ISLINGTON

Finance Department
7 Newington Barrow Way
London N7 7EP

Report of: **Corporate Director of Resources**

Meeting of:	**Date**	**Agenda item**	**Ward(s)**
Pensions Sub-Committee	5 September 2017		

Delete as appropriate	Exempt	Non-exempt

SUBJECT: The London CIV Update

1. Synopsis

1.1 This is a report informing the committee of the progress made at the London CIV in launching funds and running of portfolios over the period May 2017 to July 2017

2. Recommendation

2.1 To note the progress made to July 2017 .

3. Background

3.1 **Setting up of the London CIV Fund**
Islington is one of 33 London local authorities who have become active participants in the CIV programme. The CIV has been constructed as a FCA regulated UK Authorised Contractual Scheme (ACS). The ACS is composed of two parts: the Operator and the Fund.

3.2 A limited liability company (London LGPS CIV Ltd) has been established, with each participating borough holding a nominal £1 share. The company is based in London Councils' building in Southwark Street. A branding exercise has taken place and the decision was taken to brand the company as 'London CIV.' The London CIV received its ACS authorisation in November 2015.

3.3 **Launching of the CIV**
It was noted that a pragmatic starting point was to analyse which Investment Managers (IM) boroughs were currently invested through, to look for commonality (i.e. more than one borough invested with the same IM in a largely similar mandate), and to discuss with boroughs and IMs which of these 'common'

mandates would be most appropriate to transition to the ACS fund for launch. Each mandate would become a separate, ring-fenced, sub-fund within the overall ACS fund. Boroughs would be able to move from one sub-fund to another relatively easily, but ring-fencing would prevent cross contamination between sub-funds.

3.3.1 Further discussions have been held with managers, focussing specifically on what would be achievable for launch, taking into account timing and transition complexities. Four managers have now been identified as offering potential opportunities for the launch of the CIV. These managers would provide the CIV with 9 sub-funds, covering just over £6bn of Borough assets and providing early opportunity to 20 boroughs. The sub-funds will consist of 6 'passive' equity sub-funds covering £4.2bn of assets, 2 Active Global Equity mandates covering £1.6bn and 1 Diversified Growth (or multi-asset) Fund covering just over £300m. Those boroughs that do not have an exact match across for launch are able to invest in these sub-funds from the outset at the reduced AMC rate that the CIV has negotiated with managers.

3.4 The Phase 1 launch was with Allianz our global equity manager and Ealing and Wandsworth are the 2 other boroughs who hold a similar mandate. The benefits of transfer include a reduction in basic fees and possible tax benefits because of the vehicle used. Members agreed to transfer our Allianz portfolio in Phase 1 launch that went ahead on 2 December.

3.5 **Update to May 2017**

3.5.1 **i) Government Pooling Update** – Following the approval for the London CIV, like other pools, the CIV has been asked to submit a semi-annual progress update on pooling and this was submitted to DCLG on Friday 21st April with a copy of the response sent to all Funds. It is copied here in Appendix 4 along with the DCLG request for information.

ii) Stewardship – Following agreement by the PSJC and Board of LCIV, the Compliance Statement for the Stewardship Code was submitted to the FRC for consideration and has now been approved as a Tier One for Asset Owners. A copy of the Statement can be found here: https://www.frc.org.uk/FRC-Documents/Corporate-Governance/Stewardship-Code/London-CIV.pdf

3.6. **Update to July 2017**

i. **IAC Membership** – The membership of the Investment Advisory Committee is reviewed on annual basis with SLT members asked for nominations either for themselves or for their pension managers. This year's request for membership nominations has again received a very strong response and we are pleased to report that all nominations have been accepted. Whilst this has lead to an increase in size for the IAC, it is recognised that not all members are able to attend every meeting. In total 28 nominations were received representing 29 LLA's

ii. **Sub-funds available within the London CIV** – Current funds available –

a. 3 global equity funds:

b. LCIV Global Equity Alpha (management delegated to Allianz)
c. LCIV Global Alpha Growth (management delegated to Baillie Gifford)
d. LCIV NW Global Equity (management delegated to Newton)
e. 1 UK equity:
f. LCIV MJ UK Equity (management delegated to Majedie)
4 multi-asset/total return funds:
g. LCIV BG DGF (direct investment into the Baillie Gifford Diversified Growth Fund)
h. LCIV NWT RR (direct investment into Newton Real Return Fund)
i. LCIV PY TR (direct investment into Pyrford Real Return Fund)
j. LCIV RF AR (direct investment into Ruffer Absolute Return Fund)

iii. **Sub-Fund Launches July to September** – Over the next 3 months, a further 4 sub-funds are scheduled for launch on the CIV platform, 1 under the CQC (Commonality, Quantum and Conviction) mechanism and a further 3 that have come from the global equity procurement process.

a. The sub-fund launch under the CQC basis:
   Longview Global Equity (17-07-17) – now launched
b. Additional global equity sub-fund launches following global equity procurement, one in July and two in September:
   Henderson Emerging Markets (17-07-17)
   Epoch Global Equity Income (09/17)
   RBC Sustainable Equity (09/17)

iv. **Sub-Fund Capacity** – The IAC reviewed the capacity constraints within LCIV sub-funds at its meeting in June and agreed a communication to be issued to London Funds highlighting which of LCIV sub-funds were "limited capacity" sub-funds.

v. **Equity Strategies** – A global equity information day was held on 11th May (invitations were sent to Pensions Sectoral Joint Committee (PSJC) Members, Treasurers and Pension Managers). This provided Funds the opportunity to meet with Longview, Henderson, Epoch and RBC. Due to the timing of the general election, there was a limited presence from elected Members, but over 30 attendees were present. The feedback to the format of the day and also the presentations themselves was overall very positive. Attendees were also asked to indicate what additional equity strategies they would be interested in and this would then help inform future sub-fund launches. From the feedback on the day, the indications were that demand was highest for low volatility, core and low carbon funds. LLAs will be approached with a global equity survey to gauge demand for additional equity investment strategies.

vi. **Fixed Income and Cashflow Strategies** – This has been the prime focus for LCIV and the IAC over the last quarter, with regular meetings of the fixed income working group taking place to review a range of approaches. Following a review of Pension Fund's investment requirements and a survey of treasurers and officers, it is clear that there is strong demand for products in this area including private debt, multi-asset income, multi-asset credit, buy & maintain and corporate bonds. LCIV are currently undertaking a tender process for an adviser prior to commencing a full search for managers in key fixed income products. The timetable for launching funds in this area is being progressed and it is anticipated that sub-funds will be launched in advance of the business plan date of March 2018. LCIV and the fixed income working group are currently working to a timeline of sub-fund launches towards the end of the calendar year 2017 or early 2018.

vii. **LLA Changing Asset Allocation and Investment Strategies** – LCIV has been reviewing the LLA Investment Strategy Statements and holding meetings with the LLAs to better understand their future strategic asset allocation requirements. This shows that there is about a 6% (or about £1.8bn) move out of equity or growth type mandates into fixed income and cashflow generating asset classes. In addition LLAs are also looking to build exposure in infrastructure and property assets. This will be taken into account by LCIV as it considers its business plans for future years. As noted earlier the shift in LLA requirements means that LCIV is targeting an earlier launch date for fixed income products where feasible to do so.

viii. **Passive Funds and Fee Charges** – This is by way of a reminder to Funds that it was agreed where the CIV had negotiated London wide fee reductions on passive life funds then a charge could be applied from 1st April 2017 charged annually and based on monthly AUMs at a rate

0.005% on AUM.

ix. **London CIV Budget and Medium Term Financial Strategy** – Regular reporting on progress against the budget and targets in the Medium Term Financial Strategy is being provided to the PSJC and a copy of the report that went to the July meeting can be found here: http://www.londoncouncils.gov.uk/node/32109

x. **Recruitment** – LCIV has been actively recruiting over the last few months with a Corporate Development Director (1 year fixed term) Head of Fixed Income & Alternatives, Chief Risk Officer, Fund Accountant and Client Relations Executive having been appointed. Further recruitment is underway focusing on a Head of Global Equities and Investment Analyst. Vacancies will be placed on LCIV website and will be open to colleagues from local authorities to apply where they have the requisite skills to fulfil the roles. In addition, LCIV has also appointed two additional non-executive directors with extensive investment experience to the Board: Linda Selman (Hymans, Baillie Gifford and Scottish Provident) and Paul Niven (BMO, ISIS and RSA).

xi. **MiFID II** – The long awaited announcement from the FRC finally arrived and in line with expectations included provisions which made it easier for LA Pension Funds to opt up to professional status by recognising the collective nature of decision making in LA Pension Funds with the Committee Structures and also acknowledging the role of advisers. All local authority pension funds will need to opt-up to professional status by 3rd January 2018 to avoid being classified as retail clients leading to significant restrictions in what fund managers are able to provide to authorities by way of investment products. The LGA are working closely with the Investment Association (IA) to agree a template for all fund managers to use for Local Authority Pension Funds, which should help ease the opt-up process. LCIV are running a briefing session on the 27th July to cover both MiFID II and the Code of Transparency. In addition the LGA are running a MiFID II briefing in August. Funds should consider taking action over the coming months to opt up in order to retain professional status, rather than leaving it until towards the end of the year. LCIV will also need to receive confirmation from Funds on their ability to meet the new FCA opt-up criteria.

xii. **Stewardship** – Following the end of the year, LCIV collated a voting and engagement report from the underlying managers on LCIV platform, this was distributed to investors in the relevant sub-funds. LCIV officers have also been engaging with the Cross Pools Responsible Investment Group and the LGA on draft guidance for Administering Authorities which is due to be consulted on by the Scheme Advisory Board. The officer Stewardship Working Group will also be considering the statements issued by Pension Funds in their Investment Strategy Statements in relation to ESG, Voting and Stewardship to assess whether further work is required by LCIV to assist Funds in meeting their stewardship responsibilities.

xiii. **Governance Review of the CIV** – Colleagues will recall that it has been agreed that a governance review be carried out to look at structures and decision making for LCIV. The project Steering Committee comprises**:**

- Mark Boleat (Chair) (PSJC Chair)
- Lord Kerslake (Vice Chair)
- Eric Mackay (LCIV NED)
- Cllrs Johnson and Heaster (PSJC Party Group Chairs)
- Ian Williams and Gerald Almeroth (SLT representatives)

Pre-market engagement has taken place with 3 advisers and the ITT issued, one of whom has withdrawn. For information the final specification is attached at Appendix 6, as are the Terms

of Reference for the Steering Committee.

-

3.7 **CIV Financial Implications- Implementation and running cost**

A total of 75,000 was contributed by, each London Borough, including Islington, towards the setting up and receiving FCA authorisation to operate between 2013 to 2015. All participating boroughs also agreed to pay £150,000 to the London CIV to subscribe for 150,000 non-voting redeemable shares of £1 each as the capital of the Company . After the legal formation of the London CIV in October 2015 , there is an agreed annual £25,000 running cost invoice for each financial year ..

The transfer of our Allianz managed equities to the CIV in December 2015 was achieved at a transfer cost of £7,241.

All sub-funds investors pay a management fee of .050% of AUM to the London CIV in addition to managers' fees.

In April 2017 a service charge of 50k (+VAT) development funding was invoiced and a balance of £25k will be raised in December once the Joint Committee has reviewed the in-year budget.

Members agreed to the 0.005% of AUM option for charging fees on the LGIM passive funds that are held outside of the CIV and agreed that (depending on the outcome of discussions) the same will be applied to BlackRock passive funds.

The Newton transition cost the council 32k.

4. Implications

4.1 **Financial implications:**

4.1.1 Fund management and administration fees are charged directly to the pension fund.

4.2 **Legal Implications:**

4.2.1 The Council, as the administering authority for the pension fund may appoint investment managers to manage and invest an equity portfolio on its behalf (Regulation 8(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as amended).

4.2.2 The Council is able to invest fund money in a London CIV fund asset without undertaking a competitive procurement exercise because of the exemption for public contracts between entities in the public sector (regulation 12 of the Public Contracts Regulations 2015). The conditions for the application of this exemption are satisfied as the London authorities exercise control over the CIV similar to that exercised over their own departments and CIV carries out the essential part of its activities (over 80%) with the controlling London boroughs.

.

4.3 **Environmental Implications:**

4.3.1 None specific to this report

4.4 **Resident Impact Assessment:**

4.4.1 The Council must, in carrying out its functions, have due regard to the need to eliminate unlawful discrimination and harassment and to promote equality of opportunity in relation to disability, race and gender and the need to take steps to take account of disabilities, even where that involves treating the disabled more favourably than others (section 49A Disability Discrimination Act 1995; section 71 Race Relations Act 1976; section 76A Sex Discrimination Act 1975."

An equalities impact assessment has not been conducted because this report is updating members on the implementation of a fund structure by external managers. There are therefore no specific equality implications arising from this report.

5. Conclusion and reasons for recommendations

5.1 The Council is a shareholder of the London CIV and has agreed in principle to pool assets when it is in line with its Fund strategy and will be beneficial to fund members and council tax payers. This is a report to allow Members to review progress at the London CIV. Members are asked to note progress made to July 2017.

Background papers:
Final report clearance:

Signed by:

Corporate Director of Resources Date

Received by:

Head of Democratic Services Date

Report Author: Joana Marfoh
Tel: 0207-527-2382
Fax: 0207-527-2056
Email: joana.marfoh@islington.gov.uk