

## PENSIONS PANEL

14 March 2018

<b>Title:</b> Administration and Governance Report	
<b>Report of the Chief Operating Officer</b>	
Public Report	<b>For Information</b>
<b>Wards Affected:</b> None	<b>Key Decision:</b> No
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<b>Accountable Strategic Director:</b> Claire Symonds, Chief Operating Officer	
<b>Recommendations</b>	
<p>The Panel is recommended to note:</p> <ol style="list-style-type: none"><li>i. that the Fund is cash flow positive;</li><li>ii. the Fund's three-year budget for the period 1 April 2018 to 31 March 2021; and</li><li>iii. that interview dates for the actuarial tender will now be in October 2018. If any Member would like to be on the selection panel, please can they advise the Group Manager for Treasury and Pensions.</li></ol>	
<p>The Panel is recommended to agree that the use of the £40m prepayment is split into:</p> <ol style="list-style-type: none"><li>i. £10m retained for Working capital;</li><li>ii. £30m retained for potential investment opportunities that arise from market corrections, through an increase in allocation to Diversified Growth or capital calls from infrastructure;</li><li>iii. delegate authority to the Chief Operating Officer, in consultation with advisors and the Fund's Chair, to invest the £30m as investment opportunities arise within the market; and</li><li>iv. for officers to arrange meetings for Members to meet the four diversified growth managers on the London CIV, with the potential to either increase the allocation to Diversified Growth or to restructure the Fund's current Diversified Growth Fund. The managers on the London CIV includes:<ul style="list-style-type: none"><li>• Newton;</li><li>• Pyrford;</li><li>• Ruffer; and</li><li>• Baillie Gifford.</li></ul></li></ol>	

## **1. Introduction**

1.1 It is best practice for Members to receive regular administration data and governance updates. Administration data includes cash flow, member numbers, governance and consultations. This paper covers three main areas including:

- i. The London Collective Investment Vehicle (LCIV) update;
- ii. Actuary Contract Tender;
- iii. Pension Fund Budget 1 April 2018 to 31 March 2021;
- iv. Cash flow to 31 January 2018; and
- v. Pension Fund Pre-payment Options.

## **2. London Collective Investment Vehicle (LCIV) Update**

2.1 Following the departure of the LCIV Chief Executive, Hugh Grover, the Chief Investment Officer, Julian Pendock has now also stepped down.

### **2.2 LCIV fixed Income and Cashflow Strategies**

Pending the completion of legal and operational due diligence the first (more liquid) Fixed Income products have been appointed., These new funds will include:

- LCIV Global Bonds Fund (run by PIMCO)
- LCIV Liquid Loans Fund (run by Ares)
- LCIV Private Debt Fund (run by Ares)
- LCIV Multi Asset Credit Fund – Long Only (run by CQS)
- LCIV Multi Asset Credit Fund – Long/Short (run by MidOcean)

2.3 In line with new regulatory changes LCIV now requires written soft commitments to funds before they can submit prospectuses to the Financial Conduct Authority. As there are already LLAs with assets in the CQS fund, LCIV are actively working towards launching this fund in March. The other fund launch dates will be contingent on the receipt of soft commitments.

2.4 The managers for the LCIV Multi Asset Credit Fund (Illiquid) will be announced in Q2 2018.

## **3. Actuarial Contract Tender**

3.1 At the September Pension Panel Members delegated authority to officers to commence procurement for an actuary, using the National LGPS Framework. Members agreed, the interview dates will likely be in late November.

3.2 As the Fund will be tendering for an investment manager later this year it is proposed to carry out a joint tender for both the Actuary and Investment Advisor. Draft requirements will be taken, for Member agreement, in June 2018, with interviews and appointments to take place in September 2018. The National LGPS Framework will be used for both tenders.

## **4. Pension Fund Budget 1 April 2018 to 31 March 2021**

4.1 Table 1 provides Members with the Fund's three-year budget to 31 March 2021.

**Table 1: Pension Fund Budget 1 April 2018 to 31 March 2021**

<u>Contributions</u>	<b>2018/19 Budget</b>	<b>2019/20 Budget</b>	<b>2020/21 Budget</b>
<b>Employee Contributions</b>			
Council	4,500	4,000	3,500
Admitted bodies	2,200	2,000	1,800
Scheduled bodies	2,500	2,600	2,700
<b>Employer Contributions</b>			
Council	18,000	16,000	14,000
Admitted bodies	5,000	4,500	4,000
Scheduled bodies	9,000	9,400	9,700
<b>Pension Strain</b>	1,000	1,000	1,000
<b>Transfers In</b>	2,500	2,500	2,500
<b><u>Total Member Income</u></b>	<b>44,700</b>	<b>42,000</b>	<b>39,200</b>
<b><u>Expenditure</u></b>			
<b>Pensions</b>	- 33,000	- 34,500	- 36,000
<b>Lump Sums and Death Grants</b>	- 6,000	- 6,000	- 6,000
<b>Payments to and on account of leavers</b>	- 3,500	- 3,500	- 3,500
<b>Administrative expenses</b>	- 600	- 600	- 600
<b>Total Expenditure on members</b>	<b>- 43,100</b>	<b>- 44,600</b>	<b>- 46,100</b>
<b><u>Net additions for dealings with members</u></b>	<b>1,600</b>	<b>- 2,600</b>	<b>- 6,900</b>
<b><u>Returns on Investments</u></b>			
<b>Investment Income</b>	7,000	7,500	7,500
<b>Profit (losses)</b>	35,000	35,000	35,000
<b>Investment management expenses</b>	- 3,100	- 3,100	- 3,100
<b>Net returns on investments</b>	<b>38,900</b>	<b>39,400</b>	<b>39,400</b>
<b>Net increase (decrease) in the net assets</b>	<b>40,500</b>	<b>36,800</b>	<b>32,500</b>
<b>Opening Market Value</b>	<b>1,000,000</b>	<b>1,040,500</b>	<b>1,077,300</b>
<b>Closing Market Value</b>	<b>1,040,500</b>	<b>1,077,300</b>	<b>1,109,800</b>

4.2 The three-year budget shows a movement from members being employed by the Council to being funded by admitted bodies. The significant movement of staff out of the Council and into the various companies set up by the Council, including Be First, Traded Services, Home Services and Schools Improvement Partnership, will have two main impact on the Fund's cashflow and its structure.

- i. Initially the Council contribution will decrease and the admitted body increase.
- ii. As the admitted bodies close schemes their contributions will decrease.

As a result of these changes in cashflow, the overall member income will decrease in 2019/20 and 2020/21. Given the potential for the Fund to be cashflow negative in 2019/20 a report will be taken to the June Panel outlining options available to cover

4.3 An increase in lump sum payments is projected but it is expected that this will be mitigated by an increase in pension strain. Pension payments are forecast to increase

due to an increase in the number of pensioners as well as to reflect an estimated pension increase of 3.0% for 2018/19.

- 4.4 Overall the Fund is expected to be cashflow negative in 2020/21 if investment income and management expenses are included but return is excluded. Fund manager fees are forecast to drop from £3.5m to £3.0m by 2020.

## 5. Cash flow to 31 December 2017

- 5.1 Table 2 below provides Members with the Fund's Cash flow to 31 December 2017.

**Table 2: 2017/18 Forecast Pension Fund Cash Flow**

	<b>2017/18 Budget £000's</b>	<b>2017/18 Forecast £000's</b>	<b>Over / Under £000's</b>
<b><u>Contributions</u></b>			
<b>Employee Contributions</b>			
Council	6,000	7,003	1,003
Admitted bodies	800	355	(445)
Scheduled bodies	2,400	2,145	(255)
<b>Employer Contributions</b>			
Council	22,500	23,789	1,289
Admitted bodies	2,000	1,167	(833)
Scheduled bodies	8,900	8,155	(745)
<b>Pension Strain</b>	1,000	2,189	1,189
<b>Transfers In</b>	2,500	3,256	756
<b><u>Total Member Income</u></b>	<b>46,100</b>	<b>48,059</b>	<b>1,959</b>
<b><u>Expenditure</u></b>			
Pensions	(30,000)	(31,451)	(1,451)
Lump Sums and Death Grants	(6,000)	(7,716)	(1,716)
Payments to and on account of leavers	(3,500)	(4,629)	(1,129)
Administrative expenses	(550)	(600)	(50)
<b>Total Expenditure on members</b>	<b>(40,050)</b>	<b>(44,396)</b>	<b>(4,346)</b>
<b><u>Net additions for dealings with members</u></b>	<b>6,050</b>	<b>3,663</b>	<b>(2,387)</b>
<b><u>Returns on Investments</u></b>			
Investment Income	6,000	6,000	-
Profit (losses)	35,000	75,000	40,000
Investment management expenses	(3,300)	(3,200)	100
Net returns on investments	37,700	77,800	40,100
<b>Net increase (decrease) in the net assets</b>	<b>43,750</b>	<b>81,463</b>	<b>37,713</b>
<b>Asset Values</b>	<b>960,557</b>	<b>998,270</b>	
<b>Liabilities</b>	<b>(1,100,000)</b>	<b>(1,200,000)</b>	
<b>Funding Level</b>	<b>87.3%</b>	<b>83.2%</b>	

- 5.2 Administration costs are forecast to be £100k higher than budget as an external company will complete the Fund's Guaranteed Minimum Pension reconciliation.
- 5.3 Pension costs are significantly higher than budget due to the full effect year effect of the 2016/17 retirements and an increase in early retirements from the UEL.
- 5.4 Overall the Fund is forecast to end the financial year at around 83.2% funded based on a prudent gilt plus model. This compares favourably with the triennial valuation results where the fund is 77.6% funded and is due to higher than expected returns and a decrease in inflation expectations.

## 6. Pension Fund Prepayment Options

- 6.1 As part of the Council's savings options, it will prepay two years' worth of pension contribution totalling £40m to the Pension Fund on the 3<sup>rd</sup> of April 2018. The prepayment is for its forecast pension contribution for 2018/19 and 2019/20.
- 6.2 Currently the Council already prepays one year of its contributions, with the prepayment of £20m previously being used to cover capital calls from the Fund's infrastructure investment.
- 6.3 The Fund is currently overweight equities, against its strategic allocation. Table 1 below shows the allocation as at 22 February 2018 against the Fund's strategic allocation. Although the equity overweight position is significant, this will be used to fund the Fund's infrastructure investments as required.

**Table 1: Fund Current Allocation**

Asset Type	Current Allocation at 22 February 2018	Strategic Allocation	Difference
Equity	53.9%	48.0%	5.6%
Bonds	3.6%	4.0%	-0.5%
Global Credit	6.8%	8.0%	-1.3%
Infrastructure	6.6%	9.0%	-2.4%
Absolute Return	16.8%	18.0%	-1.3%
Property	6.4%	7.0%	-0.6%
DA	5.9%	6.0%	0.0%
Cash	0.0%	0.0%	0.5%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>0.0%</b>

- 6.4 There is currently an underweight position within Absolute Return strategies of 1.3%, which equates to approximately £13m. There is a similar underweight position in Credit. Both strategies have underperformed over the past few years, with Credit particularly underperforming.
- 6.5 Currently the London CIV have two very good Diversified Growth managers, namely Baillie Gifford and Ruffer. It would be appropriate for Members to meet both these managers to see if they can provide improved returns but within a diversified alternatives strategy to the current underperforming strategies but also with a view to topping up the Fund's underweight position in Diversified Growth.

6.6 One additional consideration for the use of the prepayment is that most asset classes are very highly valued, with the potential for short-term market corrections to occur. These corrections are often oversold, where the values drop significantly before increasing again a few weeks later. During these periods it would be useful for the Fund to be able to increase its allocation, subject to discussion with the Fund's advisors, to take advantage of these investment opportunities.

6.7 It is recommended that the use of the £40m prepayment is split into:

- v. £10m retained for Working capital;
- vi. £30m retained for potential investment opportunities that arise from market corrections, through an increase in allocation to Diversified Growth or capital calls from infrastructure;
- vii. delegate authority to the Chief Operating Officer, in consultation with advisors and the Fund's Chair, to invest the £30m as investment opportunities arise within the market; and
- viii. for officers to arrange meeting with the four diversified growth managers on the London CIV, including:
  - Newton;
  - Pyrford;
  - Ruffer; and
  - Baillie Gifford.

## **7. Consultation**

7.1 Council's Pension Fund governance arrangements involve continuous dialogue and consultation between finance staff and external advisers. The Chief Operating Officer and the Fund's Chair have been informed of the commentary in this report.

## **8. Financial Implications**

*Implications completed by: Claire Symonds, Chief Operating Officer*

8.1 The Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. The management of the administration of benefits and governance of the Fund rests with the Pension Panel.

## **9. Legal Implications**

*Implications completed by: Dr. Paul Feild Senior Governance Solicitor*

9.1 The Council operates the Local Government Pension Scheme which provides death and retirement benefits for all eligible employees of the Council and organisations which have admitted body status. There is a legal duty fiduciary to administer such funds soundly according to best principles balancing return on investment against risk and creating risk to call on the general fund in the event of deficits. With the returns of investments in Government Stock (Gilts) being very low they cannot be the primary investment. Therefore, to ensure an ability to meet the liability to pay beneficiaries the pension fund is actively managed to seek out the best investments. These investments are carried out by fund managers as set out in the report working with the Council's Officers and Members.

## **10. Other Implications**

10.1 There are no other immediate implications arising from this report though the Public Service Pensions Act changes will have an impact on the short and long-term workload of the Pension Fund. This will continue to be monitored.

**Background Papers Used in the Preparation of the Report:** None

**List of appendices:** None