

PENSIONS COMMITTEE

10 June 2020

Title: Administration and Governance Report	
Report of the Chief Operating Officer	
Open Report	For Information
Wards Affected: None	Key Decision: No
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Accountable Director: Philip Gregory, Finance Director	
Accountable Strategic Leadership Director: Claire Symonds, Acting Chief Executive	
Recommendations	
<p>The Committee is recommended to note:</p> <ol style="list-style-type: none">i. that the Fund is cash flow positive,ii. the Fund's three-year budget for the period 1 April 2020 to 31 March 2023,iii. update on the appointment of Hymans Robertson for its Investment Consulting Services and Barnett Waddingham for its Actuarial Services, andiv. Independent Advisors LGPS Update on Scheme Advisory Board Project Good Governance in the LGPS and other significant developments in the LGPS- May 2020	

1. Introduction

1.1 It is best practice for Members to receive regular administration data and governance updates. This report covers four main areas including:

- i. Pension Fund Budget 1 April 2020 to 31 March 2023,
- ii. Cash flow to 31 March 2020,
- iii. Update on Actuarial and Investment Consulting Tender, and
- iv. Independent Advisors LGPS Update on Scheme Advisory Board Project Good Governance in the LGPS and other significant developments in the LGPS- May 2020

2. Pension Fund Budget 1 April 2020 to 31 March 2023

2.1 Table 1 provides Members with the Fund's three-year budget to 31 March 2023.

Table 1: Pension Fund Budget 1 April 2020 to 31 March 2023

<u>Contributions</u>	2020/21 Budget	2021/22 Budget	2022/23 Budget
Opening Market Value	974,493	1,012,293	1,050,243
Employee Contributions			
Council	6,800	6,600	6,400
Admitted bodies	1,000	900	800
Scheduled bodies	1,950	2,000	2,050
Employer Contributions			
Council	21,000	22,000	23,000
Admitted bodies	4,000	3,750	3,500
Scheduled bodies	7,250	7,400	7,500
Pension Strain	1,000	1,000	1,000
Transfers In	2,500	2,500	2,500
<u>Total Member Income</u>	45,500	46,150	46,750
<u>Expenditure</u>			
Pensions	-36,500	-37,500	-38,500
Lump Sums and Death Grants	-7,000	-6,500	-6,500
Transfers Out	-2,500	-2,500	-2,500
Administrative expenses	-700	-700	-700
<u>Total Expenditure on members</u>	-46,700	-47,200	-48,200
<u>Net dealings with members</u>	-1,200	-1,050	-1,450
<u>Returns on Investments</u>			
Investment Income	7,500	7,500	7,500
Profit (losses)	35,000	35,000	35,000
Investment management expenses	-3,500	-3,500	-3,500
Net returns on investments	39,000	39,000	39,000
Net increase (decrease) in assets	37,800	37,950	37,550
Closing Market Value	1,012,293	1,050,243	1,087,793

- 2.2 The three-year budget shows a movement from members being employed by the Council to being funded by admitted bodies as staff move across to the various companies set up by the Council. The forecast is for the Council contribution to increase as the rate increases from 21.0% in 2020/21, 22.0% in 2021/22 and 23.0% in 2022/23. Admitted body contribution will initially increase, but as the admitted bodies are closed to new entries, their contributions will decrease over time. Due to these changes, the overall member income will decrease in 2021/22 and 2022/23.
- 2.3 An increase in death grant payments is projected in 2020/21. Pension payments are forecast to increase due to an increase in the number of pensioners as well as to reflect a pension increase of 1.7% for 2020/21.
- 2.4 Overall the Fund is expected to be cashflow negative for net dealings with members but cashflow positive if investment income and management expenses are included. Officers will be working with the fund managers over the coming year to establish a process to utilise the income from property and infrastructure to fund any cash flow shortfalls.

3. Cash flow to 31 March 2020

- 3.1 Table 2 below provides Members with the Fund's Cash flow to 31 March 2020.

Table 2: Actual Pension Fund Cash Flow to 31 March 2020

	2019/20 Budget £000's	2019/20 Actual £000's	Over / Under £000's
<u>Contributions</u>			
Employee Contributions			
Council	6,200	6,829	629
Admitted bodies	1,000	924	-76
Scheduled bodies	1,900	1,909	9
Employer Contributions			
Council	22,000	24,440	2,440
Admitted bodies	6,900	3,540	-3,360
Scheduled bodies	7,100	7,062	-38
Pension Strain	1,000	738	-262
Transfers In	2,500	4,588	2,088
<u>Total Member Income</u>	48,600	50,030	1,430
<u>Expenditure</u>			
Pensions	-35,000	-34,771	229
Lump Sums and Death Grants	-6,000	-6,512	-512
Payments to and on account of leavers	-2,500	-6,007	-3,507
Administrative expenses	-750	-721	29
<u>Total Expenditure on members</u>	-44,250	-48,011	-3,761
<u>Net additions for dealings with members</u>			
	4,350	2,019	-2,331
<u>Returns on Investments</u>			
Investment Income	7,000	7,000	0
Profit (losses)	35,000	- 60,000	-95,000
Investment management expenses	-3,100	-4,188	-1,088
<u>Net returns on investments</u>	38,900	-57,188	-96,088
<u>Net increase (decrease) in the net assets</u>			
	43,250	-55,169	-98,419
<u>Asset Values</u>			
	1,065,250	974,493	
<u>Liabilities</u>			
	1,347,500	-1,189,704	
<u>Funding Level</u>	79.05%	81.9%	

4. Investment Advisor and Actuary Tender

- 4.1 On 28 January 2020, the Pension Fund tendered for an Actuary and Investment Consultant using the National LGPS Framework for Actuarial and Investment Consultancy Services. A Further Competition was issued as per the framework to assess and evaluate with Actuary and Advisor best meets the Fund's requirement.
- 4.2 A deadline for receipt of proposals was set at 17:00 on 11 February 2020. Officers evaluated and scored each service provider based on specific and targeted technical proposals submitted in providers' application. In addition, specific additional requirements were included as a part of the evaluation criteria.

Evaluation Criteria	Percentage	Basis
Quality Offered	35%	Specific Questions
Service Fit	30%	Presentation + Specific Questions
Value for Money	35%	Model Fund Pricing Portfolio

From this evaluation, two providers from each service were shortlisted for a presentation and interview. Officers and the funds independent advisor interviewed Hymans Robertson and Mercer to provide Investment Consulting Services on Monday 24th February 2020 and Hymans Robertson and Barnett Waddingham to provide Actuarial Services on Wednesday 26th February 2020.

A decision was made to appoint Hymans Robertson for Investment Consulting Services and Barnett Waddingham for its Actuarial Services.

The contract commenced for the Investment Consultant on 1st April 2020 and the start date for the Actuary will be 1st July 2020. Officers are providing information to the Investment Consultants to ensure a smooth transition.

4.3 **Strategy Review**

Upon appointment, Hymans Robertson have been asked to provide a Strategy Review report for Member consideration at the September Pension Committee, using the actuarial assumptions and cashflows provided by the current actuary. The Strategy Review will likely contain several strategy recommendations. Consequently, training on asset allocation and the investment strategy is being provided to Members at today's meeting.

5. **Independent Advisors LGPS Update on Scheme Advisory Board Project Good Governance in the LGPS and other significant developments in the LGPS- May 2020**

5.1 **Introduction**

The purpose of this paper is to update the Pensions Committee on developments relating to two important issues. Firstly, developments relating to the Good Governance in the LGPS project which have occurred since the last update to the Pensions Committee. Secondly, to report on the outcome of a legal case relating to the LGPS in respect of which the Supreme Court delivered its judgement on 29 April 2020

5.2 **Good Governance in the LGPS project**

As reported in detail in previous papers (Pensions Committee 13 March 2019, Item 7, Appendix 1; 12 June 2019 Item 7, Appendix 1; 18 September 2019, Item 6; 11 March 2020, Item 5) the Scheme Advisory Board for England and Wales (SAB) has been developing proposals to significantly enhance governance within the LGPS.

This project – The Good Governance in the LGPS project - is the most important development presently underway in the LGPS as it seeks to fundamentally enhance and strengthen the governance of the individual LGPS Funds across England and Wales (now 85 in total). Completion of the project and its effective implementation across the LGPS in England and Wales is surely the most effective means of maintaining the existing and longstanding local management of the LGPS and avoiding the possibility of compulsory amalgamations of individual Funds going forward.

As previously reported a Phase I report was produced by Hymans Robertson in July 2019 and a Phase II report by Hymans Robertson and two stakeholder Working Groups was considered by the SAB and issued in November 2019. [The Independent Advisor to the Barking and Dagenham Fund was a member of both the Working Groups]. This Phase II report included a broad range of proposals to enhance the governance of the LGPS across

England and Wales. At the meeting of the Scheme Advisory Board held on 3 February 2020 it was agreed that the two working groups who prepared the Phase II report be combined to form an Implementation Group (of which the Independent Advisor to the Barking and Dagenham Fund is a member). It was further agreed that this group prepare a detailed paper for consideration by the Board at its meeting in May 2020 to include proposals for necessary changes to the LGPS Regulations and new Statutory Guidance, the establishment of Key Performance Indicators, and the process for the independent assessment of the governance of the individual LGPS Funds in England and Wales.

The Implementation Group began its work in February 2020. In March an initial draft of the new Statutory Guidance on Governance in the LGPS and draft paper on the role of the LGPS Senior Officer were issued and circulated for comments. The social distancing restrictions introduced by the government in March prevented the group meeting in person. Telephone conferencing discussions were held but attendance was limited due to the fact that local government Officers on the group were engaged in responding to Coronavirus.

Therefore, on 6 April 2020 at a virtual meeting involving the SAB Chair, Vice Chair and Chairs of the Investment and Cost Management Committees it was agreed to stand down the Implementation Group until further notice but that the project team at Hymans Robertson be asked to continue to work on papers for consideration by the Implementation Group once meetings again become viable. This action was approved at the Board meeting of SAB held on 5 May 2020. Consequently, the timetable for the completion of the Good Governance in the LGPS project is on hold pending the resolution of the Coronavirus epidemic.

The MHCLG were represented on both the Phase II Working Groups and are represented on the (Phase III) Implementation Group. Therefore, the proposals of the Good Governance in the LGPS project are likely to be adopted, eventually, by the MHCLG and compliance with them required of all LGPS Funds in England and Wales through the issuing, in due course, of new Statutory Guidance on Governance in the LGPS.

5.3 Supreme Court Case regarding 2016 LGPS Statutory Guidance

In 2016 the Local Government Pension Scheme (Management and Investment of Funds) Regulations were updated. To accompany the new Regulations the Government issued Statutory Guidance to assist Administering Authorities in the LGPS to formulate, publish and maintain their Investment Strategy Statement as required under the new Regulation 7. This was entitled “Guidance on Preparing and Maintaining an Investment Strategy Statement.”

This Statutory Guidance was 10 pages long and provided much clear and helpful guidance to Administering Authorities. The Statutory Guidance did however include two short paragraphs that became the subject of a case taken by the Palestine Solidarity Campaign and an individual member of the LGPS who claimed that the inclusion of two specific paragraphs in that guidance was unlawful and that they should be removed.

This case concerned the breadth of the ethical investments that Administering Authorities of the LGPS (such as Barking and Dagenham) are permitted to make. In the final judgement on the case delivered by the Supreme Court on 29 April 2020 Lord Wilson defined (in paragraph 1) an ethical investment as follows “*By an ethical investment, I mean an investment made not, or not entirely, for commercial reasons but in the belief that social, environmental, political or moral considerations make it, or also make it, appropriate.*”

The two paragraphs that the claimants believed were unlawful are in italics below.

- “*However, the Government has made clear that using pension policies to pursue boycotts, divestment and sanctions against foreign nations and UK defence industries are inappropriate, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government.*”

- An Administering Authority *“Should not pursue policies that are contrary to UK foreign policy or UK defence policy”*

The case was originally heard in the High Court in 2017 which declared the two passages in the Guidance under challenge to be unlawful. This decision was reversed by the Court of Appeal in 2018. Leave was granted for the case to be finally determined by the Supreme Court which heard the case in November 2019 and delivered its Judgement on 29 April 2020.

In their judgement the Supreme Court determined by a majority of 3 to 2 that the two passages in the Guidance under challenge were indeed unlawful as in issuing them the Secretary of State had exceeded his powers. As part of the Judgement (in paragraph 31) Lord Wilson stated *“Power to direct HOW administrators should approach the making of investment decisions by reference to non-financial considerations does not include power to direct (in this case for entirely extraneous reasons) WHAT investments they should not make.”*

On 11 May 2020 the LGPS Scheme Advisory Board for England and Wales posted the following initial statement on its website: *‘The SAB welcomes the clarity brought by the judgement of the Supreme Court in the case of R (on the application of Palestine Solidarity Campaign Ltd and another) Appellants) v Secretary of State for Housing, Communities and Local Government (Respondent). In seeking to restrict the outcome as well as the considerations taken account of by an LGPS administering authority when developing its responsible investment policy, the government has been judged to have overstepped its powers. It is the Board’s view that Responsible Investment policy decisions belong at the local level reflecting: the need to pay pensions both now and in the future; local democratic accountability and the views of scheme members; and that outcomes of policy developments should not be subject to restrictions based on unrelated matters’*

The judgement issued by the Supreme Court is 35 pages long and the statements made by the Judges in this may have implications beyond the issue of the two passages in the Statutory Guidance which were the subject of the case. Therefore, the Scheme Advisory Board has agreed that its Secretariat, in conjunction with the Board’s legal adviser, draft a statement summarising the Judgement for publication on the Board’s website. This will include the direct effect of the decision and possible indirect impacts of the decision. This statement should provide Administering Authorities, including Barking and Dagenham, with greater clarity as to any wider implications and consequences of the judgement.

It can however be said with certainty that the judgement does not undermine the overriding duty of the Administering Authority, in the words of the 2016 Statutory Guidance on Preparing and Maintaining an Investment Strategy Statement, that *“...schemes should make the pursuit of a financial return their predominant concern...”* This element of the Statutory Guidance was not disputed in this case.

6. Consultation

- 6.1 Council’s Pension Fund governance arrangements involve continuous dialogue and consultation between finance staff and external advisers. The Finance Director and the Fund’s Chair have been informed of the commentary in this report.

7. Financial Implications

Implications completed by: Philip Gregory, Finance Director

- 7.1 The Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. The management of the administration of benefits the Fund is supported and monitored by the Pension Board.

8. Legal Implications

Implications completed by: Dr. Paul Feild Senior Governance Solicitor

- 8.1 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.
- 8.2 This report refers to the recent Supreme Court decision in R (on the application of Palestine Solidarity Campaign Ltd and another) (Appellants) v Secretary of State for Housing, Communities and Local Government (Respondent). Its implications are considered.
- 8.3 It related to a judicial review of Guidance issued by the Secretary of State on preparing and maintaining an Investment Strategy Statement. The Guidance was issued pursuant to regulation 7(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (SI 2016/946) ("the 2016 Regulations"), and to take effect when the regulations did so, on 1 November 2016. The Guidance was entitled: "Local Government Pension Scheme: Guidance on Preparing and Maintaining an Investment Strategy Statement".
- 8.4 The guidance contained new stipulations designed to prohibit LGPS funds from pursuing boycotts, divestment and sanctions against foreign nations and UK defence industries. This guidance was challenged on the basis that the Secretary of State had exceeded his authority in that the power to issue guidance was limited to the purpose of the legislation creating the power. The challenge was successful in the High Court and so the Secretary of State appealed to the Court of Appeal where he won as the Court reversed the High Court's decision. A further appeal was then entered to the Supreme Court (the replacement to the House of Lords and the highest court in the land). Here the objectors to the Guidance were successful by a majority 3 to 2 judges who held that the guidance extended to matters outside the Secretary of States authority to give guidance. It was determined that the position was that the Secretary of State sought to promote the government's own wider political approach, by insisting that, in two particular contexts related to foreign affairs and to defence, administering authorities could not refrain from making particular investments on non-financial grounds, regardless of the views held by the scheme members. The flaw according to the majority was that the position was that judgements about non-financial considerations in investment decisions were for administering authorities not the Secretary of State to take. Administering authorities may take non-financial considerations into account provided that in doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision.
- 8.5 In terms of direct implications, the guidance will need to be changed or at least amended. However, for practical purposes it has no specific impact for Barking and Dagenham as the administering authority has no stated intentions with regards to foreign policy or UK defence and within its investment strategy.

9. Other Implications

- 9.1 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