Complete Agenda

Democratic Services
Swyddfa'r Cygnor
CAERNARFON
Gwynedd
LL55 1SH

Meeting

PENSIONS COMMITTEE

Date and Time

TUESDAY, 8TH SEPTEMBER, 2015

FOLLOW ON FROM THE ANNUAL MEETING

Location

Ystafell Gwyrfai, Council Offices,

Caernarfon, Gwynedd. LL55 1SH

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(DISTRIBUTED Tuesday 2 September 2015)

PENSIONS COMMITTEE

MEMBERSHIP (7)

Plaid Cymru (3)

Councillors

Peredur Jenkins **W. Tudor Owen** **Gethin Glyn Williams**

Independent (2)

Councillors

Trevor Edwards **John Pughe Roberts**

Labour (1)

Councillor Glyn Thomas

Liberal Democrats (1)

Councillor Stephen W. Churchman

Co-opted Members

Councillor Margaret Lyon, Conwy County Borough Council Representative

Councillor Hywel E. Jones, Isle of Anglesey County Council Representative

Aelodau Ex-officio / Ex-officio Members

Chairman and Vice-Chairman of the Council

A G E N D A

PENSIONS COMMITTEE, 16.06.15

Present: Councillors: Stephen Churchman, Trevor Edwards, Peredur Jenkins, Hywel E Jones (Isle of Anglesey County Council), W Tudor Owen and John P. Roberts.

Officers: Dafydd Edwards (Head of Finance Department), Caroline Roberts (Investment Manager), Gareth Jones (Pensions Manager) and Lowri Haf Evans (Member Support and Scrutiny Officer).

1. ELECTION OF CHAIRMAN FOR 2015/2016

Resolved to re-elect Councillor Tudor Owen as Chairman of the committee for 2015/16.

2. ELECTION OF VICE-CHAIRMAN FOR 2015/2016

Resolved to elect Councillor Stephen Churchman as Vice chairman of the committee for 2015/16.

3. APOLOGIES

Apologies were received from Councillors Margaret Lyon (Conwy County Borough Council Representative) and Peter Read.

4. DECLARATION OF PERSONAL INTEREST

No declarations of personal interest were received from any members present.

5. URGENT ITEMS

Update on establishing Gwynedd Council Pension Board.

(a) Following the interview process, it was reported that six members had been appointed for the Pension Board: Anthony William Deakin (Cartrefi Conwy), Victoria Louise Hallaron (Cartrefi Cymunedol Gwynedd), Osian Richards (Gwynedd Council), Huw Trainor (North Wales Police), Sharon Warnes (retired - formerly Gwynedd Council) and the nomination of one elected member of Gwynedd Council would be confirmed soon. The inaugural meeting of the Pension Board would be held on 13 July, 2015. It would be the responsibility of the Pension Board to assist the administrative authority to ensure compliance with all relevant regulations, other legislation and requirements which were relevant to the scheme. The Board would also assist the authority to ensure effective and efficient governance and administration of the fund.

(c) In response to a question, it was noted that members of the Pension Board would include three representatives of the employers and three representatives of members of the scheme.

6. MINUTES

The Chairman signed the minutes of the previous meeting of this committee, held on 24 March 2015, as a true record.

7. MEETINGS OF THE INVESTMENT PANEL

(a) Submitted – the report of the Head of Finance Department proposing a change in the arrangements of meetings of the Investment Panel. Since February 2014, it was noted that the meetings of February and May were held in London and the meetings of July and November were held in Caernarfon. Based on the trial period, it was highlighted that holding the meetings of February and May in London was ill-timed for the officers because of pressure of work during this time with the Financial Strategy / Budget in February and closure of the Council accounts and Pension Fund in May. It was suggested that it would make more sense to arrange the meetings of February and May in Caernarfon and the meetings of July and November in London.

(b) The recommendation to accept the report was proposed and seconded.

(c) In response to an observation, it was noted that it was intended to commence the new arrangement in November 2015 and to continue with the annual cycle until it was reported differently.

RESOLVED TO ACCEPT THE REPORT OF THE HEAD OF FINANCE DEPARTMENT

8. RECONCILING MEMBERS' GUARANTEED MINIMUM PENSIONS (GMP)

(a) Submitted – the report of the Pensions Manager, providing information and seeking support to fund additional specialist software to assist with the new work processes. The background to the request was elaborated upon and it was noted that there would be changes to the administrative arrangements and responsibility for Guaranteed Minimum Pensions. It was noted that a substantial number of members of the Gwynedd Pension Fund continued to be the subject of GMP assessments for annual pension increases or as part of transfer calculations. These assessments would have to be implemented and this minimum reconciled before March 2018.

(b) Her Majesty's Revenue and Customs was responsible for calculating and informing schemes of GMP levels but it was proposed to transfer the responsibility to schemes by March 2018. Prior to the transfer, the GMP would have to be reconciled to ensure that all the GMP they had corresponded to the HMRC records. It was noted that national surveys showed that the levels of errors/inconsistencies were high, which meant a large amount of complicated additional work for high-level staff to implement. The costs were estimated at £300k (staff and resources). There would be a need for a team of staff to commence the work during the spring of 2016.

(c) Members were asked to,

- note the process of reconciling the GMP, the likely cost and its effect on the resources of the pensions unit.
- agree retrospectively to fund the additional software at a cost of approximately £8,300 per whole or part year.
- note that update reports would be submitted to the Committee on the ongoing work from time to time and that may include a request for funding

temporary staff and a request for decisions on error tolerances and write off levels.

(ch) It was proposed to approve in accordance with the recommendation and this was seconded.

RESOLVED TO ACCEPT THE REPORT AND THE RECOMMENDATIONS LISTED BY THE PENSIONS MANAGER

The meeting commenced at 2pm and concluded at 2.30pm

MEETING	**PENSIONS COMMITTEE**
DATE	**8 SEPTEMBER 2015**
PURPOSE	**UPDATE THE COMMITTEE ON THE WELSH PENSIONS COLLABORATION PROJECT**
TITLE	**WELSH LOCAL GOVERNMENT PENSION FUNDS - WORKING TOGETHER**
AUTHOR	**CAROLINE ROBERTS, INVESTMENT MANAGER**

1. INTRODUCTION

1.1 The Committee is aware of the project undertaken by the Pensions Subgroup of the Society of Welsh Treasurers and approved a contribution to the cost of the Business Case for a common investment approach in October 2014. The report was produced by Mercer and has been considered by the Welsh Treasurers. It was agreed that a summary report would be provided by Mercer for consideration by those responsible for governance in each of the eight pension funds.

1.2 The Summer Budget in July presented by the Chancellor of the Exchequer included reference to the Local Government Pension Scheme as follows:

Local Government Pension Scheme pooled investments
The government will work with Local Government Pension Schemes administering authorities to ensure that they pool investments to significantly reduce costs, while maintaining overall investment performance. The government will invite local authorities to come forward with their own proposals to meet common criteria for delivering savings. A consultation to be published later this year will set out those detailed criteria as well as backstop legislation which will ensure that those administering authorities that do not come forward with sufficiently ambitious plans are required to pool.

1.3 The work already undertaken by the Welsh funds has demonstrated that common investment is the way forward and further development of this collaboration will demonstrate commitment to pooling of investments.

2. ALL WALES COLLABORATION REPORT

2.1 A copy of the summary report from Mercer is attached to this report as **Appendix A**. The report recommends that the Welsh Funds:

- Spend time to develop a share set of principles for collaboration.
- Pursue a more collaborative approach in order to avail the key benefits which include economies of scale and lower costs, increased consistencies, enhanced governance and operational management across the Welsh Funds.
- Select a single passive provider for passive assets to obtain immediate cost savings. A pooling structure would not be required to achieve these gains.
- Establish a pooling framework to extend on collaboration beyond passive assets.
- Adopt a regulated (pooling) vehicle along with a model that supports leveraging the infrastructure of a third party provider (rather than building such infrastructure internally).
- Consider framing the new collaborative framework as optional for each Welsh Fund but target mandates that are common to all to ensure strong uptake and an engaged and simple approach.
- Consider active equity as the immediate mandate to commence under the new collaborative framework. The analysis conducted highlights that mandates offer the greatest potential for cost savings and improved net of fees returns.
- Agree a set of next steps to take forward the project, including a workshop / training session and development of a project plan, including the potential tender process to assess suitable partners / providers to support the new collaborative framework.

3. CURRENT POSITION

3.1 Each of the Welsh Pension Funds will present the attached report to their Pensions Committee or equivalent in September 2015.

3.2 At the request of the Pensions Subgroup, the Welsh Collaboration Investment Group held a meeting in July 2015 to establish the way forward to select a single passive manager as this can be achieved without a pooling structure. This would be a joint procurement exercise to deliver fee savings by jointly appointing the same manager. A briefing report from this meeting is attached to this report as **Appendix B**.

3.3 As noted above the next step is to establish a pooling framework for the Welsh Funds with the aim of reducing fees and to concentrate on equity investments first. The recommended option is to use ‘rent’ a structure from a third party rather than creating a bespoke structure just for Wales as it would be more flexible and cost effective. An independent advisor will be procured to assist with the procurement process.

4. RECOMMENDATION

4.1 In order to retain control of our own agenda as eight Welsh Pension Funds, each Pensions Committee is asked to support further work as detailed in the appendices, specifically to:

- Investigate opportunities for reduced fees for passive investments.
- Jointly assess the detailed business case for pooling frameworks for other investments.

MERCER
MAKE TOMORROW, TODAY

ALL WALES COLLABORATION

JULY 2015

MARSH & McLENNAN COMPANIES

CONTENTS

Executive Summary

This paper provides an overview of the work completed to support the eight Welsh LGPS Funds ("the Welsh Funds") in their considerations in establishing a collaborative governance and investment framework. The paper recommends that the Welsh Funds:

- **Spend time to develop a shared set of principles for collaboration.**
- **Pursue a more collaborative approach in order to avail the key benefits which include economies of scale and lower costs, increased consistencies, enhanced governance and operational management across the Welsh Funds.**
- **Select a single passive provider for passive assets to obtain immediate cost savings. A pooling structure would not be required to achieve these gains.**
- **Establish a pooling framework to extend on collaboration beyond passive assets.**
- **Adopt a regulated (pooling) vehicle along with a model that supports leveraging the infrastructure of a third party provider (rather than building such infrastructure internally).**
- **Consider framing the new collaborative framework as optional for each Welsh Fund but target mandates that are common to all to ensure strong uptake and an engaged and simple approach.**
- **Consider active equity as the immediate mandate to commence under the new collaborative framework. The analysis conducted highlights that these mandates offer the greatest potential for cost savings and improved net of fees returns.**

Agree a set of next steps to take forward the project, including a workshop / training session and development of a project plan, including the potential tender process to assess suitable partners/providers to support the new collaborative framework.

Background

We begin at the point at which the eight LGPS Funds in Wales have decided there is merit in exploring whether investing their assets together is (tangibly) worthwhile.

There are a range of options for investing collectively and for each option we have considered;

- The costs of set up
- The financial benefits
- Implementation issues
- The governance implications
- The legal implications

We have made recommendations in terms of the options we feel should be taken forward and as such have provided details of next steps for implementation.

Proven Benefits?

At the outset of the project, Officers of the eight Funds were clear that a discussion was needed on the benefits of collaborative investing and the extent to which these were proven; the rationale being that this may help form the guiding principles or aims of any collaboration project.

In order for collaboration to be "proven", we arguably need to obtain improved investment returns after fees.

Reductions in fees are of course tangible, but arriving at improved investment returns can be a result of a number of inter-related factors, and so the singular impact of collaboration may be difficult to definitively prove.

Nonetheless, there are a range of factors, be they direct or indirect, that collaboration will bring to the table, which we believe will have a measurable benefit;

- Increased scale would **reduce costs** but also allow for more **diversified, but focused** portfolios

Care would need to be taken not to "over-diversify"; however, a weight of collective assets would allow for more focused or specialised portfolios, perhaps covering opportunities that would not be possible on an individual Fund basis. We also believe there is a real opportunity to take a long term approach in illiquid, alternative assets that may not exist at an individual Fund level presently. A carefully considered collective vehicle, tailored for the needs of the LGPS, would have distinct merits — managed by the LGPS for the LGPS.

There needs to be an awareness of **diseconomies of scale** however (for example, smaller boutique managers may not be able to facilitate large pools of assets).

- Improvements in governance

By delegating manager decisions to a joint Welsh body, individual Funds will have more time to spend on strategic issues such as funding and investment strategy. Structured correctly, a joint body operating outside the usual Committee cycle will increase the speed of decision making and

be able to be more "market aware". There is of course also the point that "eight heads may be better than one" in terms of diversity of ideas.

- **Increasing operational efficiencies**

Currently eight Funds are independently diverting internal resources and paying fees to external providers. Where there is commonality in services required, whether it be investment related (e.g. a manager selection requirement for a particular asset class) or operational (e.g. use of a custodian), collaboration can drive operational efficiencies of a significant magnitude.

3

Governance

Governance is Key

Key to any potential collaborative project is whether each individual Fund is on board and willing to commit to a **shared set of principles.** With this in place, a sensible governance structure will be easier to achieve.

It is worth noting that we are not recommending any degree of compulsion for any individual Welsh Fund to invest in a collaborative Welsh entity; although clearly the direction of travel post Budget is that meaningful steps are likely to be required by all Funds in England and Wales. However, each Fund (and its associated Committees), if deciding to use the structure, will need to be on board with the concept of delegation to a collective entity of some description with respect to manager selection, monitoring and implementation. With this in mind, we would suggest that it is crucial that a joint vision or set of principles is established at outset that local Committees can buy into and reference at future points.

We would strongly recommend that after consideration of this report, the eight Funds prioritise the establishment of a shared set of principles. Issues to resolve will include:

- What is the primary aim of collaboration?
    - Cost savings
    - Pursuit of excellence — governance and investments
    - Implementation of a long term investment philosophy
- How will success be measured?
- Will decisions require a majority or full consent?
- Will all Funds approach engagement with Committees collectively or individually (at outset and on an ongoing basis)?
- How will operational issues such as procurement be dealt with?
- How often and where will the group meet, and with the difficulties presented by geography and travel, will sub groups for potentially separate work streams be established?
- What asset classes / mandates to include in the initial collaboration framework?

Good governance is crucial

There is academic research that suggests the existence of a good governance premium; ranging from 0.05% p.a. (Clarke, 2007) to 1-3% p.a. (Ambachtsheer 2007, Watson Wyatt 2006)

"Pension Fund Governance can make a positive difference to financial performance, cost efficiency, and the trust of stakeholders in the institution" (Clark, 2007)

There are several reasons as to the relevance of a governance premium in this case. In the first instance, by delegating investment manager issues to a collective entity, the more important considerations of funding and investment policies can be given more time by Committees (locally) at each Welsh Fund. Second, the governance structure of the collective entity itself is of utmost importance in the role it plays in efficient decision making and implementation.

Any collective entity will have an Investment Committee of some description that will need a Terms of Reference to determine its precise make up and roles / responsibilities and this will become more tangible once a collective model is established. In the meantime, we would make the following initial suggestions:

- All Funds participating will require representation, but on the grounds that it is our opinion (and experience) that smaller groups tend to operate more efficiently, we would recommend that each Fund has just one representative;

- Depending on the structure chosen, it may be that an independent chair and a secretary are considered. Otherwise, it may be worth considering having a rotating chair with perhaps each Fund's representative serving as chair for six months;

- To maximise the professionalism of decision making, we would suggest that the Fund representatives are Officers with investment experience / expertise;

- It may be worth considering having an elected official from each local Committee form a Consultative Committee that could receive periodic reports from the Investment Committee.

Summary:

- Key to any potential collaborative project is whether each individual Fund is on board and willing to commit to a shared set of principles.

- We would suggest that these principles are formalised at outset and are focused around:

    - Aims of collaboration
    - Measures of success
    - Decision making process
    - Engagement at a local level
    - Operational considerations

- In putting in place an appropriate governance structure, a balance needs to be struck between retention of issues at a local level (where appropriate); but the need to delegate aspects where it "makes sense" to do so.

4

Avoiding Complexity

What can be done within the current arrangements for each Fund?

It would seem sensible before embarking on a project requiring change, to consider whether there are efficiencies that can be easily exploited within the existing arrangements.

We have considered the following areas:

- Investment manager fees (based on commonalities across current assets / manager structure);

- Other expenses (e.g. custodian and consulting costs).

Investment manager fees

An obvious place to start is to review the aggregate investment manager fees currently in place across the eight Funds. We reviewed the following areas:

- Aggregate fees — how do fees of the eight Funds in aggregate compare to other large mandates?
- Potential for savings within passive mandates
- Commonalities within active mandates
- Initial thoughts on alternatives
- Implications for bond portfolio

A summary of our findings is below. Further detail on each aspect is outlined in the appendix.

	Comment can
Aggregate fees	Current fees are generally competitive across the board compared to our Global Fee Survey (used to benchmark fees relative to the industry). However, due to the lack of comparable data, our Fee Survey does not provide information on mandates of the scale possible across the eight Welsh funds collectively.
P- otential for savings within passive mandates	Fees are relatively good value compared to other passive mandates globally. However, this is an area of increasing focus for joint procurements, so it may be an area worthy of investigation. We believe there is potential for fee savings in Wales as a collective seeking to negotiate with the leading passive managers. Based on recent experience, this ***could*** lead to savings of £800,000 p.a. We would caution however that other factors (such as profits on stock lending and costs of trading) would also need due consideration in addition to headline manager fees.
C- ommonalities within active UK and global equity strategies	There is limited commonality between the Funds' manager line-up. Even where there are consistencies at a manager level, due to Fund specific requirements in the majority of cases there is little scope to enable Funds

to leverage any economies of scale under the current structure.

However, there is consistency of strategy and allocation across the Funds and so equity mandates may actually offer the greatest scope for initial collaboration.

Initial thoughts on alternative assets	It is very difficult to quantify any potential for immediate cost savings through leveraging any commonalities due to complex structures in place. There is also little point in attempting to renegotiate fees with private markets managers given the Funds are "locked in" to these investments. There is potential for significant savings should Funds collaborate on alternatives under a revised model that aggregates Funds' assets — but the "model" will need to be in place first.
Implications for bond portfolios	The make-up of the individual Funds' bond portfolios are wide ranging, and can broadly be categorised into UK Government, UK Corporate and Global bonds. There is little commonality between mandates and so little scope to harvest significant fee savings with mandates in their current formats. We do however note that from a strategic perspective the case for holding bonds in the current environment is changing. Therefore to the extent to which these mandates are up for review there may be more potential for collaboration going forward.
Other expenses	The Funds incur "other" expenses of c£1.6m p.a., with the largest expenses relating to custodian and consulting costs. We would view custody as an area where fee savings could be made. From the data provided, there are at least 3 named custodians and by looking to procure a single custodian across Wales we would expect significant savings to be made as a result of incredibly aggressive pricing in the market. We would suggest any wins here are considered as part of the wider collective investment model for Wales as opposed to a standalone custodian decision being made.

Summary:

- We have investigated the potential for cost efficiencies in respect of investment manager fees and other expenses under the existing arrangements. Given the allocations and consistency of UK and global equity across the Funds, these mandates offer the greatest scope for initial collaboration.

- The diversity across mandates at present suggests that there are limited initial savings to be made without aggregating assets in some way. The exception would be the passively managed funds, which could achieve savings of c£800,000 p.a. should the funds appoint a common manager.

- There are also potential fee savings to be made in respect of appointing a common custodian. We would however suggest that this is considered as part of any wider collective investment model considered.

Asset Pooling

Should Assets be Pooled?

In order to achieve lasting scale, we believe that there needs to be some form of asset pooling across Funds. This need not be wholescale; we would suggest that careful consideration is given to the type of assets or mandates that would provide either the greatest efficiencies, or the greatest opportunity for creating excellence in investment.

Joint procurements would provide an initial level of cost savings, but there still needs to be some sort of structure in place to enable the project to "have legs" and with that in mind, joint procurements probably have more mileage for less complex mandates such as passive.

The advantage of pooling is that it provides some sort of physical structure on which a joint entity can be based.

As part of this exercise, Officers considered in detail various methods of asset pooling and the types of structure that exist. The conclusion was reached that from a risk management perspective, a regulated structure with proper operational controls and expertise will provide a more robust solution and establish a professional framework that would stand up to best practice and provide longevity of approach.

Whilst at first glance, an unregulated structure like a Common Investment Fund may feel like a more simple solution it doesn't solve any governance issues for the Welsh Funds. There would need to be a lead authority or a joint body of some description that would take responsibility for manager selections, reporting and monitoring, transitions, and unitisation.

A Joint Structure

How to achieve a joint, regulated structure

In order to establish a Welsh fund / vehicle, a Management Company will be required and there are two options; either "build" a Welsh Management Company, or "rent" the structure from a provider.

In practice, the two options become three;

1. Establish a Welsh Management Company ("build");
2. Use the Management Company of a third party custodian ("rent");
3. Access the Management Company of third party provider to tailor a Welsh solution ("rent").

Option 1— Establish a Management Company (the "build" option)

Costs and Timescales

Officers have considered in detail the requirements, timelines, costs and ongoing obligations associated with the establishment of a management company and related regulated fund structure.

As a guide, we estimate that the minimum timeframe involved to establish a fund and related entities is **12-18 months.** The timeframe is also contingent on a dedicated team of internal and external resources working on this project on a full-time basis and all aspects of the project going to plan.

In addition to the external tax and legal costs that we expect will be incurred (estimated to be in the region of £0.5m to £0.8m) considerable resources, both internal and external (in the form of consultants) in terms of time and costs need to be considered.

We estimate total resource related costs (internal and external) to be in the region of £2.7 to £3.1 m, bringing the **total initial cost estimate to between £3.2m and £3.9m.**

This estimate is based on Mercer's own experience and cannot be relied upon as a definitive figure and is also contingent on no OJEU processes being triggered for providers, which we believe in practice is unlikely.

Under the appropriate regulation, the initial capital requirement for the Management Company is estimated to be between £3 - £6 million. This amount is subject to regulatory change and ongoing monitoring by the Welsh Funds.

On-going considerations

Having established a Management Company and related Fund, the Welsh Funds have ultimate fiduciary responsibility.

While certain functions may be outsourced, there is a requirement that the Fund is not a "letter box" entity. The Management Company will need to satisfy the Regulator on an ongoing basis that it has adequate management resources to conduct its activities effectively and employs personnel with the skills, knowledge necessary for the discharge of the responsibilities allocated to them.

There are considerable ongoing governance, oversight and reporting requirements to be undertaken by the Welsh Funds as a result of the establishment of regulated entities and funds. Examples include:

- Board representation and quarterly Board meetings
- Required governance structure and committees, internal policies and procedures to mitigate risk
- Oversight of all service providers
- Regulatory reporting and filings

The Welsh Funds will be subject to the Regulator's supervision, which is carried out as follows:

- Analysis of returns submitted to the Regulator
- Risk-rating of companies
- Themed and general inspections
- Review meetings
- Regular correspondence and engagement with companies under Central Bank supervision

The Regulator has the power to impose sanctions on regulated entities for breaches of regulatory requirements ranging from substantial fines to, ultimately, the loss of authorisation. It is therefore crucial that any regulated entity has access to an adequately resourced and experienced team of compliance professionals. As is common with regulators around the world, the Central Bank is increasingly focused on supervision and enforcement.

Option 2 — Access the Management Company of a third party provider (the "rent" option)

The second option would be to use the standalone, pre-existing Management Company of a Custodian or an Investment Manager (for example). This approach would provide the benefits of avoiding to "build" an internal management company and would therefore avoid the associated cost and complexity outlined in Option 1.

There are of course a range of governance considerations related to this option and Officers will consider these in detail before and as part of any potential procurement exercise.

However, it should also be noted, that while a Custodian and/or Investment Manager may be able to provide a Management Company and infrastructure, the needs to support a collaboration framework are typically wider. The Welsh Funds would still require internal resources to support the governance and operations layer outside the Management Company to cover project management, manager appointments and implementation and asset transition.

A Custodian would not typically have the internal investment expertise or capabilities to provide this wider support. In addition, the appointment of an investment manager in this role may create challenges with other investment managers managing the assets of the Welsh Funds in that they would need to provide their stock holdings and undertake fee negotiations (typically confidential information) with a competitor.

Notwithstanding this, Option 2 would be a viable option where the Welsh Funds would like to establish an internal team (significantly less than would be required under Option 1) to co-ordinate their investment arrangements.

Option 3 — Access the Management Company of third party provider to tailor a Welsh solution (a further "rent" option)

The third option is for a third party provider to tailor a solution for Wales using their existing infrastructure and **in addition, to support the operational co-ordination of the new framework on a day to day basis.**

Ideally a provider would be found who has experience of this role with other UK pension schemes and has established a number of different umbrella fund structures. This means that the Welsh Funds would not need to go through the full legal process of establishing a fund - the provider could simply launch a bespoke fund via an umbrella structure.

In addition, Option 3 would not require the development of internal Wales' resources as the appointed provider would provide the expertise, project management and operational governance to set up and operate the new arrangement on behalf of the Welsh Fund.

Some thoughts on the differences between Options 2 and 3

The difference between Option 2 and Option 3 is that the latter allows for an integrated investment advisory support to the Welsh Investment Committee decision-making process, along with implementation in terms of set up, execution of manager appointments / replacements, transitions and rebalancing etc. **These services would need to be contracted separately under Option 2.**

It is also unlikely that Option 2 would provide support in terms of co-ordinating and execution between managers, transition managers, custodians, pension advisors, legal advisors. It is therefore likely to require specialist / specific Officer support; perhaps in the form of a dedicated project manager or internal team or delegated to external consultants.

Specifically, Option 2 would also not allow for any potential manager fee reductions above and beyond the scale of the Welsh assets (no access to global buying power, which may be important if take up amongst the Welsh Funds is low to begin with).

Because the set up costs of option 3 are likely to be absorbed by the provider (and probably recouped by way of a minimum ongoing fee once assets are invested) there are no cost implications for Funds who decide not to participate from the outset. This does however assume that a minimum scale is achieved via those Funds who do invest.

It is also worth raising the issue of ongoing advice in terms of manager selection and implementation, and monitoring. Under Option 3, all these items are covered and there would be no requirement for individual Funds who are committed to engage these services at a Fund level. Of course, it may be the case that existing Fund consultants and advisors are engaged to provide advice on the recommendations of the Investment Committee to the collective structure, but that would be an individual Fund choice.

Nonetheless, we understand that, in order to fully assess the differences between Options 2 and 3, the Welsh Funds may wish to seek proposals from interested parties along with associated cost estimates.

Costs of rental (Options 2 and 3) versus current approach

Officers have considered in detail the indicative costs associated with the existing approach compared with either of the two rental options.

As a starting point, and for simplicity, we looked at the eight Funds' **active UK and global equity** allocation and assessed the potential costs of a collaborative approach according to various levels of take up.

There were several reasons for starting with one asset class only:

- It is more tangible in the sense that the simpler we make it, the fewer assumptions that are needed,
- We believe that by starting with one asset class and getting a structure in place, it is more likely that any collaboration project will actually get off the ground;

- Equity is arguably far less controversial (and easier for a collective to agree on) than a wider ranging project such as "alternatives";
- Once a robust governance structure is in place, more complex decisions such as the structure of an alternatives portfolio have a proper forum for discussion.

The potential estimated cost savings for options 2 and 3 are outlined below:

Cost saving (p.a.)	100% take up	50% take up	25% take up
Option 2	£1.6m	-£0.3m	-£0.5m
Option 3	£2.7m	£1.0m	£0.1 m

The calculations above relate only to the tangible expected cost savings relating to investing UK and global equities collaboratively. Further savings would be achieved as more assets (in particular alternative assets) were introduced to the structure. In addition, the performance impact of an improved governance structure has not been incorporated.

There are several notes to the estimated and these can be found in the

appendix. **Recommendation**

We would discount the build option (option 1) on the grounds of initial cost, timings and resource constraints and would recommend that consideration is given to Option 2 or 3. The differences between Option 2 and 3 relate to the desire for the Welsh Funds to establish an internal team to co-ordinate and manage day to day the various components of the new collaborative arrangements. This is the key question that should be considered (along with the cost) between Option 2 and 3.

We would **further recommend** that the Welsh Funds consider the following question:

Is there a need for a "big bang" solution (i.e. having a collaborative approach that covers all asset classes from day 1) or should a solution be phased or incremental?

We would strongly recommend that consideration is given to the latter, on the following grounds:

- Although the costs savings associated with a single asset class are clearly lower than the entire asset allocation, starting singularly means that a platform and governance structure can be built that will allow more complex decisions to be given proper consideration.

- We would predict that by starting with an asset class such as equity and allowing others to follow, the project will have a much shorter timescale to fruition.

Summary:

- In order to establish a Welsh fund / vehicle, a Management Company will be required — this can be **"built"** or the structure could be **"rented"** from an existing provider.

- The estimated costs of build would be c£3-4million and it would take at least 12-18 months to establish, plus any procurement time in addition. The internal resource required to build would also be significant. On this basis, **we have discounted "build" as a viable option for Wales.**

- There are two main ways in which the Funds could "rent" a Management Company — either solely purchasing the infrastructure (option 2) or by using a tailored third party approach, which would also incorporate governance and operational oversight (option 3). **The upfront costs, internal team requirements, and timescales are significantly reduced under the rental option and is therefore our favoured approach.**

- There are **expected to be cost savings associated with collaboration** and we have provided information using active UK and global equities as a starting point. The costs do however vary depending upon take up and the solution sought (from an increase in fees of £0.5m p.a. to a reduction of fees of £2.7m p.a.). **The savings would increase as more asset classes are incorporated; significantly in the case of alternatives.** In addition, the additional benefits in terms of long term investment philosophy and the governance premium should also be considered.

- The **key question to decide between Options 2 and 3 relates to the desire to develop internal resources and priority for cost-efficiency** across the Welsh Funds. **Costs savings are expected to be increased further if other asset classes are adopted over time —** most notably from alternatives, albeit noting that this is likely to be a longer term project first in terms of running off existing commitments and second building a long term collective strategy.

- In setting up an appropriate course of action, we would **strongly advocate a phased / incremental approach to collaboration** (e.g. using global equities as a starting point); as opposed to a "big bang" solution (which might cover all asset classes from day 1). This would reduce the timescales for implementation and the level of complexity in the shorter term.

- We would suggest that the **next step for the Welsh Funds would be to invite nonbinding proposals from potential "rental" providers** in order that a comparison of services and costs can be made.

7

Legal Issues

Advice has been sought from Sacker and Partners who looked at the following principal questions:

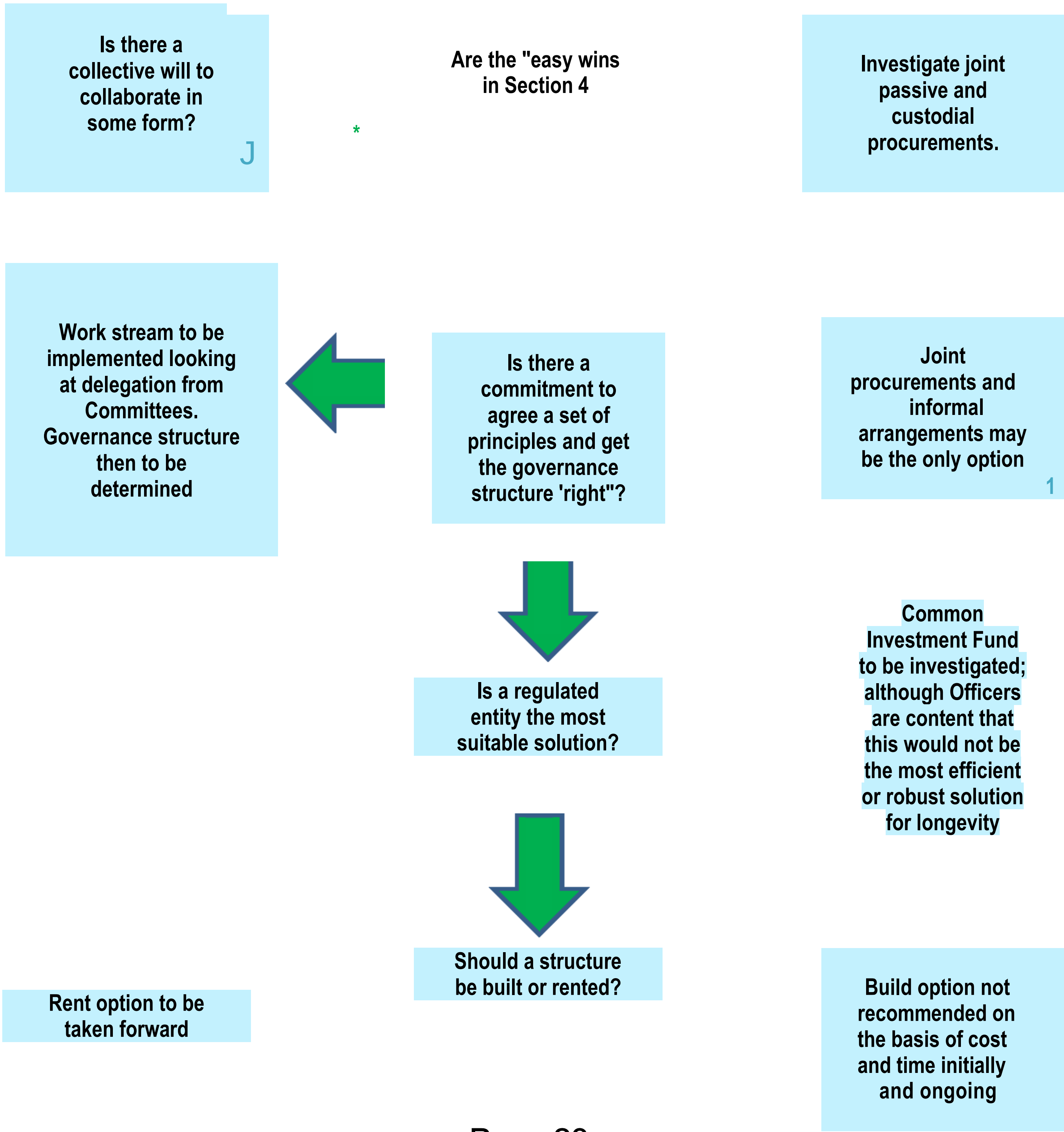
- **do the Councils have power to implement the Proposals being considered;**
- **how do the proposals interact with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 ("Investment Regulations"); and**
- **what procurement obligations apply?**

Sackers have not identified any legal show stoppers which would prevent the Councils proceeding. However, they do identify a number of points in relation to governance, delegation and procurement that Officers will take into account as the project progresses.

Decision Making — An Overview

The project undertaken by Officers has been all encompassing, and a summary has been provided within this report.

By way of a summary, the following diagram may help the reader work through the decisions that Officers are minded to make:



9

Summary and Recommendations

There are significant savings to be made; both direct and indirect, some more quantifiable than others, through pooling assets and investing collectively.

Governance and delegation

For the Welsh Funds to use a collective structure there must be a shared vision and we would suggest that a set of principles are established at outset.

We believe that there is a premium to be achieved through good governance and sufficient time should be spent in establishing the correct construct of an investment committee of a collective investment structure.

We further believe that there is a real opportunity here to establish a collective with long term principles of investment at its heart; a philosophy that in itself has been show to add real value.

Steps that could be taken without the need for a collective structure

In the particular circumstances that the Welsh Funds find themselves (most notably little cross-over of existing mandates), we conclude that there are few "easy wins" in terms of leveraging existing mandates. We do however recommend that a joint procurement is effected for passive management and possibly custodial arrangements (once decisions have been made on a collective structure).

We would suggest that a single passive manager for Wales would not need to operate under a collective structure and that savings of around £800,000 p.a. could be made if all Funds participated at current levels of assets under passive management. It is likely that this would need to be procured under OJEU due to the additional services deployed by passive managers, such as swing management / rebalancing roles. We have not allowed for transition costs in this instance, on the grounds that passive mandates ought to be transferred between managers on an in-specie basis.

In addition, we note that a joint custodian procurement, presumably utilising the National LGPS Custodian Framework, could harvest further savings. ***However, this is not a step we would suggest considering until decisions are made on collective investing.***

A collective structure

We have recommended, for reasons of future proofing and efficiency, that ***a regulated vehicle is the optimal solution*** for any collective vehicle.

We would further recommend that ***a structure is "rented"*** (i.e. leveraging the existing infrastructure of a third party) ***as opposed to "built"*** (on the grounds of cost, resource and time). An increasing number of sophisticated institutional investors across Europe are moving in this direction.

The attraction of a rental model lies in its ***flexibility;*** there will be minimum asset sizes that need to be committed in order to make it a viable proposition for the provider, but by no means do all eight Funds need to commit all of their assets to make it work. We suggest that a rental model using active equity as a starting point will offer tangible savings. This feels like an "easy win"; a starting point to try out a collective arrangement whilst a longer term plan on more complex assets is determined.

There are reduced or no set up costs to be incurred under Options 2 and 3, other than procuring the provider, by the Funds. These are bourne by the provider who will likely charge a minimum ongoing fee for an initial period in order to cover this; just an ongoing operating cost, which means that Funds need only commit (and pay) when they are ready to invest. Of course the cost savings would be greater the more Funds that invest, but we would suggest that the idea of a platform being available to rent / use when needed may be more attractive than compulsion to use a model that has been expensive to build independently.

Under the right model / provider, there would be no "give up" in innovation; the Funds would be free to consider a range of options and perhaps these are more plentiful in the alternative assets space.

The next step will be to assess the options that are available from the various providers under this model and we can help formulate a template for discussion if required.

Critical Mass

Under the rental model, critical mass will be determined by the minimum fee set down by the chosen provider, but it will also depend on the time period over which savings need to be demonstrated.

For example, if half of the Funds (by asset value) commit to looking at global equities first under a rental model, then the immediate fee savings may be net neutral and a commitment would be needed towards a longer term aim of adding additional asset classes.

Legal Issues

Sackers' high level advice confirms that the use of a contractual vehicle should not, in their view, be subject to any limits under the LGPS Investment Regulations. They have not identified any show-stopper legal issues with the use of a manager, either rented or built.

Sackers have also confirmed their view that there is no legal obligation to go through a formal Procurement Regulations 2015 (or "OJEU") procedure in respect of the initial investment into a bespoke pooled vehicle or in respect of the appointment of a "rented" manager. However, they note that some Councils choose to go through a procurement obligation for policy and/or reputational reasons even where the Regulations do not require this.

Recommendations

- To consider the appointment of a single passive manager across the eight Welsh Funds (regardless of any decision to proceed with a collective structure; although noting that this could just as easily fall under the collective structure for ease).

For actively managed assets:

- To avoid compulsion; a collection of the willing with a shared set of principles is likely to result in a more robust, focused arrangement;
- To be clear on guiding principles;
- To consider the governance structure;
- To consider the set-up of a regulated vehicle;

- To consider leveraging the infrastructure of a third party provider to tailor a Welsh solution.

- To start with a single asset class, with a view to adding more complex propositions once the structure and its governance arrangements are up and running. Given our analysis, both UK and global equity would offer a strong starting point to fit into the new collaborative framework given the allocation and consistency of these mandates across the schemes and the potential to leverage material cost savings.

- We would suggest a training workshop to discuss the details and workings of the new framework to be set up for the summer period.

- After the workshops, the next step for the Welsh Funds would be to invite non-binding proposals from potential providers in order that a comparison of services and costs can be made.

Next steps

We would see the next steps of the project being as follows:

Stage	Time scale
Development of guiding principles	Summer 2015
Training for Key Stakeholders on principles and options	Summer 2015
Workshop / training for Officers on the operational aspects of the "rent" Summer 2015 option.	
Draft of specification for providers	Q3 2015
Draft Terms of Reference for All Wales Investment Committee	Q3 2015
Each Fund to work through constitutional issues in terms of delegation Q3 2015 to All Wales Investment Committee	
Initial due diligence meetings with providers	Q4 2015
OJEU Process to begin (if required)	Q4 2015

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Jo Holden
Mercer
July 2015

APPENDIX

Notes to cost savings calculations

The savings quoted are in relation to manager fees only and for one asset class (UK and global equity) only. It should also be noted that recent fees for UK equity have been higher than has historically been the case due to strong performance and the addition of performance related fees. Therefore, rather than use more recent fees, we have taken a longer term historic average.

Alternative assets are the area where anecdotally the largest savings could be made but this would be a longer term project first in terms of running off existing commitments and second building a long term collective strategy.

Over time, for a Fund committing a significant proportion of assets, there would be associated reductions in fees for:

- **Custody**
- **Reporting**
- **Procurement / manager selections**

Based on each Fund committing to the collective arrangement, we estimate an additional £0.1m of savings per annum per Fund (or £0.8m collectively).

In addition, the additional premia discussed earlier in terms of *long term investment philosophy* and the *governance premium* should also be considered.

Additional costs

There would also be transaction costs in migrating to the new arrangement. However, in practice, we would expect the fund to be built around existing high quality managers where appropriate.

There would also be the costs of procurement and internal resource to be

incorporated. *Implementation fee*

Options 2 and 3 may have an "implementation fee", be that implicit or direct.

All services will be included within Option 3 and the provider may well waive the fee.

Option 2 however will require the Welsh Funds to undertake, or outsource, the following tasks and therefore there will be a set up or implementation cost:

- **Advice in relation to manager selection and portfolio construction**
- **Procurement of managers**
- **Transition services**

Assumptions

The key assumptions outlined in the analysis are as follows:

- **Current approach:**

  We have assumed the current manager fees (including performance fees) represent the cost of the typical manager fees under the existing arrangements. Where take up is reduced, we have assumed the basis points fee remains the same.

- **Option 2 — Custodian approach:**

  We have assumed that, based on the size of assets in place should manager appointments be made as a collective the costs could reduce should all global equities be moved into this structure. The fees secured under the 50% and 25% take up options are higher to reflect the discounts being secured with managers reducing.

  The structural fee in adopting this approach with a custodian increases (in basis point terms) as take up rates fall.

- **Option 3 — Tailored approach:**

  We have assumed that using a third party provider, the fees secured with managers would be the same regardless of the take up. This is owing to the buying power already being in place from a global organisation with extensive assets under management

  In line with Option 2, the structural fee in adopting this approach with a custodian increases (in basis point terms) as take up rates fall.

The numbers outlined here are indicative and would be dependent upon the managers and structural platform used.

Clearly the above relates solely to actual monetary cost savings and does not allow for any potential for improved decision making and the extent to which this translates to improved investment returns.

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4COMPANIES

Briefing Report: Welsh Collaboration Investment Group, July 2015

1.00 PURPOSE OF REPORT

1.01 To ask Members to approve the participation by the Fund in a joint procurement exercise with the other 7 pension funds in Wales for the appointment of a single provider for passive investments.

2.00 BACKGROUND

2.01 The Society of Welsh Treasurers (SWT) Pensions Sub Group commissioned Mercer to develop a business case for the establishment of a governance structure and investment framework that will allow the eight Welsh LGPS funds to invest collaboratively.

2.02 Mercer completed this report in May 2015 and one of the recommendations was to consider the appointment of a single provider for passive investments across the eight Welsh funds. Further, that this could be done in advance of any further work on a 'collective investment vehicle' and that significant savings could be achieved.

2.03 It was agreed at the SWT Pensions Sub Group meeting on 26 June 2015 that a sub group of investment officers from all eight funds would meet and provide advice on this recommendation to the September meeting and a briefing paper for all funds to present to their panels/committees.

2.04 The investment officers met on 31 July 2015 at which there was a consensus for a potential way forward following detailed discussion.

3.00 CONSIDERATIONS

Passive Mandates

3.01 To remind Committee Members, managers of passive investments simply follow the index and hence the fees are low compared with active mandates where manager skill is required to pick stocks. Therefore, the choice of manager is of relatively less importance and fees are the main driver for the procurement.

3.02 However, there are some more subtle differences between providers relating 'bid offer spreads', stock lending, currency hedging and the range of funds available which have a marginal impact on investment performance and need to be considered alongside fees. Hence it was concluded that appointing a third party to assist with the procurement would add value to the process.

3.03 In Wales, we have circa £3bn passive equity and bond exposure across the eight funds with **three managers** across **eighteen mandates**. Analysis showed there is a disparity of fees between managers and mandates leading to the assumption that immediate savings could be made if one provider was appointed which agreed with the Mercer report.

3.04 There are differing approaches to passive exposures across the funds, for example, some preferring a global rather than regional approach but the aim of the procurement would be to appoint a provider for passive investments who could meet both current and future needs of all eight funds. Hence certain agreed principles are recommended to be adopted:

- Individual investment strategies (geographical requirements) would be accommodated.
- Each fund would retain investment autonomy and independence and ownership of assets.
- The passive mandate would be either pooled or segregated (if no fee impact).
- ESG considerations and currency hedging to be accommodated if required.

3.05 Based on these principles the investment officers agreed to recommend:

- The appointment of one provider for passive investments on behalf of the eight Welsh Pension Funds.
- A joint procurement exercise to deliver fee savings to all eight funds by jointly appointing the same provider.
- The appointment of a third party to facilitate the procurement and provide expert advice, the costs to be split equally, which will be sourced via the Clwyd Fund's consultant framework.

3.06 Once approved by Committees/Panels delegation for the appointment should be given to relevant investment officers.

Timetable

3.07 If approval is received for the procurement and relevant delegations given the new provider could be appointed and in place by April 2016. This assumes the Clwyd Fund launches the search for a consultant early October which enables the OJEU search to commence for the provider by the end November 2015.

4.00 <u>RECOMMENDATION</u>

4.01 That Members agree to the participation of the Fund in the joint procurement exercise as outlined in the report.

MEETING	**PENSIONS COMMITTEE**
DATE	**8 SEPTEMBER 2015**
PURPOSE	**CIPFA'S CODE OF PRACTICE REQUIRES THAT A REPORT BE PRODUCED ON THE RESULTS OF THE COUNCIL'S ACTUAL TREASURY MANAGEMENT ON BEHALF OF THE PENSION FUND.**
TITLE	**TREASURY MANAGEMENT 2014/15**
AUTHOR	**CAROLINE ROBERTS, INVESTMENT MANAGER**

1. Introduction and Background

CIPFA's revised Code of Practice on Treasury Management was adopted by the Council on 1st March 2011 and the Council fully complies with its requirements. The Code requires that I report on the results of the Council's actual treasury management in the previous financial year against expectations.

In accordance with the Welsh Assembly Government's Statutory Guidance on Local Government Investments, which requires an authority to produce an Annual Investment Strategy, it was considered best practice for the Gwynedd Pension Fund (the "Fund") to adopt Gwynedd Council's Treasury Management Strategy Statement (TMSS) for 2014/15, as amended for the purpose of the Pension Fund. The Pensions Committee approved the TMSS at its meeting on 17 March 2014. As a result, I am required to report on the results of the actual treasury management in 2014/15 against expectations.

2. Investment Activity

The Welsh Assembly Government's (WAG's) revised Investment Guidance came into effect on 1st April 2010 and reiterated the need to focus on security and liquidity, rather than yield. It also recommended that strategies include details of assessing credit risk, reasons for borrowing in advance of need and the use of treasury advisers.

Pension Fund Balances	Balance on 31/03/2014 £m	Balance on 31/03/2015 £m
Balances	10.7	13.4

As requested by the Pensions Committee on 17 March 2014, the pension fund's money was pooled with the Council's general cashflow. As agreed at the Pensions Committee on 24 March 2015 this arrangement continues in 2015/16. Interest rates are still very low but there is no reason to change this decision.

The table below shows a summary of where this pooled money was invested during 2014/15.

Investments	Balance on 01/04/14 £'000	Investments Made £'000	Maturities/ Investments Sold £'000	Revalue to Fair Value £'000	Balance on 31/03/15 £'000	Average Rate %
Call Accounts with Banks with ratings of A- or higher - short term	20,825	157,650	(160,055)	0	18,420	0.47
Investments with Banks and Building Societies with ratings of A- or higher - short term	27,000	52,597	(42,595)	0	37,002	0.78
Building Society Covered Bond – long term	0	1,088	0	33	1,121	0.45
Money Market Funds	0	89,796	(89,796)	0	0	2.09
TOTAL INVESTMENTS	**47,825**	**301,131**	**(292,446)**	**33**	**56,543**	
Increase/ (Decrease) in Investments £m					8,718	

Security of capital has remained the Authority's main investment objective. This was maintained by following the Authority's counterparty policy as set out in its Treasury Management Strategy Statement for 2014/15.

Counterparty credit quality was assessed and monitored with reference to credit ratings (the Authority's minimum long-term counterparty rating was A- across rating agencies Fitch, S&P and Moody's), credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

Credit Risk

Counterparty credit quality as measured by credit ratings is summarised below:

Date	Value Weighted Average Credit Risk Score	Value Weighted Average Credit Rating	Time Weighted Average Credit Risk Score	Time Weighted Average Credit Rating	Average Life (days)
31/03/2014	5.69	A	5.80	A	102
30/06/2014	5.19	A+	5.12	A+	139
30/09/2014	5.01	A+	3.21	AA	118
31/12/2014	5.39	A+	3.49	AA	148
31/03/2015	5.24	A+	3.62	AA-	64

Scoring:
-Value weighted average reflects the credit quality of investments according to the size of the deposit
-Time weighted average reflects the credit quality of investments according to the maturity of the deposit
-AAA = highest credit quality = 1
- D = lowest credit quality = 26
-Aim = A- or higher credit rating, with a score of 7 or lower, to reflect current investment approach with main focus on security

Counterparty Update

The European Parliament approved the EU Bank Recovery and Resolution Directive (BRRD) on April 15, 2014. Taking the view that potential extraordinary government support available to banks' senior unsecured bondholders will likely diminish, over 2014-15 Moody’s revised the Outlook of several UK and EU banks from Stable to Negative (note, this is not the same as a rating review negative) and S&P placed the ratings of UK and German banks on Credit Watch with negative implications, following these countries’ early adoption of the bail-in regime in the BRRD.

S&P also revised the Outlook for major Canadian banks to negative following the government’s announcement of a potential bail-in policy framework.

The Bank of England published its approach to bank resolution which gave an indication of how the reduction of a failing bank’s liabilities might work in practice. The Bank of England will act if, in its opinion, a bank is failing, or is likely to fail, and there is not likely to be a successful private sector solution such as a takeover or share issue; a bank does not need to be technically insolvent (with liabilities exceeding assets) before regulatory intervention such as a bail-in takes place.

The combined effect of the BRRD and the UK’s Deposit Guarantee Scheme Directive (DGSD) is to promote deposits of individuals and SMEs above those of public authorities, large corporates and financial institutions. Other EU countries, and eventually all other developed countries, are expected to adopt similar approaches in due course.

In December the Bank’s Prudential Regulation Authority (PRA) stress tested eight UK financial institutions to assess their resilience to a very severe housing market shock and to a sharp rise in interest rates and address the risks to the UK’s financial stability. Institutions which ‘passed’ the tests but would be at risk in the event of a ‘severe economic downturn’ were Lloyds Banking Group and Royal Bank of Scotland. Lloyds Banking Group, [whose constituent banks are on the Authority’s lending list], is taking measures to augment capital and the PRA does not require the group to submit a revised capital plan. RBS, which is not on the Authority's lending list for investments, has updated plans to issue additional Tier 1 capital. The Co-operative Bank failed the test.

The European Central Bank also published the results of the Asset Quality Review (AQR) and stress tests, based on December 2013 data. 25 European banks failed the test, falling short of the required threshold capital by approximately €25bn (£20bn) in total – none of the failed banks featured on the Authority's lending list.

In October following sharp movements in market signals driven by deteriorating global growth prospects, especially in the Eurozone, Arlingclose advised a reduction in investment duration limits for unsecured bank and building society investments to counter the risk of another full-blown Eurozone crisis. Duration for new unsecured investments with some UK institutions was further reduced to 100 days in February 2015.

The outlawing of bail-outs, the introduction of bail-ins, and the preference being given to large numbers of depositors other than local authorities, means that the risks of making unsecured deposits rose relative to other investment options. The Authority therefore has started to use secured investment options or diversified alternatives such as covered bonds, in addition to unsecured bank and building society deposits. Deposits were generally made over short periods in order to reduce the risk. Use of secured options including non-bank investments and pooled funds as well as covered bonds is likely to increase in order to reduce the risk of default.

Update on Investment with Heritable Bank

The authority has now recovered 94% of its investment in Heritable Bank. It is likely that further distributions will be received and that the full amount should be recovered. The timing of future distributions is unclear and depends on settlement of the ongoing court case. Notice that a dividend will be paid in August 2015 has been received but the amount is not yet known.

3. Recommendation

The Pensions Committee is asked to receive the report on investment of the Fund's cash, pooled with the Council's cash, in 2014/15 for information.

Credit Score Analysis

Scoring:

Long-Term Credit Rating	**Score**
AAA	1
AA+	2
AA	3
AA-	4
A+	5
A	6
A-	7
BBB+	8
BBB	9
BBB-	10

The value weighted average reflects the credit quality of investments according to the size of the deposit. The time weighted average reflects the credit quality of investments according to the maturity of the deposit

The Authority aimed to achieve a score of 7 or lower, to reflect the Authority's overriding priority of security of monies invested and the minimum credit rating threshold of A- for investment counterparties.

COMMITTEE: **PENSIONS COMMITTEE**

DATE: **8 September 2015**

TITLE: **"Know your onions" - Local Government Pension Scheme Trustees' Conference**

PURPOSE: **To advise members of the content and value of the Local Government Pension Scheme Trustees' Conference, 25-26 June, 2015, in the Cardiff Marriott Hotel**

AUTHOR: **Dafydd L Edwards, Head of Finance**

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1. INTRODUCTION

The Local Government Pension Scheme (LGPS) Trustees' Conference provided interesting information about several aspects regarding development of the LGPS and aspects of fund investment. The event was attended by three delegates from the Gwynedd Fund, namely Councillor Peredur Jenkins, Councillor Eifion Jones, and Dafydd L Edwards (Head of Finance).

2. "KNOW YOUR ONIONS"

This conference was titled "Know your onions", and in the context of financial pressure facing Local Authorities, it was acknowledged from several points of view that the affordability and sustainability of the LGPS (particularly as individual funds) would be critically examined, therefore trustees must "know their onions" in order to be able to defend the LGPS.

3. LGPS – NATIONAL GOVERNANCE

The keynote speaker Bob Holloway, DCLG, focused on the "facilitative" work of the (national) Scheme Advisory Board, guidance on establishing Local Pension Boards, deficit management, key performance indicators, and funds taking undue risk. On structural reform of the LGPS, Bob Holloway confirmed that "the Government is considering its position".

4. FREEDOM AND CHOICE

Annemarie Allen, Senior Pensions Consultant with Barnett Waddingham, outlined the sweeping new flexibility from April 2015, LGPS members' ability to transfer to defined contribution schemes, the potential for less contributions from wages, and more enquiries to fund administrators.

Conference delegates generally supported the view that the Government's policy of providing flexible access to cash (withdrawing pension benefits) was an irresponsible "scandal".

5. CESSATION OF CONTRACTING OUT

Karen McWilliam and Alison Murray, both from AON Hewitt and formerly with Hymans Robertson, explained the significant additional National Insurance cost for employers (2.3% of the payroll on average), and complexity of reconciling pension scheme ("GMP") liability with HMRC records. They outlined how this reconciliation was a huge task for Pension Fund administrative staff which must be completed before April 2018, and could not be achieved within existing staff resources.

6. PROSPECTS FOR 2016 (TRIENNIAL VALUATION)

Liam Robson and Jeff Houston of the LGA presented general investment performance over recent years, and discussed setting of future actuarial assumptions, inflation and longevity, as well as cost pressures imposed on the LGPS by HM Treasury. While funds have remained cash positive since the last valuation, HM Treasury's revaluation methodology and 'club transfer' costs counter these gains.

7. INNOVATIVE WAYS TO INVEST

Andy Fox of Lancashire Pension Fund outlined their proposed partnership with the London Pensions Fund, which will mean pooling £10bn of assets to invest, but **not** fund merger.

The business case proved that collaboration in investment, would be worthwhile, purely from a (£10m pa) reduction in investment managers' fees, while it was suggested that investment outcomes could also improve.

The business case was challenged by Gwynedd Fund delegates, inter alia, and it was established that there was no evidence to prove better returns from pooling / size, but that is the two pension funds' aim.

A number of challenges were noted, including legal, governance, regulatory, political, and staffing issues.

8. ADDITIONAL VOLUNTARY CONTRIBUTIONS ("AVCs")

We received a lively and interesting presentation from Richard Harrison from the Prudential on AVC provision. He confirmed that the 100% tax free option from AVCs (unique to the LGPS) mean that they remain a good way to save for retirement and suggested that funds should do more to communicate this to scheme members.

9. OTHERS

Interesting presentations were also received from Eversheds on pensions' case law, national Shadow Board members on local boards' progress, and the Pensions Ombudsman on complaints against LGPS funds.

10. INVESTMENTS ACROSS THE GLOBE

Atul Shinh from Investec suggested that the economic cycle, further to rising equities since 2008, was not yet overheating. He viewed equities continued to be good value and even Japanese equities were exciting for the first time in decades.

He continued that technology looks attractive as an asset class, but careful selection is necessary with emerging markets and property.

On the "know your onions" theme, Investec closed the conference amusingly, saying *"that's shallot"*.

Gwynedd Fund delegates met Investec's Stephen Lee at the conference and secured free training (as provided at official LGPS sessions) for Gwynedd's Pensions Board.

11. CONCLUSIONS

This event included coverage of many aspects of pensions, delivered in an understandable format, and provided useful networking opportunities.

Further to all delegates' committed attendance at all sessions of the conference, Gwynedd's delegates are wiser further to attendance at the conference, and unanimously recommend that Gwynedd Pensions Committee should continue to support this event.