

**CYNGOR SIR POWYS COUNTY COUNCIL**

**Pensions and Investment Committee  
16<sup>th</sup> July 2015**

**REPORT BY:** Strategic Director of Resources

**SUBJECT:** Wales Audit Office ‘ Review of the LGPS Funds in Wales: costs, structure and management’

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**REPORT FOR:** Information

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**1 Introduction**

- 1.1 As Committee may be aware the Wales Audit Office (WAO) and PriceWaterhouseCoopers (PwC) were commissioned earlier this year by the Welsh Government to review the LGPS Funds in Wales. The subsequent report was published in May.

**2 Background**

- 2.1 The LGPS is under intense scrutiny to ensure it remains sustainable for the future, whilst at the same time ensuring that it is both efficiently run and cost effective and clearly accountable to all its members and stakeholders.
- 2.2 DCLG currently has overall responsibility for regulatory oversight of the 89 LGPS Funds in England and Wales. DCLG identified that improvements in managing the investments of the LGPS were likely to generate efficiencies several times (i.e. 6 to 10 times) greater than improvements in member administration. DCLG commissioned research on various options, comparing the use of Collective Investment Vehicles and LGPS Fund mergers. Hymans Robertson reported on these options in March 2014, concluding that CIVs were likely to be somewhat more effective than LGPS Fund mergers in delivering substantial investment cost efficiencies. A high level of CIV take up, whether by mandation or encouragement of voluntary participation, was recognised as essential.
- 2.3 Accordingly, DCLG indicated that it does not intend to impose mergers on the 89 LGPS Schemes in England and Wales. Instead, it consulted on “opportunities for collaboration, cost savings and efficiencies” primarily considering the case for CIVs and possible structures for them. However the consultation gave no steer on whether their use would be voluntary or with some mandation imposed on Funds.

- 2.4 This WAO review has included the benefits, risks and issues of using CIVs and of merging the 8 Welsh LGPS Funds from an investment perspective. They also considered certain funding, administration, governance and operational issues. Throughout the review the WAO has been cognisant of the possibilities for the reorganisation of local government in Wales and of the legal constraints that may be encountered if it were desired to pursue certain options for the LGPS Funds. The WAO have sought to identify areas (regarding LGPS management and structure) in which it might be helpful to seek legal competence for the Welsh Government.

### **3 WAO Conclusions**

- 3.1 There is now a broad consensus that investment scale delivers real investment performance improvements which would tend to reduce deficits. Across Wales, based on £11.8 billion of assets, an improvement in net investment performance of £45 million a year is a reasonable target. Achieving this is financially more important than rearranging administration. New investment arrangements could be established within 2 years.
- 3.2 In Wales, investment scale can be delivered using different options. Scale can be achieved either by merging the 8 existing LGPS Funds or by establishing or using a CIV. Such a CIV could be established for Wales, or the 8 existing LGPS Funds in Wales could participate in CIV(s) for England and Wales if DCLG facilitates such arrangements.
- 3.3 The option of merging to form an intermediate number of LGPS Funds for Wales should be disregarded. A case exists for continuing with the existing eight LGPS Funds; a case exists for merging them all to form a single LGPS Fund for Wales. But there is no case predicated on efficiency for an intermediate number of Funds.
- 3.4 A high level of participation is vital if a CIV is to deliver the £45 million annual performance improvement envisaged. This requires either mandation or a high level of voluntary participation to achieve investment scale. In the absence of a sufficient level of CIV participation only merger into a single Fund will deliver the expected improvement in investment performance. Lower levels of participation would generate lesser savings.
- 3.5 There is a legal issue associated with mandation to use a CIV. In essence, there is a European Directive that can be interpreted as prohibiting government from directing authorities on investment decisions (including participation in a CIV). Some legal opinions would, however, indicate a more flexible interpretation.
- 3.6 There is also a legal issue associated with merging LGPS Funds. In essence, merger would require either DCLG sponsored legislation in Westminster or the transfer of legal competence in this area to the Welsh Government.

- 3.7 One sequence of events might be to establish a CIV for Wales, with voluntary participation. This may be sufficient to achieve the scale envisaged if participation was at or close to 100%. In the event that participation was lower, mandation (of CIV use) could be sought or merger (of LGPS Funds) actioned, subject in each case to resolving the relevant legal issues.
- 3.8 Reorganisation of the LGPS in Wales can be pursued before, at the same time as, or after reorganisation of the Unitary Authorities. They are substantially independent decisions.
- 3.9 The key impact of reorganising the Unitary Authorities is to amalgamate current funding positions created over a long period of time in the sense that each new Unitary Authority would inherit both the assets and liabilities of the relevant predecessor Unitary Authorities. A process of averaging would take place. In most, but not all scenarios researched, the averaging has a modest impact.
- 3.10 Mergers between LGPS Funds would not have this type of averaging impact. The assets and liabilities of each Unitary Authority would carry over into a single LGPS Fund for Wales, and they could continue to be separately identified and measured to derive a funding level for each Unitary Authority. A coherent single actuarial approach would however be expected if there were to be a single LGPS Fund. The definition of the approach would require care, not least to maintain acceptable contribution stability between the results of the 2016 and 2019 actuarial valuations (assuming the merger was concluded by 2019/2020).

#### **4 WAO Recommendations to Welsh Government**

- 4.1 It is recommended that (subject to DCLG's forthcoming response to the consultation, which may result in optional or mandatory participation in CIV(s) that might be established across England and Wales) the Welsh Government supports the establishment of a CIV for all eight funds in Wales.
- 4.2 A CIV could be established over the next two years, in advance of local government reorganisation. Following reorganisation, participation in the CIV should be reviewed. If participation is not at an optimal level to secure the maximum investment returns then the Welsh Government should then consider merging the existing eight funds into a single LGPS fund for Wales.

#### **5 Recommendations**

- 5.1 Committee is asked to note the contents of this report.

<b>Recommendation:</b>		<b>Reason for Recommendation:</b>	
<ul style="list-style-type: none"> <li>To note the contents of the report.</li> </ul>		As per report	
<b>Person(s) To Action Decision:</b>			
<b>Date By When Decision To Be Actioned:</b>			
<b>Relevant Policy (ies):</b>	N/A		
<b>Within Policy:</b>	N/A	<b>Within Budget:</b>	N/A
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<b>Relevant Local Member(s):</b>	