CLWYD PENSION FUND

Statutory Guidance on Asset Pooling

Introduction

The Clwyd Pension Fund Committee welcomes the opportunity to contribute to this informal consultation on Statutory Guidance on Asset Pooling for administering authorities. The Clwyd Pension Fund will also participate in the response from the Wales Pension Partnership, therefore this will focus on matters of specific interest, and from the perspective of, the Clwyd Fund.

Background

Flintshire County Council (FCC) is administering authority for the Clwyd Pension Fund (CPF) and delegates responses to such consultations to the CPF Committee. The CPF Committee is five elected members from FCC, an elected member from each of the other two unitary authorities, a representative for other employers and a scheme member representative appointed via the joint trade unions, all with equal voting rights.

The Committee have also considered the views of the CPF Advisory Panel (which is the FCC Chief Executive, FCC Chief Financial Officer, Clwyd Pension Fund Manager, Independent Governance Advisor, Investment Consultant and Fund Actuary) on this consultation response at our Committee on 20th February 2019.

Context for CPF Response

The CPF Investment Strategy Statement (ISS) already outlines in some detail how the CPF manages investment and funding risks to achieve our objectives, including pooling. In terms of this consultation there are some points in our ISS the CPF Committee would like to emphasise:

- Before taking any investment decisions, whether strategic, tactical, passive or active management, private market investments (geographically local or otherwise), social impact investments etc., the CPF Committee ensures proper advice is taken. The CPF considers proper advice as being from a FCA regulated advisor which we think is much stronger than the definition within the LGPS Regulations. Additional due diligence is ensured by the Independent Governance Advisor including considering any conflicts of interest on advice received.
- In the longer term CPF is committed to investing assets through the WPP for the reasons outlined in the consultation subject to WPP providing the appropriate portfolios in line with the CPF's investment strategy. However, the CPF investment allocation is not a ‘typical’ LGPS fund allocation with focus on the risk management strategy (LDI or funding flightpath being a fundamental part), a relatively low allocation to listed equities (especially actively managed)

and a relatively high allocation to illiquid private markets. Early discussions between our Investment Consultants and the WPP Pool Company have identified difficulties of delivering certain parts of our strategy via the Pool, especially the risk management strategy. The CPF investment strategy is shown below for illustration and will be reviewed by our Investment Consultant next financial year. The CPF Committee is determined that pooling should not undermine our risk management approach and will continue to hold local assets **whilst proper advice is received to do so in the interests of our stakeholders**.

Asset Class	Strategic Allocation (%)
Developed Global Equity	8.0
Emerging Market Equity	6.0
Credit Portfolio	15.0
Multi-Asset Credit (liquid)	*12.0*
Private Credit (illiquid)	*3.0*
Real Assets Portfolio	12.0
Property	*4.0*
Infrastructure	*8.0*
Private Markets	10.0
Tactical Portfolio	21.0
Diversified Growth	*10.0*
Best Ideas	*11.0*
Managed Account	9.0
Liability Hedging	19.0

NB: 4% of the Developed Global equity allocation already transitioned to WPP. The other 4% is allocated to a Blackrock Smart Beta product which is part of a joint procurement for passive investments with member funds of WPP which is outside the definition of a ‘pooled asset’; in the consultation.

The Informal Consultation

On the whole the CPF Committee is content with the statutory guidance with the exception of some points of principle and detail relating to the CPF context above.

Para 3 Structure and Scale

1. **Para 3.1 – benefits of scale and collaboration**

We agree with the ambition to achieve the goals set out in this paragraph. However, the CPF Pension Committee already goes to great lengths to ensure that these benefits have been achieved for assets allocated prior to pooling.

We feel there are certain instances where pooling cannot improve the benefits set out over and above what the Committee has already achieved. This combined with the bespoke nature of some of the strategies held by the CPF mean we feel that the ambitions set out cannot be improved in a pooled environment for a select number of our holdings. An example of this is the Liability Hedging portfolio which has been designed to meet the specific liability profile of CPF and we make some comments about Responsible Investment and Social Impact at the end of the response.

2. **Para 3.6 – Regular review of active and passive management**

Although we agree that this should be reviewed, we do not agree that this is a matter for the pool company. There is a conflict of interest, especially as per para 5.5, passive investments can be held outside the pool and hence the pool company will not earn fees. This should remain a local decision with the pool member taking proper local advice and reviewing their Fund ISS appropriately. In addition the comment that “they should consider moving from active to passive management” should be followed by the wording “or vice-versa”. We believe each style of management offers benefits to investors.

Para 4 Governance

3. **Para 4.4**

We agree that as a CPF Pension Committee we should take a long term view of pooling implementation and costs and that we should take account of the interests of our scheme members, our employers and our local taxpayers and should not seek to simply minimize costs in the short term.

However, the CPF Committee’s fiduciary responsibilities are to our local scheme members and employers. Although decisions made in the interests of our local stakeholders will usually also benefit wider stakeholders across the pool and the scheme as a whole, we do not agree that we should be making decisions where it is to the detriment of our local stakeholders simply for pooling purposes, which this paragraph currently implies.

4. **Para 4.5 & 4.6**

Our observation on the paragraphs relating to the role of pension boards is that they are more statements of fact rather than giving any guidance as such. The CPF Committee is supportive of the 'Pool Governance body' considering advice from wider stakeholders, and would prefer some more definite guidance here than as stated 'they can' and 'they may'. However we are not blind to how contentious this issue has become within and across pools with varying opinions likely to be expressed.

5. **Para 4.8 & 4.9**

Our observation of these two paragraphs is similar to 4.5 & 4.6, the statements are factual, but don't draw any conclusions on the role of pool bodies and pool members in asset allocation. We understand the sentiment, but feel that the guidance is sufficiently loose to allow for significant differences in interpretation, which in turn could result in lack of clarity around where responsibilities lie.

Para 5 Transition of assets to the pool

6. **Para 5.5**

We believe there are some asset holdings (in addition to direct property, infrastructure and passive life contracts) that can be more effectively managed by individual pool members. In particular risk management strategies that are bespoke and have limited or no applicability to other pool members. We feel that local member funds should have the opportunity to demonstrate where they feel asset holdings are more effectively outside of a pooled environment.

Provided that member funds are able to demonstrate the value for money and benefit of these holdings they should be granted an exemption until such a time as the Pool Company can demonstrate it can manage the asset as effectively as the pool member. For the avoidance of doubt we feel this should extend beyond direct property, infrastructure and passive life contracts to any asset where superior local management can be demonstrated.

Para 6 Making new investments outside the pool

7. **Para 6.2**

This states that a small proportion of a pool members assets may be invested in local initiatives within the geographical area or in products tailored to particular liabilities specific to that pool member. It then states that local assets would not normally exceed an aggregate of 5% of the value of pool member assets. Generally, we believe stating any limit (albeit appreciating not normally stated) is a step backwards to previous regulation that quoted several limits that have now been removed, and can be explained and justified locally in the ISS. Despite this we are uncomfortable with mixing investments within a geographical area and products tailored to particular liabilities within one definition and limit. The amount of assets for liability hedging is a strategic allocation that would be reviewed subject to the Fund's future cash flows, market opportunities to hedge out interest and inflation risk and funding position, not by ad hoc limit or for a requirement to pool.

Para 6.2 also states that the local assets should be 'subject to a similar risk assessment…' which we agree with, but especially in terms of 'local initiatives within the geographical area' this should cross reference to existing regulations on being able to consider Social Impact providing the policy is explained with a fund's ISS.

For clarity we also note that paragraph 7.3 – infrastructure - mentions investments 'in their own geographic areas'. We assume that if these are not invested through the pool then they will be subject to the 5% 'normal limit' as a local asset.

8. **Para 6.3**

Although we are not against pool members being able to invest in other pools for the reasons stated i.e. collaboration or specialisation we are uncomfortable with the justification for this being simply 'improved net returns'. We would prefer the reason to be 'to deliver the pool members investment strategy which cannot be delivered via their own pool company'. If the wording remains as it is, it has the potential for pool members to be regularly switching from one pool to another in the search for better returns, and ultimately putting at risk achievement of investment and pooling objectives of of themselves, and other pool members, and pool companies.

9. **Para 7.5**

We would be a little uncomfortable with the comment that all residential property is included within the definition of infrastructure. Whilst we understand the reasoning for this inclusion, and believe that a number of residential property investments do fit the definition of infrastructure, there are a number of higher risk, higher returning examples of residential property investments that, in our mind do not fit.

Para 8 Reporting and Para 2 Definitions

The Wales funds, and we understand other funds, have made considerable savings through joint procurement of passive global equity. As explained in your consultation (para 5.5) these are outside your definition of a pooled asset. It does seem a shame that these benefits are not reported in 8.2 to our stakeholders. We also believe that by having a separate category for these 'jointly procured assets' it would help the MHCLG identify those funds holding local assets without reason. The Clwyd Fund invest in a Managed Account which is also a platform which other LGPS funds can join and again fee savings have been achieved by this approach, but we recognize is outside the pooling definition.

Additional Point

One final point we would like to add is that there is no mention of responsible investment. We understand there will be separate guidance being issued from SAB on this but it would still be helpful to consider in due course whether that merits some additional wording to be incorporated in here (perhaps cross referring). In particular the challenge of pool companies meeting the requirements of individual fund RI policies may be worth consideration.

We recognize responsible investment is now becoming a matter of increased interest and focus of our stakeholders. For context the Clwyd Pension Fund has considered within its private markets portfolios (25% of the Clwyd Fund) the level of compliance with Social Development Goals, with an objective to increase current compliance from 30% to 50% over time. However, within private markets this will require niche and relatively small investments for which there will be no fee saving from pooling. We are concerned that without local discretion to invest in these areas our local responsible investment and social impact objectives will be sacrificed which is contrary to the wishes of our stakeholders. This is a further reason for our comments made earlier on paragraph 5 & 6 of the consultation and consider this another reason why assets can continue to be invested locally.

We would welcome further discussion as a Fund or through our participation in the WPP on how we demonstrate value for money to all our stakeholders.

Cllr David Hughes

Chair of Clwyd Pension Fund Committee