final draft to the company's Board of Directors and this committee for formal agreement.

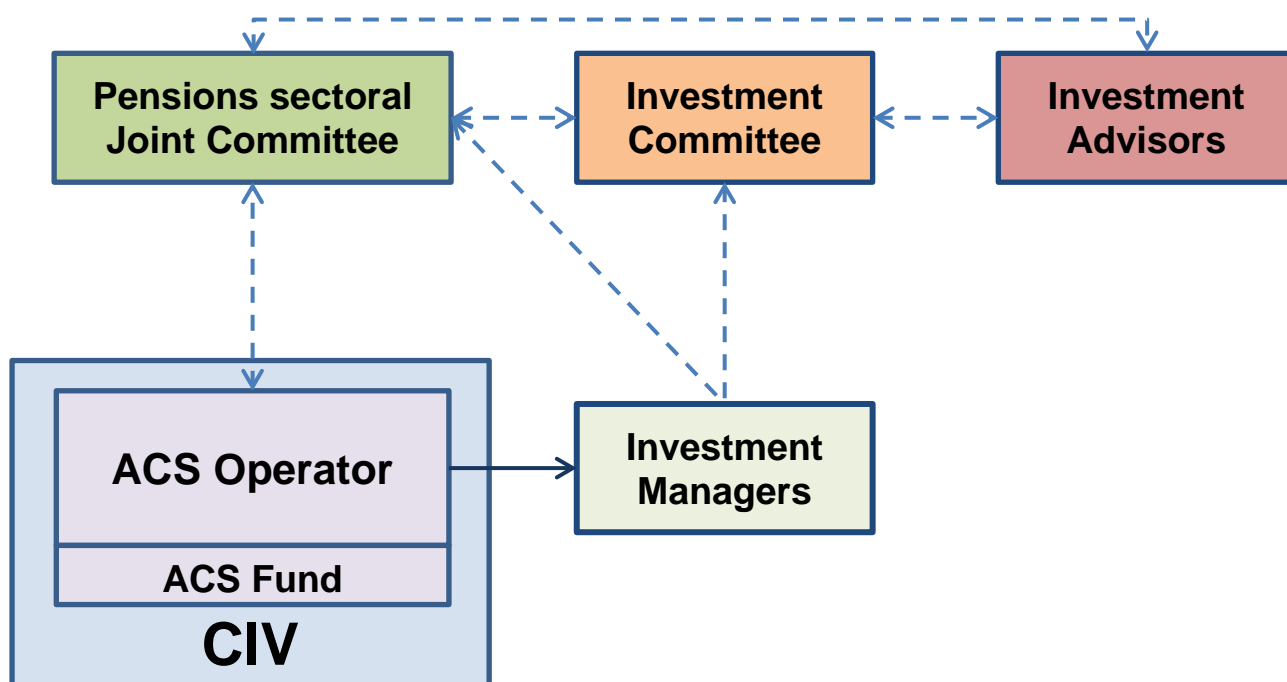
### **Structuring the ACS fund**

20. Final decisions about the initial fund structure will be taken later following consultation with the participating boroughs and the Investment Management industry. However, it is thought that a pragmatic starting point is to analyse which Investment Managers (IM) boroughs are currently invested through, to look for commonality (i.e. more than one borough invested with the same IM in a largely similar mandate), and to discuss with boroughs and IMs which mandates would be most appropriate to transition to the ACS fund for launch. Each mandate would become a separate, ring-fenced, sub-fund within the overall ACS fund. Boroughs will be able to move from one sub-fund to another relatively easily, but ring-fencing will prevent cross contamination between sub-funds.
21. The strategy being proposed for launch does, however, raise the question of whether the CIV can enter into contracts with IMs without the need for procurement (were procurement rules to apply there would be a significant risk that current borough-Investment Manager relationships may not be replicated on the ACS fund). Because of the critical nature of this issue to the overall strategy the advice of counsel has been sought.
22. Counsel's initial advice suggests that Regulation 6(2)(h) of the Public Contracts Regulations (as amended) can be relied upon to take these contracts outside of the EU

procurement regime. However, because this advice is so important to the CIV's proposed launch strategy it is intended to return to Counsel for clarification of a few points before circulating the final advice around the boroughs.

23. It is worth noting that, beyond the launch phase, the intention of the CIV company would be to normally carry out competitive procurements for the contracts which it concludes in the same way as currently seen across the boroughs.
24. Over time the fund will evolve and develop, with the potential for some mandates to be removed and others to be brought on. The Operator will not be regulated to give investment advice to the boroughs (at least not initially), and so thought is being given to the governance structures that might inform decision making of the boroughs and ensure that the boroughs' needs and wishes are reflected in the fund going forward.
25. Figure 2 illustrates current thinking in this area; it shows that an investment committee might be formed, with a number of LGPS experts drawn from across the boroughs, and potentially some independent experts. This committee would meet to consider how the ACS fund is performing and how it might be developed. Those considerations would be informed by input from a panel of procured investment consultants/advisors. Reports and recommendations would flow from the Investment Committee to the PCJC (similar to the way borough officers and investment advisors support borough pension committees). The PCJC would consider the recommendations made by the Investment Committee and feed its recommendations to the Operator. The Operator will act on the recommendations of the Joint Committee, subject to the necessary due diligence checks and so on that it will be required to carry out as the regulated body with responsibility for the good management of the ACS fund.

Figure 2



26. This is not an entirely settled structure and its final form will depend on the wishes of the boroughs, the final directors of the ACS Operator being content, and what is acceptable to the FCA from a regulatory perspective.

#### **Relationship between the London boroughs, the CIV and other LGPS funds**

27. A number of LGPS funds outside of London have shown an interest in what the boroughs are seeking to achieve. This has included both, looking at the governance and structures being proposed as a source of learning and information, as well as asking if the CIV will be open to investors beyond just the London boroughs.

28. On the point of the ACS fund being open to other investors, it is a requirement of the legislation underpinning an ACS fund that it must be open to all qualified investors (it will be what is known as a Qualified Investor Scheme (QIS)). Clearly the Operator will need to manage this as it is not the intention that it should take on, for instance, investors from the private sector. However, it could be that the boroughs might wish the CIV to accept investments from other LGPS funds, and this may well be attractive in terms of the benefits to be derived from additional scale.

29. Should the boroughs wish to have the ACS fund open to the wider LGPS in the future, there are some issues to be worked through to ensure that this can be achieved without undermining the ability of the boroughs to use the CIV without having to procure its products (investment opportunities) or the services of the Operator.

30. Because of the potentially critical nature of this issue it has been raised with Counsel as part of the advice noted above. In essence, Counsel has been asked to confirm that the boroughs' relationship with the company is exempt from procurement, and whether opening the CIV to investments from other LGPS funds would undermine that position and lead to the boroughs having to procure the services of the company.
31. In brief Counsel has confirmed that he is of the view that there are two possible arguments that might be used to argue that the relationship between the boroughs and the CIV is procurement exempt. These are either (1) the application of the Teckal Exemption (which can apply where a contracting authority (in this case a London borough or the City of London) contracts with a legally distinct entity (usually this will be a company that the authority has set up, either on its own or in concert with others), to provide services) or (2) that Regulation 6(2)(h) of the Public Contracts Regulations 2006 (as amended) provides an appropriate exemption to the application of the Regulations.
32. The Teckal exemption is based on a set of rules which includes that 80% of the company's turnover must derive from its 'parent' authorities. In the context of allowing other LGPS funds to invest in the CIV this presents a potential problem if significant investments, and therefore fees, were to be generated by investments from other parts of the LGPS (i.e. non-London authorities). It may still be possible to establish the company as a Teckal body but it will be less straightforward.
33. The second argument, is that "contracts" between the London boroughs (who are members of London LGPS CIV Ltd) and the CIV itself and any associated contracts with third party suppliers to which the boroughs may become signatories (e.g. Asset Servicer) do not need to be procured, as such arrangements are excluded from the application of the Regulations by virtue of Regulation 6(2)(h). The specific exemption provides that the Regulations do not apply to the seeking of offers for *"financial services in connection with the issue, purchase, sale, or transfer of securities or other financial instruments in particular transactions by the contracting authorities to raise money or capital."*
34. Counsel has confirmed that in his opinion this exclusion does apply and therefore the boroughs do not need to procure the services of the CIV. In effect this means that at the outset the boroughs can rely on either the Teckal exemption or Regulation 6(2)(h) to use the CIV without procurement.
35. Relying on Regulation 6(2)(h) counsel also advises that any LGPS fund can choose to invest through the CIV without the need for procurement even though they are not a

participating member of the CIV. If the reliance is placed on Regulation 6(2)(h) rather than Teckal the “80%” rule is no longer an issue.

36. As noted above, because this issue is so critical to the overall strategy for the CIV, the programme’s legal advisers have been asked to go back to Counsel with some points needing clarification. Once this clarification has been received a note will be circulated to the boroughs.

## **Budget**

37. Since the report to Leaders’ Committee in December 2013, and the subsequent report in February 2014, 30 boroughs have agreed to participate in the CIV and have each contributed £25,000 to a dedicated fund held by London Councils which was initially for the purposes of “...exploring the proposal...”. As noted above the initial exploratory project has swiftly moved to being an implementation programme. The February report provided an estimated budget, based on what was known at the time, that proposed an implementation cost in the region of £1.5 million.

38. Attached at Annex A is an updated budget showing expenditure committed to date and anticipated expenditure through to launch. From Annex A it can be seen that the total estimated expenditure to launch is now £1,713,831.

39. At its inaugural meeting of 14 October 2014 the board of London LGPS CIV Ltd. were presented with this budget overview and were recommended to write to the Treasurer of each participating borough proposing that each borough make an additional contribution of £25,000 now and a further contribution of the same amount at the beginning of the next financial year.

40. The board agreed to the recommendation and letters have now been sent, and invoices will be raised shortly for the first amount, although it should be noted that one borough has indicated that an invoice should not be sent until after this meeting and subject to a final decision by members of the borough’s pension committee.

41. The committee will wish to note that there will be an anticipated underspend at launch of £516,169 which will contribute towards the first year’s operating expenses as the CIV becomes established and the ‘business as usual’ (BAU) budget and fee structure comes into play.

42. A BAU budget is being worked on by the TSG, but this is heavily reliant on the final definition of the company’s operating model and as such it will be brought to the committee at a later meeting.

## **Timeline**

43. The TSG has been working hard during 2014 to make swift progress, a significant amount has been achieved, but there is a lot of ground still to cover. As things stand it looks likely that the CIV will launch in the summer of 2015, but key to this will be defining the company's operating model and taking this to the FCA for authorisation – the FCA can take up to six months to consider an application for authorisation, although it is hoped that they might be able to process this application more swiftly.

## **Government Consultation**

44. Government Ministers have shown significant interest in the LGPS over the last two years and have been particularly keen to consider options for reform that might deliver cost savings and efficiencies.

45. On 2 May 2014 the Government released a consultation titled Local Government Pensions Scheme: Opportunities for collaboration, cost savings and efficiencies, which drew on an earlier call for evidence on the future structure of the LGPS, which ran through the summer of 2013, and supplementary cost-benefit analysis of proposals for reform that the Government commissioned from Hymans Robertson LLP.

46. The package of proposals set out in consultation included:

- Establishing common investment vehicles to provide funds with a mechanism to access economies of scale, helping them to invest more efficiently in listed and alternative assets and to reduce investment costs;
- Significantly reducing investment fees and other costs of investment by using passive management for listed assets, since the aggregate fund performance has been shown to replicate the market;
- Keeping asset allocation with the local fund authorities, and making available more transparent and comparable data to help identify the true cost of investment and drive further efficiencies in the Scheme;
- A proposal not to pursue fund mergers at this time.

47. The Government posed five questions in the consultation, which were:

Q1. Do you agree that common investment vehicles would allow funds to achieve economies of scale and deliver savings for listed and alternative investments? Please explain and evidence your view.

Q2. Do you agree with the proposal to keep decisions about asset allocation with the local fund authorities?

Q3. How many common investment vehicles should be established and which asset classes do you think should be separately represented in each of the listed asset and alternative asset common investment vehicles?

Q4. What type of common investment vehicle do you believe would offer the most beneficial structure? What governance arrangements should be established?

Q5. In light of the evidence on the relative costs and benefits of active and passive management, including Hymans Robertson's evidence on aggregate performance, which of the options set out above offers best value for taxpayers, Scheme members and employers?

48. The consultation closed on 11 July 2014, and by agreement of Leaders' Committee London Councils submitted a response on behalf of its members which in summary said:

- London Councils endorses the Government's decision not to pursue fund mergers at this time.
- London Councils believes that Collective Investment Vehicles (CIVs) can offer significant savings and the opportunity for improved investment returns through economies of scale and access to alternative investments.
- London Councils strongly endorses the proposal to keep asset allocation decisions with the local fund authorities.
- London Councils has no firm view on the number of CIVs that should be set up, but does believe that a single CIV for the entire LGPS would generate dis-economies of scale and potential disruption to the investment market.
- London Councils believes that an FCA regulated ACS is the most suitable form of CIV for the London boroughs, and proposes a governance structure that allows the boroughs strong oversight and control within the regulatory framework.
- London Councils believes that passive management should not be enforced at any level and that individual fund authorities should have the ability to use active management as part of their investment strategies. London Councils also believes that the London CIV could enhance governance and could act as a catalyst to deliver the benefits of active management for individual pension funds.

49. London Councils' officers have continued to engage closely with their counterparts in Government and, while ultimate decisions are still to be made by Ministers, there has been no indication that the Government thinks the boroughs should stop their plans to establish a CIV. Indeed, the fact that the Government's consultation clearly shows that Ministers have developed their thinking away from LGPS fund mergers (although not to the point of abandoning the potential for mergers altogether), towards encouraging the development of CIVs, and that the Local Government Minister has met with Mayor Jules Pipe and Cllr Teresa O'Neill since the consultation, could both be taken as positive signs of encouragement.

### **Conclusion**

50. Significant progress has been made towards establishing a CIV for those London boroughs that wish to participate in the arrangements. This report has provided an update on the key aspects of that progress to date. There is still significant ground to be covered across the three projects underpinning the programme, further reports will come to future meetings of the committee to ensure that members are kept fully informed and have regular opportunities to comment on and steer implementation over the coming months.

### **Recommendations**

51. The committee is recommended to consider and note the contents of this report.

### **Legal implications**

52. These are captured in the body of the report.

### **Financial implications**

53. This report outlines progress on a range of issues, primarily financial and governance processes, required to successfully establish the London LGPS CIV. These will continue to be developed as the requirements of the company become clearer and the operating model is firmed up. Annex A details the current budget plan in respect of preparatory costs and highlights the contributions from participating boroughs to cover all anticipated commitments up until launch.

### **Equalities implications**

54. There are no equalities implications for London Councils

### **Attachments**

Annex A      Budget Overview



## **Background papers**

13 March 2012, Leaders' Committee report:

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=4796](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=4796)

13 November 2012, Leaders' Committee report:

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5072](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5072)

11 December 2012, Leaders' Committee report:

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5109](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5109)

14 May 2013, Leaders' Committee report:

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5252](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5252)

19 September 2013, Executive report:

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5353](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5353)

26 November 2013, Executive report:

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5490](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5490)

10 December 2013, Leaders' Committee report

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5495](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5495)

11 February 2014, Leaders' Committee report

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5562](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5562)

11 March 2014, Leaders' Committee report

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5598](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5598)

15 July 2014, Leaders' Committee Report

[http://www.londoncouncils.gov.uk/committees/agenda.htm?pk\\_agenda\\_items=5668](http://www.londoncouncils.gov.uk/committees/agenda.htm?pk_agenda_items=5668)

<b>Budget Overview</b>			
		£	£
<b>Expenditure committed to date</b>			
Deloitte - initial consultancy		-£150,000	
Eversheds		-£170,000	
Northern Trust		-£22,080	
Eversheds - procurement advice (inc. Counsel)		-£15,890	
Project Manager (to May 2015)		-£70,000	
Mercer		-£49,950	
Office equipment		-£911	
			-£478,831
<b>Income to date</b>			
Borough contributions (30 boros x £25k)		£750,000	£750,000
	<b>Balance</b>		£271,169
<b>Estimated expenditure to Mar 2015</b>			
Tax advice consultancy		-£144,000	
ACS set up costs		-£320,000	
Legal costs		-£160,000	
Transition consultant		-£20,000	
Recruitment and employment costs of CEO / CIO / COO and non-exec board members		-£190,000	
			-£834,000
<b>Additional income from boroughs now</b>		£750,000	
(30 boros x £25k)			£750,000
	<b>Balance</b>		£187,169
<b>Estimated expenditure Apr 2015 - launch</b>			
Tax advice through to launch		-£36,000	
ACS set up		-£100,000	
Legal costs		-£40,000	
Transition consultant		-£80,000	
Anticipated employment costs of CEO / CIO / COO and non-exec board members to launch		-£165,000	
			-£421,000
<b>Additional income from boroughs Apr 2016</b>		£750,000	
(30 boros x £25k)			£750,000
	<b>Balance</b>		£516,169
<b>Total estimated expenditure to launch</b>			-£1,733,831

## Pensions CIV Sectoral Joint Committee

### Fund Manager Analysis Update

Item no: 7

**Report by:** Hugh Grover      **Job title:** Programme Director, London LGPS CIV

**Date:** 17 December 2014

**Contact Officer:** Frederick Fuller

**Telephone:** 020 7934 9844      **Email:** [frederick.fuller@londoncouncils.gov.uk](mailto:frederick.fuller@londoncouncils.gov.uk)

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#### **Summary**

This report provides the committee with an update on progress made by the Technical Sub-Group in analysing borough investments with Investment Managers and the consideration they have given to a proposed strategy for structuring the CIV fund for launch.

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**Recommendations** The committee is recommended to:

- i. Note and provide any guidance on the content of this report, especially on the subject of infrastructure investment.
-



# Fund Manager Analysis Update

## Background

1. Earlier in the summer the Technical Sub-Group ((TSG) the officer group made up of pensions experts from across the boroughs supporting the CIV programme) approached all the participating London boroughs and asked for each to provide data covering their investment profile (which Investment Managers (IM), scale of assets invested, and the type of investment mandate). From analysis of this data it was possible for the TSG to get a picture of which mandate types were held by each borough and with which IMs.
2. Having considered the data the TSG were of the view that adopting a strategy based on bringing 'common' mandates (i.e. mandates with two or more boroughs invested in them) onto the fund for launch could be a pragmatic approach, which could deliver scale efficiencies and opportunities for most boroughs without the need for boroughs to change from one IM to another. Data suggested that 28 boroughs would have the potential for between £5bn and £9bn of assets to transition. The majority of these assets would be listed equities and fixed income, with the 'alternative' investments (such as private equity and property) being viewed as 'phase two' (i.e. after launch).
3. Based on that strategy it was initially recognised that focussing on the top nine Investment Managers by quantum of assets under management, and adding a tenth smaller manager could deliver a viable outcome to launch the fund – subject to borough decisions about investment in the CIV that would follow later.
4. This report provides the committee with an update about work that has progressed over the summer.

## Progress

5. Since the analysis over the summer based on borough data, every participating borough has given London Councils written permission to engage with the IMs to both request detailed data and to meet with them to discuss what opportunities, based on the TSG's proposed strategy, might be available for the fund for launch. This data has brought the total number of IMs being engaged with to fourteen. These managers collectively manage over £14.5 billion of Borough assets, which accounts for over half of the total assets under management across all the borough pension funds.
6. Initial discussions with the IMs focussed upon listed equities and fixed income. However, managers have been quick to point out that there are other areas that may also prove easier than anticipated to bring onto the CIV at launch, such as some of the multi-asset

funds (many of these referred to as Diversified Growth Funds) and a number of the more straightforward property mandates.

7. Subsequent analysis suggests that of the £14.5 billion of assets, £8.4 - £9.9 billion could potentially be brought onto the CIV for launch through eleven separate managers. Whether or not the full amount will be brought on for day one is subject to further analysis, cost considerations, discussions with the Asset Servicer when procured, and possibly some pragmatism about what can be realistically achieved.
8. Although fee reductions only make up a small part of the CIV's overall benefit to the boroughs, they are arguably the most immediate and tangible benefit. For this reason managers have been asked to provide initial un-negotiated estimates of potential fee savings.
9. Between the eleven managers with mandates that might be collectivised for launch, nine have provided estimates of fee savings, totalling £2.8 million per annum, with an average reduction of 20% per manager. It should be noted that these fees are un-negotiated and therefore will be subject to change. These savings vary considerably from manager to manager and are inevitably not spread evenly across the boroughs (some will gain more in savings than others).
10. There are a number of reasons for this spread of savings across the boroughs. Broadly, based on the strategy being proposed, some boroughs:
  - Have greater commonality in their choice of mandates and managers than others and therefore could have significantly greater amounts of assets moving to the CIV at the point of launch;
  - Have an investment strategy that is focussed primarily on passive investment where generally potential fee savings are lower as fees are already low. However, as some of these passive mandates have large amounts of borough assets in aggregate, and the fees are generally based on ad valorem scales, the process of collectivisation leads to some boroughs saving substantial amounts of money through more assets accruing fees at a lower point in the scale;
  - Might have the opportunity to collectivise their active mandates and as the fees for these investments are generally significantly higher than for passive mandates the potential for substantial fee reductions is much greater.

11. Conversations will continue with a small number of managers who have yet to meet for discussions with London Councils.

### **Next Steps and Strategy**

12. The strategy of the TSG thus far has been to concentrate on those managers which currently have mandates shared by two or more boroughs.

13. Of those managers with common mandates, the TSG has focussed upon those that cover both quantum of assets and as many of the boroughs that are participating in the CIV as possible. This strategy has the benefit of narrowing down the number of managers efficiently and also quickly obtains the critical mass needed for the CIV in terms of quantum of assets.

14. Based on the current strategy and analysis so far, this approach leaves one of the participating boroughs with no common mandates currently in line to come onto the CIV for launch because of their current pattern of asset allocation. However, boroughs will continue to review their current asset allocation decisions and it may be that this position will change before launch.

15. In addition, it may be that when the fund structure is finally defined and shown to the boroughs some might decide to move a current mandate to an alternative on the CIV to gain advantage from the lower fees that can follow.

16. Further analysis is due to take place on the remaining borough assets, and savings calculated accordingly. More formal negotiations with fund managers are likely to start in the New Year, with members of the TSG performing this function. It has been suggested to London Councils that this and the process of drawing up agreements with IMs, could both take some time, hence the need to progress quickly with the decision of how the fund is likely to be made up and the more formal negotiations with those managers involved.

17. Once these more formal negotiations have happened it will be possible to provide each participating borough with an outline of what mandates might be brought onto the fund for launch and what level of saving would accrue.

18. Further reports will come to the committee as this work progresses, including a more detailed strategy for engaging with the boroughs and particularly the process for requesting borough investment decisions from their Pensions Committees.

### **Infrastructure investments**

19. The strategy proposed by the TSG would not encompass infrastructure at this time (primarily because there is no commonality in this asset class across the boroughs), however the officers of the TSG are very conscious that members will be interested in the opportunities that the CIV might present in this area.

20. The committee is invited to discuss their views on infrastructure investment to provide guidance to the TSG so that further work can be done on this asset class with a view to a report coming to a future meeting.

### **Recommendations**

21. The board is recommended to:

- i. Note and provide any guidance on the content of this report, especially on the subject of infrastructure investment.

### **Financial implications**

22. There are no financial implications for London Councils.

### **Legal implications**

23. There are no legal implications for London Councils.

### **Equalities implications**

24. There are no equalities implications for London Councils.



## Pensions CIV Sectoral Joint Committee

### Asset Servicer Procurement Update

Item no: 8

**Report by:** Hugh Grover      **Job title:** Programme Director, London LGPS CIV

**Date:** 17 December 2014

**Contact Officer:** Frederick Fuller

**Telephone:** 020 7934 9844      **Email:** [frederick.fuller@londoncouncils.gov.uk](mailto:frederick.fuller@londoncouncils.gov.uk)

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#### Summary

This report provides the committee with background and a progress update relating to the procurement of the Asset Servicer (a key provider to the CIV). It notes that the procurement is underway through an OJEU process using the competitive dialogue route and that six potential providers responded to a PQQ, and following evaluation that led to three being shortlisted.

The tender is now at the ITT stage, with responses received from the three bidders on 28<sup>th</sup> November.

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**Recommendations** The committee is recommended to:

- i. Note the content of this report and the on-going progress of the procurement
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# Asset Servicer Procurement Update

## Background

1. A key provider to the CIV will be an Asset Servicer (covering fund administration, depository and custodian roles). Putting this provider in place is key to finally defining the CIV's operating model and will be of great importance to the Financial Conduct Authority when they are asked to give consideration to authorising the arrangements being put in place to run the CIV overall.
2. As the contract with the Asset Servicer will be of high value and is likely to span several years (possibly up to five) the procurement is going through an OJEU process using the competitive dialogue route.
3. A Pre-Qualifying Questionnaire (PQQ) was published in the summer inviting interested parties to respond. Six potential providers submitted PQQ responses, which, following a scoring process, led to a shortlist of three candidates being invited to enter into the competitive dialogue stage and respond to a detailed Invitation to Tender (ITT).
4. As this contract is so important to the successful delivery and operation of the CIV, London Councils contracted with Mercer Sentinel (recognised experts in the contracting of such services) to inform the procurement process.
5. This procurement process is being facilitated by London Councils, on behalf of the CIV Operating Company, and is being supported by the Technical Sub-Group (TSG). The contract with the Asset Servicer will be between London LGPS CIV Ltd. (the CIV's Operating Company) and the selected provider, as such the decision to appoint rests with the company's interim directors.

## Discussion

6. A detailed ITT was drawn up over a number of weeks by both Mercer and members of the TSG and was issued on Friday 7 November to the three shortlisted candidates. The three unsuccessful candidates have now been informed in writing of their position by Mercer.
7. The ITT closed on Friday 28 November.
8. All three bids are being assessed against the scoring criteria published in the ITT, which focuses in part upon three scenarios for the CIV fund through which the candidates have drawn up pricing models.

## **Next Steps**

9. On 10 December, a number of representatives from Mercer, the boroughs and London Councils will be attending clarification meetings with the three shortlisted candidates. The meetings will provide an opportunity to pose any questions that have arisen from their ITT responses, as well as give the candidates a final opportunity to clarify their position and support their ITT response. Following those meetings the responses will be given their final scoring.
10. Based on the final scores a report will be drafted for the Board of Directors of London LGPS CIV Ltd. to consider and make a final decision about which candidate should be awarded the contract. This decision will be published as a 'contract award notice' on the Internet (and relayed directly to each candidate) on Friday 19 December. The award notice will be followed by a mandatory standstill period of 10 calendar days, which will expire during the Christmas holiday break, thus leading to a final contract award in the New Year.
11. A report will come to the next meeting of the committee informing members of the outcome of this process.
12. The committee will wish to note that this is the first of a number of procurements that will be run over the coming months to put the necessary suppliers to the CIV in place, including an audit company, tax consultants and a compliance consultant. All procurements will be run following best-practice procurement methodologies.

## **Recommendations**

13. The committee is recommended to:
  - i) Note the content of this report and the on-going progress of the procurement.

## **Financial implications**

14. There are no financial implications for London Councils.

## **Legal implications**

15. There are no legal implications for London Councils.

## **Equalities implications**

16. There are no equalities implications for London Councils.

# Pensions CIV Sectoral Joint Committee

## Dates of Future Meetings

Item no: 9

**Report by:** Alan Edwards      **Job title:** Governance Manager

**Date:** 17 December 2014

**Contact Officer:**

**Telephone:** 020 7934 9911      **Email:** Alan.e@londoncouncils.gov.uk

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**Summary**      This report notifies members of the proposed Pensions CIV Sectoral Joint Committee meeting dates for 2015.

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**Recommendations**      The committee is recommended to:

- i.      Note and agree the proposed dates for the Pensions CIV Sectoral Joint Committee for 2015.

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## **Dates of Future Meetings**

### **Pensions CIV Sectoral Joint Committee: Proposed Dates**

- Wednesday 25 February 2015
- Wednesday 25 March 2015
- Wednesday 27 May 2015
- Wednesday 29 July 2015 (AGM)
- Wednesday 23 September 2015
- Wednesday 4 November 2015

1. All the above meetings start at 10.30am (with 10:00am political pre-meets if required) and will be held at 59½ Southwark Street, London, SE1 0AL.

### **Recommendations**

2. The committee is recommended to:
  - i. Note and agree the proposed dates for the Pensions CIV Sectoral Joint Committee for 2015.

### **Legal implications**

3. There are no legal implications for London Councils

### **Financial implications**

4. There are no financial implications for London Councils

### **Equalities implications**

5. There are no equalities implications for London Councils