

## **Borders to Coast Pension Partnership Limited: Legal Opinion**

### **1. Background**

In our capacity as legal advisers to the participant funds in the pooling arrangement known as Borders to Coast Pensions Partnership (the “**BCPP Pool**”), we have been asked to provide a legal opinion to each of the administering Authorities who have agreed to participate in that arrangement to support that participation (the “**Authorities**”).

We have reviewed and commented, on behalf of the Funds, on the following documentation:

- a summary of the governance arrangements prepared by Eversheds;
- a draft Shareholders' Agreement to be entered into by each of the participating funds in their capacities as Administering Authorities of those funds and Borders to Coast Pensions Partnership Limited (“**BCPP Limited**”);
- a draft Inter-Authority Agreement (“**IAA**”) between the Authorities; and
- a draft set of Articles of Association for BCPP Limited.

We have also seen copies of three advice notes dealing with the following subjects:

- Eversheds' advice on the basis of LGPS participation and liability in case of default dated 20 December 2016;
- Eversheds' advice on Regulatory Capital dated 12 January 2017, and
- Deloitte's draft advice Regulatory Capital dated 23 December 2016.

### **2. Compliance with relevant legislation: Corporate Structure**

The participation in the BCPP Pool involves the subscription for separate classes of shares in BCPP Limited on an equal basis by each of the Authorities.<sup>1</sup>

The creation of two classes of shares, one of which will be voting (“**A Shares**”) and one non-voting (“**B Shares**”), enables simplification of the treatment of voting and regulatory capital which is necessary for the purposes of BCPP Limited gaining appropriate authorisation from the

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<sup>1</sup> South Yorkshire Pensions Authority will be acting on its own behalf and that of the Sheffield City Region Combined Authority, which is the administering authority for the South Yorkshire Passenger Transport Pension Fund (the “**SYPTPF**”) which, it has been decided for economic reasons, will not become a shareholder in its own right.

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Financial Conduct Authority (the “**FCA**”) in order to conduct its business i.e. as an alternative investment fund manager.

In subscribing for the shares in BCPP Limited, each of the Authorities will be using their statutory powers under the Localism Act 2011 (in particular Sections 1 and 4(2)), respectively the general power of competence and the requirement on local authorities to use a company where it does something for a commercial purpose).<sup>2</sup> The other relevant statutory powers are contained in the Local Government Pension Scheme Regulations 2013 which designate (in schedule 3) the Authorities which are required to maintain and administer pension funds.

Because the purpose of participation in the BCPP Pool is to enable the Authorities to discharge their statutory investment powers (in respect of pooling of investments) by their pension funds, it is appropriate for both the voting A shares and the regulatory capital represented by B Shares to be held as investments of the Pension Funds.

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (“2016 Regulations”) effectively ring-fence Pension Fund money from other assets of the Authorities under Regulation 4. This applies of course to benefit payments, which must be paid from the Pension Fund (Regulation 4(4)), but also to all income and capital gains arising in respect of investments held by the fund (Regulation 4(1) (c) and (d). Regulation 4(5) goes on to state that “any costs, charges and expenses incurred [in] administering a pension fund may be paid from it”, except for costs relating to pension sharing orders (ie relating to divorce cases). From a legal perspective we see no reason why the costs of investing in (including the future operation of) BCPP Limited cannot be charged to the Pension Fund, in the same way as other investment expenses, since these are incidental to the investment made.<sup>3</sup>

By investing in BCPP Limited and consequently the BCPP Pool, the Authorities will be complying with their other obligations under the 2016 Regulations.). Since the repeal of the previous regulations (the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009), there are no quantitative limits on the way in which each administering authority must invest its pension fund, other than a prohibition on investing more than 5% of the total value of that fund in entities which are connected with the relevant authority within the meaning of Section 212 of the Local Government and Public Involvement in Health

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<sup>2</sup> As far as the SYTPF is concerned, the relevant references are to the Transport Act 1968, Sections 10A and 10B(6).

<sup>3</sup> This is a legal, not an accounting, interpretation of Regulation 4. Please see Schedule 1 re the scope of our advice.

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Act 2007 or more generally by reference to the restriction on employment related investments under section 40 of the Pensions Act 1995. As explained in Eversheds' note on Regulatory Capital, those tests will only apply to the Authority in whose pension fund BCPP Limited participates as an employer. Those restrictions will not be breached on mathematical grounds by that Authority (one twelfth of the regulatory capital requirement of EUR10 million being significantly less than the value of any of the Authorities' pension fund assets).

Separately, there are obligations on each of the Authorities to formulate an investment strategy in accordance with Regulation 7 (the "**Investment Strategy Statement**") and to comply with any directions by the Secretary of State under Regulation 8. Each Authority's Investment Strategy Statement therefore must confirm that its participation in the BCPP Pool will discharge the statutory obligation under Regulation 7(2)(d), (i.e. to state the Authority's approach to pooling of investments, including the use of collective investment vehicles and shared services).

A further consequence of the corporate structure which is required for FCA purposes is that, because each of the Authorities will have a controlling influence over BCPP Limited, it will be a "controlled company" for the purposes of the Local Authorities (Companies) Order 1995. This (and the disclosure obligations flowing from that status) are reflected in the Shareholders' Agreement.

### 3. **Fiduciary duties of the Authorities**

DCLG's consultation paper on the 2016 Regulations (in their draft form) made it clear that the Government accepted that Administering Authorities, when exercising their statutory investment powers, did so under a fiduciary duty (to members and employers). There is nothing in the pooling arrangement that would conflict with that duty.

### 4. **Procurement compliance**

BCPP Limited is to be established as a company which is compliant with Regulation 12 of the Public Contracts Regulations 2015 (the ("**Regulations**")<sup>4</sup>. This allows the Authorities to enter into contracts with BCPP Limited without observing the standard requirements of the Regulations, including most importantly the requirement for an open and competitive tender. This exception applies because: (i) each of the Authorities will exercise control over BCPP

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<sup>4</sup> The test is commonly referred to by reference to the leading case in this area, Teckal Srl v Comune de Viano and Azienda Gas-Acqua Consorziale di Reggio-Emilia [1999], whose principles have now been codified into Regulation 12.

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Limited jointly: (ii) its activities will be carried out solely in the performance of tasks entrusted to it by the Authorities; and (iii) there will be no private capital participation in BCPP Limited.

The essential element of joint control is evidenced through the list of reserved matters which is set out in Part A of Schedule 1 to the Shareholders' Agreement. In addition, the Shareholders' Agreement specifies that the business of BCPP Limited will be to act as an alternative investment fund manager for the Shareholders (clause 2), and there will be no private investment in the company. We are accordingly satisfied that the engagement of BCPP Limited by each of the Authorities will not require the procurement of those services to be provided by BCPP Limited to be competitively tendered.

It should be noted that compliance with the conditions set out above is an ongoing requirement in order to ensure that the Authorities continue to benefit from the exception in the Regulations. Any future changes to the nature of the Authorities' control over BCPP Limited, the scope of its activities or the entry of any private capital may therefore alter this analysis. For that reason we have drafted into the amendment clause in the Shareholders' Agreement a further protection that no amendment will be permitted that would have the effect of undermining the compliance of BCPP Limited with the Regulations.

### **5. State Aid**

Each of the Authorities will pay BCPP Limited a fee, referred to as the operating charge, which we understand is intended to cover BCPP Limited's operating costs. The method of calculating the operating charge and its likely amount have yet to be determined. From a State aid compliance perspective, on the assumption that the charge represents a commercial charge in consideration for services that BCPP Limited provides to the Authorities, at market value, and thus is a cost that a private investor in a similar position to the Authorities would expect to pay, it will not constitute State aid. In addition, if BCPP Limited will only act for the Authorities and not for any third parties (either public or private) – i.e., it will not be active on the market – any payment it receives from the Authorities is therefore not capable of distorting competition. It therefore would not constitute State aid. Since BCPP Limited will not, we understand, be tendering for business from other LGPS authorities or other investors, we do not consider that it would be active in this way.

### **6. Governance Model: Local Government Law Compliance**

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The Inter-Authority Agreement documents the terms on which each of the Authorities will participate in a joint committee under Sections 101 and 102 of the Local Government Act 1972. The statutory framework under the above sections contains no restrictions which have been breached by the proposals set out in the Inter-Authority Agreement and the terms of reference for the joint committee are therefore in keeping with the requirements of legislation (and with good governance).

### **7. Other statutory compliance**

Both the Shareholders' Agreement and the Inter-Authority Agreement contain requirements on the Authorities and BCPP Limited (under the Shareholders' Agreement) to comply with other legislation which is applicable to local authorities in general terms. That includes the Equality Act 2010, the Freedom of Information Act 2000, the Environmental Information Regulations 2004, anti-bribery legislation and data protection legislation. Schedule 2 of the Inter-Authority Agreement, which sets out the constitution of the Joint Committee, also makes provision for the meetings of the Joint Committee to be open to members of the public unless it is necessary to exclude the public in accordance with Part VA of the Local Government Act 1972.

### **8. Conclusion**

Based on the draft documentation which we have seen, we are satisfied that the proposal to participate in the BCPP Pool and to subscribe for shares in BCPP Limited is in compliance with the statutory obligations which fall upon the Authorities, and there are no obstacles to the structure which has been proposed.

**Squire Patton Boggs (UK) LLP**  
**[20] January 2017**

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### APPENDIX 1: Scope of Advice

- 1 The advice in this report is provided only to the administering authorities participating funds (the “**Authorities**”) in Border to Coast Pension Partnership Limited (“**BCPP**”). It was prepared solely for the purpose of assisting the Authorities in accordance with the scope of our appointment to advise them on participating in BCPP. It is not advice to any other connected or stakeholder parties, auditors or other advisers, or other third parties (“**Third Parties**”). No part of this advice may be passed on to Third Parties without our written agreement but, if it is so passed, we accept no responsibility, and will have no liability in contract, tort or otherwise, to those Third Parties in relation to this advice.
- 2 This advice only considers the legal issues in relation to the proposed investment in BCPP by the Authorities. We have reached our conclusions based on an understanding of the law as at the date of this report. Accordingly, it is possible that this report will need to be updated if the law changes. However, we will only do so if we are specifically instructed to do so. We have not considered or advised on the tax efficiency of the matter or its commercial or accounting implications where we understand the Authorities have taken separate advice from Deloitte.
- 3 The documents on which this advice has been based are as set out in paragraph 1 of the report above. In accepting instructions from the Authorities we have not undertaken to review, nor are we responsible for reviewing, all or any elements of any other documentation (unless specifically agreed in writing) which may be relevant to specific Authorities. In particular, it is not within the scope of our appointment to review the constitutional documents of any of the Authorities. Accordingly, we do not accept liability should our advice be based on erroneous assumptions or documents or information with which we have not been provided.