

CYNGOR SIR POWYS COUNTY COUNCIL

Pensions and Investment Committee 29th September 2017

REPORT BY: Strategic Director of Resources

SUBJECT: Markets in Financial Instruments Directive II – Opting Up

REPORT FOR: Decision

1 Introduction

- 1.1 Under the terms of the Markets in Financial Instruments Directive II (“MIFID II”) on 3rd January 2018 LGPS Funds will be classified as ‘Retail Investors’. This will mean that Aon would be no longer able to provide investment advice to the Pension Fund and that investment managers would be unable to offer the Fund certain types of investment products. In order to avoid this situation, the Financial Conduct Authority (“FCA”) in partnership with the Local Government Association (“LGA”) have devised a process to enable LGPS Funds to ‘opt up’ to professional client status. This process must be completed by 3rd January 2018.

2 Background

- 2.1 MIFID II is the European Union’s second Markets in Financial Instruments Directive. Examples of poor investment decisions and mis-selling by local and public authorities across Europe have resulted in provisions within MIFID II which aim to give greater protection to such authorities by re-classifying them as retail clients from their current Professional client status with effect from 3rd January 2018.
- 2.2 This reclassification will mean that all financial services firms like banks, brokers, advisers and fund managers will have to treat local authorities in the same way they do individuals and small businesses. That includes ensuring that investment products are suitable for the customer’s needs, and that all the risks and features have been fully explained. This increased level of protection will both restrict the firms, assets and vehicles available to the client and also increase the reporting and disclosure requirements paperwork for both the firm and the client, to prove to the regulator that all the necessary steps have been taken, and as evidence in case of alleged mis-selling.
- 2.3 MIFID II does include an option for retail clients to ‘opt up’ provided certain tests are passed which are designed to ensure the client has sufficient knowledge, expertise and experience to understand the additional risks they will be taking as a professional client.

- 2.4 Therefore the Council will need to apply to be opted up to professional status, as it is difficult to see how an LGPS authority could manage an effective investment strategy without doing so. The application to opt up will be assessed by each relevant firm which provides MIFID business (asset management, consultancy etc). The decision to allow opt up will be made on a firm-by-firm basis. Part of the assessment includes an FCA requirement for the applicant to have a legal entity identifier (“LEI”).

3 The Way Forward

- 3.1 On 3rd July, the FCA published its policy statement setting out the final rules for the MIFID II implementation. The policy statement incorporates a lot of the comments that the sector made in response to the original consultation; the rules for opt up for professional status now better recognise how local government works in practice.
- 3.2 The Scheme Advisory Board (“SAB”) and LGA are now working with the Investment Association (“IA”), the British Venture Capital Association (BVCA), the Alternative Investment Managers Association (AIMA), the Association of Real Estate Funds (AREF) and the Chartered Institute of Public Finance and Accountancy (CIPFA) in order to develop standardised opt up processes for use across the sector. The process will include standard letters and a template which will contain a series of questions which the local authority will need to answer should they wish to opt-up.
- 3.3 The Opting up process will entail:
- The local authority informing the firm that they are willing to relinquish their protection rights under MIFID II and wish to be treated as a professional rather than as a retail client.
 - The template to opt up is completed by the authority and included with the application.
 - The application is assessed by the firm and a decision is made.
 - The firm communicates the result of the assessment back to the applicant and if successful, reminds the applicant of the protections that they are foregoing.
- 3.4 Once a local authority has been opted up, they will need to disclose any material change that could affect their status. This could be done via their web-site and Annual Report. Material changes are those that fundamentally change their status i.e. a change in membership of the Committee or officer or advisor; a change in training policy etc.

4 Proposed Next Steps

- 4.1 On approval of this report:

- An LEI registration will be obtained
- Opting up application form (once an agreed standard is available) will be completed and circulated to relevant firms
- Report progress to Committee at the next meeting scheduled for 15th December.

5 Recommendation

- 5.1 Committee is asked to note the contents of this report and to give authorisation for an LEI Registration.
- 5.2 Committee is asked to give authorisation for opting up to professional client status.
- 5.3 Committee is asked to give delegated authority to the Strategic Director of Resources to take all steps necessary in order to achieve professional client status for the Council as an LGPS fund authority, by 3rd January 2018.

Recommendation:		Reason for Recommendation:	
<ul style="list-style-type: none"> • To note the contents of the report. • To authorise an LEI Registration • To authorise opting up to professional client status • To delegate authority to the Strategic Director of Resources to achieve professional client status by 3rd January 2018. 		To enable the Pension Fund's investment strategy to continue to be managed effectively.	
Person(s) To Action Decision:	Pension Fund Manager		
Date By When Decision To Be Actioned:	3 rd January 2018		
Relevant Policy (ies):	N/A		
Within Policy:	N/A	Within Budget:	N/A
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Relevant Portfolio Member(s):	Councillor Aled Davies		
Relevant Local Member(s):	N/A		