

TEESSIDE PENSION FUND

Administered by Middlesbrough Council

AGENDA ITEM 8

TEESSIDE PENSION BOARD REPORT

11 SEPTEMBER 2023

INTERIM DIRECTOR OF FINANCE – DEBBIE MIDDLETON

Pooling Consultation

1. PURPOSE OF THE REPORT

1.1 The purpose of the report is to:

- Advise the Members of the Teesside Pension Board (the Board) of an ongoing government consultation: “Local Government Pension Scheme (England and Wales): Next steps on investments” which sets out a proposed direction of travel in relation to investment pooling on the Local Government Pension Scheme (LGPS).
- Explain the process being followed in relation to the Pension Fund and Border to Coast Pensions Partnership (‘Border to Coast’) responding to the consultation.
- Outline the main points the Pension Fund is likely to make in response to the consultation.

2. RECOMMENDATION

2.1 That the Board notes the content of the consultation document and this report and provides any comments in relation to the Pension Fund’s response to the consultation.

3. FINANCIAL IMPLICATIONS

3.1 There are no financial implications resulting from this report.

4. BACKGROUND

4.1 In 2015 the Government published criteria and guidance on the pooling of LGPS assets. This guidance set out four criteria:

A. Asset pool(s) that achieve the benefits of scale (pools of at least £25 billion)

- B. Strong governance and decision making (for example: appropriate resources, governance structures, reporting, collective policies on how environmental, social and governance issues are taken into account when investing)
 - C. Reduced costs and excellent value for money (reporting on fees, transition costs and savings, appropriate justification for using active management)
 - D. An improved capacity to invest in infrastructure
- 4.2 Once this guidance was published, LGPS administering authorities went through a process which eventually resulted in eight asset pools being set up across England and Wales (Scotland was not covered by the pooling guidance). None of these pools are identical in structure or approach and the level of asset pooling that has actually taken place has varied between pools and between the constituent Pension Funds within those pools.
- 4.3. As the Board will be aware, the Pension Fund was one of twelve (now eleven following a fund merger) founder members of the Border to Coast Pensions Partnership ('Border to Coast'). Border to Coast is acknowledged as one of the most successful of the eight pools, both in terms of the amount of assets that have been pooled and the strong positive relationships that exist between the pool members and with the pool company. Border to Coast and its Partner Funds has also largely delivered the original pooling objectives the government set out in 2015.
- 4.4 The government has issued a new consultation on next steps for LGPS investments in England and Wales which looks to build and accelerate progress towards greater LGPS pooling. The objective is to achieve pools in the £50-75 billion and possible £100 billion range and to do this by initially encouraging / requiring all LGPS funds to complete the pooling process with their current pool and then reducing the number of pools from eight to an unspecified lower number. The full text of the consultation document is enclosed at Appendix A, the consultation can also be found at the following link: [LGPS \(England and Wales\): Next steps on investments](#)
- 4.5 Other aspects, as well as accelerating the pace and scale of pooling are also covered in the consultation which addresses the following five areas:
- "First, the government sets out proposals to accelerate and expand pooling, with administering authorities confirming how they are investing their funds and why. While pooling has delivered substantial benefits so far, we believe that the pace of transition should accelerate to deliver further benefits which include improved net returns, more effective governance, increased savings and access to more asset classes. We propose a deadline for asset transition by March 2025, noting we will consider action if progress is not seen, including making use of existing powers to direct funds. Going forward, we want to see a transition towards fewer pools to maximise benefits of scale.
 - Second, the government proposes to require funds to have a plan to invest up to 5% of assets to support levelling up in the UK, as announced in

the [Levelling Up White Paper \(LUWP\)](#). This consultation sets out in more detail how the Government proposes to implement this requirement and seeks views on its plans.

- Third, the government is proposing an ambition to increase investment into high growth companies via unlisted equity, including venture capital and growth equity. The government believes there are real opportunities in this area for institutional investors with a long-term outlook, such as the LGPS.
- Fourth, the government is seeking views about proposed amendments to the LGPS's regulations to implement requirements on pension funds that use investment consultants. These amendments are needed to implement the requirements of an order made by the Competition and Markets Authority (CMA) in respect of the LGPS.
- Finally, the government is proposing to make a technical change to the definition of investments within LGPS regulations.”

5. CONSULTATION RESPONSE

- 5.1 Border to Coast, together with its Partner Funds, has been working to develop a joint response to the consultation. The is still being drafted at the time of writing this report. Alongside this joint response, which it is expected all Partner Funds will be able to sign up to, each Partner Fund will also be submitting a response to government. These individual responses may emphasise particular aspects or cover areas of special concern to each Fund but are not expected to contradict the general collective approach being developed by all the pool participants. A response from our Fund is being drafted and will be presented to the Pension Fund Committee on 27 September for comments and approval.
- 5.2 Much of what the Government is proposing is in line with the approach to pooling that has already been adopted by Border to Coast and its Partner Funds. For example, on the requirement to pool all listed assets by 31 March 2025, the Fund has to a large degree already achieved this – all the Fund's actively managed equities are invested by Border to Coast (over £2.5 billion as at 30 June 2023) with only the Fund's passive equities managed elsewhere (by State Street Global Advisors – around £0.6 billion as at 30 June 2023).
- 5.3 The following table sets out the questions from the consultation together with some summary comments on collective response that is likely to be given from Border to Coast and its Partner Funds:

Question 1: Do you consider that there are alternative approaches, opportunities or barriers within LGPS administering authorities' or investment pools' structures that should be considered to support the delivery of excellent value for money and outstanding net performance?
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Support the broad thrust of the consultation. No fundamental barriers. Key issue to delivering this is good governance, along with a common vision and culture within the Pool and between Partner Funds

Question 2: Do you agree with the proposal to set a deadline in guidance requiring administering authorities to transition listed assets to their LGPS pool by March 2025?

Support the principle of transferring, or having a clear path to transition, assets to pools. Seek clarity on definitions – particularly on passive investments – these are currently being delivered outside the Pool but at low fee rates negotiated through pooling. Hard to see what savings could be achieved through transferring ownership of these assets. Should still be acceptable to retain up to 5% of assets outside pool if it meets other policy intent (e.g. local investment).

Question 3: Should government revise guidance so as to set out fully how funds and pools should interact, and promote a model of pooling which includes the characteristics described above?

Although Border to Coast and its Partner Funds support the pooling model outlined in the consultation, being overly prescriptive about approaches all Funds must take could stifle innovation.

Question 4: Should guidance include a requirement for administering authorities to have a training policy for pensions committee members and to report against the policy?

Yes, although this should be dealt with through the Government adopting and implementing the recommendations of the LGPS Scheme Advisory Board's [Good Governance Report](#).

Question 5: Do you agree with the proposals regarding reporting? Should there be an additional requirement for funds to report net returns for each asset class against a consistent benchmark, and if so how should this requirement operate?

We support clear, consistent proportionate reporting. However, applying the same benchmark against all Funds is problematic – different Funds will have varying funding levels, liability mixes and risk appetites – all of which will influence the returns they are targeting. Applying a single benchmark could be unhelpful unless these nuances are considered.

Question 6: Do you agree with the proposals for the Scheme Annual Report?

We support clear and consistent reporting.
Highlight concern on cost of additional reporting requirements – any reporting should be focused on simplicity (to aid understanding and support oversight).

Question 7: Do you agree with the proposed definition of levelling up investments?

Agree with proposed definition.
Request 5% of assets can be invested outside pool to support local investments.

Question 8: Do you agree that funds should be able to invest through their own pool in another pool's investment vehicle?

Support in principle but raise several challenges to doing this – some strategies are capacity-constrained (for example Border to Coast's initial Climate Opportunities offering was oversubscribed) so it would not always be possible to accommodate 'external' investors. Also, Border to Coast's propositions are developed by the Partner Funds so may not always suit other investors. There would also be governance and risk issues associated with taking on investors who would be clients but not owners/shareholders like the Partner Funds.

Question 9: Do you agree with the proposed requirements for the levelling up plan to be published by funds?

Support in principle but would highlight the issues that arise when pension fund assets are used to deliver 'additional' benefits not just the best risk-adjusted returns. LGPS assets are invested to deliver appropriate risk adjusted returns and should not be used to implement any Central Government policy objective – no matter how laudable it may be.
Question 10: Do you agree with the proposed reporting requirements on levelling up investments?
Agree with the proposal but note the additional burden imposed by further reporting requirements.
Question 11: Do you agree that funds should have an ambition to invest 10% of their funds into private equity as part of a diversified but ambitious investment portfolio? Are there barriers to investment in growth equity and venture capital for the LGPS which could be removed?
Agree that LGPS Funds should have an appropriately diverse investment approach and this can include private markets investment. The reference to private equity and in particular the emphasis on growth equity / venture capital in the consultation document seems unnecessarily narrow. Private markets investments in general can often include assets that provide the right risk return mix for LGPS Funds and over a timescale that suits long-term investors. It should be noted that private markets investments are typically significantly more expensive (in terms of manager fees), much less liquid and significantly more opaque than listed investments.
Question 12: Do you agree that LGPS should be supported to collaborate with the British Business Bank and to capitalise on the Bank's expertise?
Agree that there are several potential partners that could assist LGPS Funds and Pools, including the British Business Bank and the UK Infrastructure Bank Note the principle of pooling was to remove costs and highlight the risk of using the British Business Bank introducing a new layer of fees.
Question 13: Do you agree with the proposed implementation of the Order through amendments to the 2016 Regulations and guidance?
Yes – this would aid a consistent approach
Question 14: Do you have any comments on the proposed amendment to the definition of investments?
Agree with the proposed amendment (which is technical and uncontroversial)
Question 15: Do you consider that there are any particular groups with protected characteristics who would either benefit or be disadvantaged by any of the proposals? If so please provide relevant data or evidence.
No

5.4 Areas the Fund is likely to emphasise in its own response to the consultation include the following:

- Re-iterating resistance to the Government's continuing attempts to direct Funds as to how to allocate their assets. The 2015 consultation started with a drive to use LGPS Funds to pay for UK infrastructure projects, the latest iteration looks to leverage LGPS assets to help pay for the Government's 'levelling-up' agenda.
- Caution around the drive to invest in private assets – although private market performance has been very good over recent years, past performance is no

guarantee of future outcomes, and with an era of 'cheap money' seemingly coming to an end there is a risk Funds could be directed inappropriately into illiquid investments that may not deliver expected outcomes.

- The consultation blithely suggests the 'deadline' for the transfer of non-listed assets into Funds could easily be 31 March 2025 as well. In fact, there are significant barriers associated with transferring these assets. One in particular the Government could alleviate, this would be to allow the transfer of property assets from a Fund to a Pool without incurring stamp duty.

6 NEXT STEPS

- 6.1 The consultation period ends on 2 October 2023. The expectation is that the Government may either announce the outcome of the consultation or give a strong steer as to its likely announcement in the Autumn Statement (expected to be in November). The Board will be kept up to date with future developments on the guidance and/or regulations relating to LGPS investment pooling.

CONTACT OFFICER: Nick Orton – Head of Pensions Governance and Investments
TEL NO.: 01642 729040