

WILTSHIRE COUNCIL

WILTSHIRE PENSION COMMITTEE

15 December 2016

BRUNEL PENSION PARTNERSHIP – APPROVAL OF FULL BUSINESS CASE

Purpose of the Report

1. Following the Government's announcement in the July 2015 budget statement that they intended to work with Local Government Pension Scheme (LGPS) administering authorities to ensure that they pool investments to significantly reduce costs, significant work has been undertaken to set up the Brunel Pension Partnership comprising ten LGPS Funds.
2. Regular reports have been brought to the Committee at all stages of the process, with additional engagement events also being held to provide the opportunity for the Committee to provide input to the proposals. As required by Government an initial joint submission from the ten Brunel funds was approved by the Committee on 1 February, 2016 and a further more detailed response was approved by the Committee in June and submitted to the Government in July 2016.
3. Following the July submission of what was in effect an outline business case, work has been continuing developing a Full Business Case (FBC) for the Brunel Pension Partnership. The FBC has now been completed and needs to be approved by each of the ten administering authorities in order that the establishment of the Local Authority Company can be progressed.
4. The FBC sets out the individual costs and benefits for each of the ten participating funds. The FBC is attached at Appendix 1 and other appendices are included in Part II of the agenda.

Background

5. The FBC seeks approval to establish a company called Brunel Pension Partnership Ltd (Brunel company or BPP Ltd), regulated by the Financial Conduct Authority (FCA), and the new governance arrangements to establish client side joint shareholder oversight and joint contract management. It comprises five sections:
 - The Strategic Case;
 - The Financial Case;
 - The Economic Case;
 - The Commercial Case;
 - The Management Case.

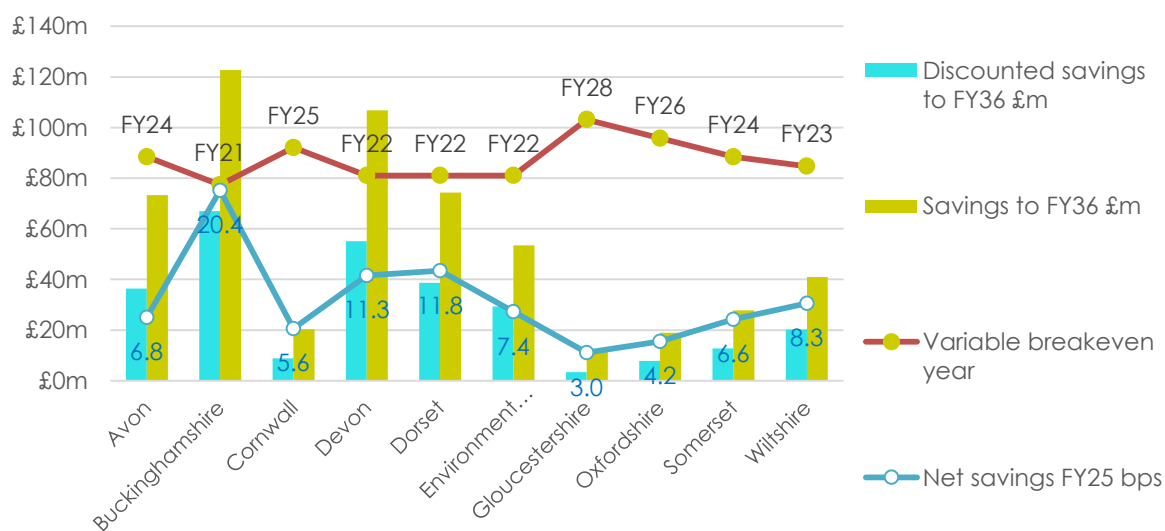
6. The FBC was reviewed by the Finance/Legal Assurance Group (FLAG), comprising the s151 and Monitoring Officers of each of the ten administering authorities, on 8 November 2016. It was supported by the Shadow Oversight Board, comprising the chairmen of the ten funds on 23rd November. The business case has been put together with significant work by officers of the ten administering authorities, supported by professional expertise provided by PwC (operational and financial support), Osborne Clark (legal support), Alpha (FCA expertise), JLT (project support) and Bfinance (investment advice). This work has supported and informed the views in this report and recommendations.
7. The strategic case focuses on the legal and regulatory requirements as well as the costs and benefits of pooling. The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (SI 2016 No 946) came into force on 1 November 2016. These regulations provide the legal basis which requires LGPS funds to pool their investments.
8. The financial case is drawn from a complex financial model that has been developed by the Brunel partnership in conjunction with PwC, which analyses the costs and savings for the partnership as a whole and for each of the individual funds. The model allows scenario testing, changes to individual assumptions and the removal of individual funds from the partnership for sensitivity analysis and stress testing the proposal. The core model analysis shows the breakdown between funds of a total of £550m forecast cumulative savings over the next 20 years.
9. The financial case also sets out the opportunity in the future if the Brunel company undertakes internal management of 50% of active equity investments internally from the 2022/23 financial year, but this decision would require the agreement of the 10 Shareholders funds.
10. The economic case examines two potential models for how to set up the Brunel company, either to rent it from a commercial provider or build it. An analysis was carried out in Stage 2 of the project to consider the relative merits and limitations of each model, examining them against three groups of issues: accountability; procurement and staffing; and costs. The analysis showed that the build model would have advantages over the rental model, especially on accountability.
11. The commercial case sets out the structure of the Brunel Pension Partnership company, and the governance and contractual arrangements that will exist. The Brunel company will be a new Financial Control Authority (FCA) regulated company wholly owned by the Administering Authorities. The company will be managed by the company board with a chairman, three other non-executive directors and three operational directors. The governance arrangements will include an Oversight Board representing each participating fund's pensions committee.
12. The management case looks at the project management that will be required:
 - to set up the FCA regulated company within the Brunel Pension Partnership (BPP) encompassing recruitment of staff, legal and physical set up, procurement of third party providers, definition and set up of the services, and obtaining FCA authorisation;
 - to establish the arrangements for governance of Brunel Pension Partnership Ltd (BPP Ltd / Brunel company) by the Administering Authorities (AAs);
 - to implement the client side governance, organisation and process changes.

Main Considerations for the Committee

13. The financial case for Brunel has been derived from the financial model put together by PwC. The core model forecasts cumulative savings for the Wiltshire Pension Fund of £41m over the next 20 years, which has a discounted present value of £20m (discount rate of 3%). This results in a breakeven point in the 2023 financial year. The savings are summarised in the following table and graph:

Costs and Savings to the Wiltshire Pension Fund 2015/16 to 2035/36

Year	Costs without pooling			Costs under the Brunel proposals					Savings/ (Costs) £m
	Manager Fees £m	Wiltshire Costs £m	Total £m	Manager Fees £m	Wiltshire Costs £m	Brunel Costs £m	Asset Gains £m	Total £m	
July 15 - Dec 16	8.64	2.82	11.46	8.64	2.82	0.12	0.00	11.58	-0.12
Jan 17 - Mar 18	7.40	2.42	9.82	7.40	2.42	0.64	0.00	10.46	-0.64
2018/19	6.19	2.00	8.19	5.85	1.85	1.76	0.00	9.46	-1.27
2019/20	6.42	2.05	8.47	5.27	1.90	3.14	-0.01	10.30	-1.83
2020/21	6.65	2.12	8.77	4.83	1.96	0.52	-0.06	7.25	1.52
2021/22	6.90	2.18	9.08	5.01	2.02	0.53	-0.15	7.41	1.67
2022/23	7.15	2.25	9.40	5.19	2.08	0.54	-0.21	7.60	1.80
2023/24	7.42	2.31	9.73	5.38	2.14	0.56	-0.30	7.78	1.95
2024/25	7.69	2.39	10.08	5.59	2.21	0.58	-0.40	7.98	2.10
2025/26	7.97	2.46	10.43	5.80	2.27	0.60	-0.50	8.17	2.26
2026/27	8.27	2.53	10.80	6.02	2.34	0.62	-0.61	8.37	2.43
2027/28	8.57	2.61	11.18	6.24	2.41	0.64	-0.72	8.57	2.61
2028/29	8.89	2.68	11.57	6.48	2.48	0.66	-0.84	8.78	2.79
2029/30	9.22	2.76	11.98	6.72	2.56	0.68	-0.97	8.99	2.99
2030/31	9.56	2.84	12.40	6.98	2.63	0.71	-1.12	9.20	3.20
2031/32	9.91	2.93	12.84	7.24	2.71	0.73	-1.26	9.42	3.42
2032/33	10.27	3.02	13.29	7.51	2.79	0.75	-1.42	9.63	3.66
2033/34	10.65	3.11	13.76	7.80	2.88	0.78	-1.59	9.87	3.89
2034/35	11.05	3.20	14.25	8.09	2.96	0.80	-1.75	10.10	4.15
2035/36	11.45	3.30	14.75	8.40	3.05	0.83	-1.95	10.33	4.42
Total Savings									41.00



14. The Brunel Partnership costs include estimated costs of transitioning assets, which are being shared by all the Pension Funds to ensure that no individual fund is disadvantaged by, or benefits from fund manager selection by the Brunel company. Other costs include the taxes involved in transitioning assets into the Brunel company and the operating costs of the Brunel company itself.
15. The actual asset transition costs for the Brunel pool will not be known until the Fund Managers have been appointed and will depend on the number of funds that need to be transitioned and the market conditions on the day of transition. The transition of assets is expected to begin in April 2018 through to 2020 for the majority of assets, although those illiquid alternative assets (which are less easy to sell quickly as there is not a defined exchange like the stock market, e.g. infrastructure / property) will need a longer transition timetable. However, from a Wiltshire Pension Fund perspective, even an increase of 50% in transition costs would only move out the breakeven point from 2023 to 2024.
16. The savings are achieved through reduced direct investment costs, predominantly investment manager fees, expected to be payable by the Pension Funds once the Brunel Company is operational. In addition there are the savings that the Pension Funds expect to make as a result of no longer needing to carry out tasks internally because of services provided by the Brunel company. In the case of the Wiltshire Pension Fund, this will be through reduced custodian, performance reporting costs and other investment administration costs. The asset gain figures reflect that the fee savings made remain invested in the Fund and will achieve an investment return.
17. In addition to the model's core estimate of savings, the finance case also outlines the opportunity for additional benefits from improved performance. This would result from improved diversification between managers and better risk management that could be achieved from investing in greater scale. A modest increase in returns of 2 basis points (0.02%) would increase the overall benefit to the Wiltshire Pension Fund over 20 years from £41m to £54m. In addition, there is a further opportunity to make savings should the Brunel company undertake internal management of 50% of active equity investments internally from 2022/23. This would increase the savings on external manager fees, and could therefore further increase the benefits to the Wiltshire Pension Fund.

Conclusions

18. Government policy, now brought into effect by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, requires the Wiltshire Pension Fund to pool its assets. In the light of this agenda the Fund has already committed to participating in the Brunel pool through the resolutions agreed at previous meetings of the Pension Committee. The Committee and the Council now need to approve the FBC to move forward with setting up the Brunel Pension Partnership Ltd company in order that the pooling proposals can progress to the implementation phase.
19. Although investment pooling is being driven by the central government agenda, the financial modelling that has been undertaken demonstrates that there are net savings opportunities for the Wiltshire Pension Fund in entering into the Brunel Pension Partnership. The detailed business case sets out the structures and governance arrangements that will be put in place, which will ensure that the Brunel company provides value for money to the Wiltshire Pension Fund.
20. The Committee is therefore asked to recommend the resolution to set up the Brunel Pension Partnership Ltd to Council. Further reports will be brought to the Committee as the project progresses.

Environmental Impact of the Proposal

21. There is no environmental impact of this proposal.

Financial Considerations

22. The attached FBC includes the financial considerations associated with this proposal and the main financial considerations are outlined above. A payback period of 5 years is the normal basis for approving a Wiltshire Council project in line with its invest to save policy. Although the current projected break even period for the Wiltshire Pension Fund in the FBC is 2023 (effectively 7.5 years), from the commencement of the transition of assets in April 2018, this falls within the 5 years timeframe, at which point investment fee savings are projected to be £1.8m per annum for Wiltshire. The assumptions used in this assessment have been set at prudent levels and stress testing reflected to show various scenarios. This still suggests a similar payback period for most changes in assumptions. As such the proposal is supported.

Risk Assessment

23. Government has signalled its clear intention that LGPS investment assets should be pooled and backstop legislation has been implemented to ensure funds invest in a pooling vehicle should proposals not be forthcoming or be ambitious enough. The FBC proposes a company structure that allows the Wiltshire Pension Fund to retain control over the governance and implementation of its future investment strategies through representation on the oversight board and through its rights under a Shareholders' agreement.

24. There remains a possibility that the proposal submitted isn't approved by the Government, as it's an approach not previously considered. Continual dialogue and meetings with representatives from HM Treasury and DCLG is ensuring they are aware of the content of this proposal and have a clear understanding of the structure and its operations. From the feedback received to date this risk appears low.

25. Participation in the pool also provides additional resilience and access to increased investment resources which can mitigate the investment the risk to the Fund.

Legal Implications

26. The legal implications arising from the FBC have been informed by the external legal adviser Osbourne Clarke and the advice has been taken into account in drafting the proposal.

27. The Local Authority Company will need to get Financial Conduct Authority (FCA) approval as required by central government, which is currently timetabled to take place between July 2017 and September 2017.

28. Under this FBC the decisions on strategic investment stay with the individual administering authority via the annual strategic investment statement. However by this proposal it is anticipated that implementation of those investment strategies will be carried out by the Local Authority Company which benefit from economies of scale.

29. The consideration and approval of this FBC will confirm in principle the strategic and financial merits of this pooling proposal and will authorise the move to the implementation stage.
30. The resolution delegates to the Pension Committee the implementation of the proposal but limits that delegation to substantially in compliance with the FBC.

Safeguarding Considerations/Public Health Implications/Equalities Impact

31. There are no known implications at this time.

Reason for Proposals

32. This proposal affects only the appointment, termination and on-going monitoring of individual investment managers currently undertaken by officers and the Wiltshire Pension Fund Committee. The implementation of the high level strategic investment strategy (e.g. which types of assets classes the Fund invests in) will remain with the Wiltshire Pension Fund.
33. Following the agreement by this Committee on 30 June 2016 to support the Fund's joint submission of the Brunel Pension Partnership, this report considers the FBC to commence the implementation of an FCA regulated company, Brunel Pension Partnership Limited. The rationale for being proactive in the establishment of an investment pool enables the Fund to retain a controlling influence in this process and provides the best current available option.

Proposals

34. The Committee is requested to consider and recommend to Full Council the following:
35. In its capacity as the Administering Authority for the Wiltshire Pension Fund, and having received and reviewed the recommendation of the Wiltshire Pension Fund Committee on 15 December 2016 and the Business Case attached to it, Wiltshire Council hereby resolves to enter into investment pooling as part of the Brunel project with respect to the Wiltshire Pension Fund's investments.
36. Such Resolution is made on and subject to the following terms and conditions:
 - a) That the Brunel Pension Partnership investment pool be developed, funded and implemented substantially in accordance with the terms and provisions described in the Business Case considered by the Pension Committee, and more particularly that:
 - a Financial Conduct Authority (FCA) regulated company to be named Brunel Pension Partnership Limited be established and operated with all necessary and appropriate arrangements as to its ownership, structure, governance and services capability.
 - a new supervisory body comprising representatives of the Council and all other participants in the Brunel Pension Partnership be established to ensure oversight of Wiltshire Pension Fund investments and participation in the Brunel Pension Partnership.
 - b) That subject to the continued viability of investment pooling, financial or otherwise Wiltshire Pensions Committee is authorised to undertake such tasks, after consideration of advice from its Chief Legal Officer, Chief Financial Officer and

Pension Fund Manager, as it thinks appropriate to progress implementation of investment pooling. To take such decisions and do all other things deemed necessary in order to promote the interests of the Administering Authority with respect to pooling, which without limitation shall include agreeing and authorising any documentation, contracts, terms of reference, financial expenditure or investment that may be required consequential upon the Fund's participation in the Brunel Pension Partnership. For the avoidance of doubt this includes the right of the Pension Committee to authorise the Chief Legal Officer and Chief Financial Officer to take such steps as are necessary to progress the project.

- c) That subject to the above, all such matters be carried out with the aim of achieving a target date for beginning investment pooling of 1 April 2018, and otherwise subject to such intermediate steps and timescales as may be considered appropriate and necessary by the Pensions Committee.

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Treasurer to the Pension Fund

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