SOLAR PV ENERGY SCHEME

Report of the County Treasurer

Please note that the following recommendations are subject to consideration and determination by the Committee before taking effect.

Recommendation: that the Committee notes the report.

1. Introduction

1.1. At its meeting on Wednesday 10th December 2014 the Devon County Council Cabinet endorsed a report by the Energy Policy Task Group set up by the Place Scrutiny Committee and resolved "that the Task Group's Report be welcomed and endorsed and the relevant Cabinet Member and Head of Service be authorised to take action to implement the Task Group's recommendations, as appropriate."

1.2. Two of the Task Group's recommendations made reference to the Pension Fund, as follows:

- *If the use of capital reserves and prudential borrowing continues to be unviable, the existing outline business case prepared by the Environmental Performance Board for the development of solar PV on redundant landfill sites and park & ride facilities, and wind turbines on County Farms, should be presented to the Investment and Pension Fund Committee.*

- *If the use of capital reserves and prudential borrowing continues to be unviable, Devon County Council should enter into a partnership with an expert body in order to produce a business case for investment by the Pension Fund in renewable energy installations across the corporate and schools estate, incorporating community investment.*

1.3. This report considers the issues involved in considering such an investment, and the criteria that would need to be applied.

2. Fiduciary Duty

2.1. Some years ago a member of the Committee, who has now left the Council, asked Pension Fund officers to investigate an investment opportunity in renewable energy schemes. Officers met with the Councillor and the promoter of the investment opportunity and he was asked to provide a more detailed business case. However, that Business case was never produced so the investment did not go ahead. Officers were cautious as the Pension Fund has a fiduciary duty to invest in order to achieve the return required to pay pensions to its members. Investments should be made to fulfil this purpose, and not to realise other benefits, e.g. of a social or environmental nature. For an administering authority to invest in a local project could be considered to be a conflict of interest, if other issues than investment return are perceived to be the motivation.

2.2. A legal opinion on fiduciary duties of administering authorities under the LGPS was published by Nigel Giffin QC in March 2014. The Opinion confirms that "*The administering authority's power of investment must be exercised for investment purposes, and not for any wider purposes. Investment decisions must therefore be directed towards achieving a wide variety of suitable investments, and to what is best for the financial position of the fund (balancing risk and return in the normal way).*"

2.3. However, it goes on to say that "*so long as that remains true, the precise choice of investment may be influenced by wider social, ethical or environmental considerations, so long as that does not risk material financial detriment to the fund. In taking account of any such considerations, the administering authority may not prefer its own particular interests to those of other scheme employers, and should not seek to impose its particular views where those would not be widely shared by scheme employers and members (nor may other scheme employers impose their views upon the administering authority).*"

2.4. The opinion also highlights that the Investment Regulations require the Fund's Statement of Investment Principles (SIP) to state how far social, environmental or ethical considerations are taken into account. The Devon Fund's SIP states that: "*Other than the monies set aside for investment in Ethical Unit Trusts (up to 1% of the Fund), investment will not be made in companies solely because of their good record in social, environmental or ethical issues*".

2.5. The legal opinion suggests that the Fund could invest in a local Solar PV development, without breaching its fiduciary duty, but only if such an investment would not risk financial detriment to the fund. In practice the potential investment would need to be assessed as providing returns at least as good as other options that could be considered. Equally the reference in the legal opinion to the SIP, and the wording of the SIP, make it clear that the Fund could only judge whether it would make such an investment on financial grounds.

3. Investment Strategy

3.1. To comply with the fiduciary requirement, any investment in a solar PV project would have to be made in accordance with the Pension Fund's investment strategy. The investments made by the Fund are governed by its asset allocation policy. An investment in Solar PV would come under the heading of infrastructure, which has a 4% allocation under the current asset allocation policy. The Fund has made a number of recent commitments to infrastructure, some of which have been funded, and some of which are awaiting drawdown. These are summarised in the following table:

Devon Pension Fund Infrastructure Commitments

	Current Value of Investment £m	% of Total Fund	Current Value plus Committed Funds £m	% of Total Fund
Aviva ReALM Infrastructure Fund	0.0		20.0	
Aviva ReALM Ground Rents Fund	0.0		20.0	
First State European Diversified IF	27.7		39.0	
Hermes Infrastructure Fund	25.3		40.5	

UBS International Infrastructure Fund	29.8		31.3	
Total	**82.8**	**2.6%**	**150.8**	**4.7%**

3.2. The table illustrates that once all the committed funds have been drawn down the allocation will exceed the asset allocation target. Before any further allocation to infrastructure was considered the Committee would need to decide whether it wished to increase its target allocation to infrastructure. Such a decision should be made on the basis of a strategic review of the asset class, not on the basis of a specific infrastructure project.

4. Business Case

4.1. Should further investment in infrastructure be warranted, then any investment would need to be based on a sound business case. The Pension Fund does not have the resources or expertise to put together such a business care or to directly organise the installation of solar panels. Therefore it would require a third party (which could be Devon County Council) to put together a full detailed business case for the Pension Fund to consider, and then manage the project if an investment was agreed. This would involve the third party concerned some risk in undertaking the cost of putting together the project with no certainty of finding willing investors.

4.2. The Fund has already made a commitment to the Aviva REaLM Infrastructure Fund, which has made significant investments in Solar PV. Therefore it could be useful to use the Aviva fund as a benchmark against which to assess any business case that came forward. Key issues to consider:

- The Aviva fund is currently seeking investments capable of delivering IRRs (Internal Rate of Return) of between 7-11% pa over the life of the asset, net of all fees and expenses, with the returns also linked to inflation. The link to inflation is an important attribute for the Fund in protecting itself against the impact of inflation on pension liabilities. The level of fees and expenses taken by the third party managing the project would also be an important consideration.

- A long lease length, around 25 years, is crucial to achieving the required returns, given that the normal practice is for the ownership to revert to the owner of the property where the solar panel is installed at the end of the lease.

- The business case would need to demonstrate the ability of those managing the installations to do so efficiently, and to deal with any maintenance issues over the lifetime of the investment. Aviva work in partnership with specialist PV developers.

- A detailed analysis of the risks involved would be required. The Aviva fund is low risk, given that there is no leverage involved and the returns are governed by regulation. This should be true of a local investment, but the business case should detail any additional risks involved.

5. Conclusion

5.1. As yet, there is no firm detailed proposal on the table for the Pension Fund to consider. Only when and if a business case is presented for consideration will a decision be required. However, any business case would need to be considered on its financial merits and according to how it fits in with the Pension Fund's Investment Strategy. The Committee would also need to be sure that such an investment did not cause a conflict of interest. The key issue in considering such an investment is likely to be that the Fund has already over-committed its current infrastructure allocation.

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Electoral Divisions: All
Local Government Act 1972
List of Background Papers - Nil
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