worcestershire countycouncil

Pensions Committee
Wednesday, 28 November 2018, County Hall, Worcester - 10.00 am

Minutes

Present:

Mr R W Banks (Chairman), Mr A I Hardman, Dr A J Hopkins, Mr R C Lunn and Mr P A Tuthill

Co-opted Member (voting) – Mr V Allison (Employer representative)

Available papers

The members had before them:

A. The Agenda papers (previously circulated); and

B. The Minutes of the meeting held on 5 October 2018 (previously circulated).

143 Named Substitutes (Agenda item 1)

Dr A J Hopkins for Mr P Middlebrough.

144 Apologies/ Declarations of Interest (Agenda item 2)

Apologies were received from Mr A Becker Mr P Middlebrough and Mr R J Phillips.

Mr V Allison declared an interest as a member of the Pension Fund.

145 Public Participation (Agenda item 3)

None.

146 Confirmation of Minutes (Agenda item 4)

RESOLVED that the Minutes of the meeting held on 5 October 2018 be confirmed as a correct record and signed by the Chairman.

147 Equity Protection (Agenda item 5)

The Committee received an update presentation from Jason Wood and Mark Davies of River and Mercantile on the Equity Protection Strategy.

In the ensuing debate, the following points were made:

- Jason Wood indicated that as the Equity Protection Strategy was half way through the contract period, it was an appropriate stage to consider how it was progressing. Although no

action was recommended at this stage, the Committee might wish to amend the Strategy prior to its date of maturity

- Philip Hebson commented that at some point a decision would need to made about the future approach to equity protection and whether it would be appropriate to enter the active equity market
- In response to a query, Mark Davies suggested that in the event of a major market fall, the strong funding position of the Fund could provide an opportunity for re-investment in equities market
- Philip Hebson explained that although there had been a recent fall in markets, they had only fallen to a level slightly below the original starting point. Mark Davies added that most pension funds would be concerned about a fall in markets. Even if the market rallied, there would remain concerns and the asymmetry factor (in other words as the performance neared the cap, the risk/return balance was out of kilter) became more important because of the exposure to market forces at that point
- Mark Davies explained that there remained enough upside and reasonable protection within the strategy so that no action was needed at present. The staff at River and Mercantile monitored the performance of the Strategy on a daily basis, taking into account the asymmetry factor, the market factor and the replacement strategy factor. The Fund would only be contacted when it was considered that a restructuring of the contract could be beneficial
- What would be the cost to the Fund of withdrawing from the contract with River and Mercantile before the date of maturity? Jason Wood explained that there would be a market trading cost of around 5 – 15 basis points. This was a market charge not a fee to the company
- Michael Hudson commented that the Committee needed to weigh up the benefits of adopting equity protection against the Fund's appetite for risk as it entered the next phase after the maturity date for this Strategy. The date of maturity for this particular Strategy had been planned to coincide with the forthcoming Triennial Valuation. Mark Davies emphasised that the equity protection product could be tailored to meet the needs of the Investment Strategy of the Fund
- In response to a query, Michael Hudson indicated that this Fund was one of only two funds in LGPS

Central who had taken out some form of equity protection. The key issue for the Fund to determine going forward was whether it wanted long or short term protection. If the Committee deemed that some form of equity protection was necessary, a decision would need to be made as to the form of equity protection tool required and whether the existing tool should be reviewed. Mark Davies added that the strategy needed to focus on protection of funding levels rather than market performance

- In response to a query, Michael Hudson explained that the Fund's actuary would base their view on the performance of the Fund with particular reference to the approach taken to equity protection. Philip Hebson added that at a recent presentation by Mercers, the Fund's actuary, reference was made to the adoption of either a single option strategy or a dynamic strategy. The Fund had adopted a single option strategy with a time line leading up to the Triennial Valuation. The question would be whether to move to a more dynamic strategy. Some dynamic strategies required officers to take active market decisions on a monthly basis thereby effectively operating an active management role which he considered to be too complex
- The Equity Protection Strategy was a means of minimising actuarial risk. However if the markets performed well then the Fund could be missing out on large amounts of upside. There was a view that global growth would continue and the Fund should be cautious of making short-term decisions. It would be appropriate to review the performance of the Strategy in February/March 2019
- The Equity Protection Strategy had been adopted for the right reasons however it was not indefinite and any future decision should take into account the impact of inflation
- Philip Hebson explained that it was possible to pay for an insurance premium to allow the Fund to keep the upside but that would be at a significant cost
- The Fund was approximately 95% funded therefore it would seem beneficial to continue with a strategy that maintained a fully funded scheme to give employers a degree of assurance about contribution rates over a longer period. In response, it was commented that although the interests of employers should be borne in mind,

the interests of the Pension Fund should be the key driver for the Strategy. Michael Hudson added that there was a danger that a 'comfort blanket' approach to consolidating the current funding levels for the Fund would fail to expose the Fund to market risk at a time when a more riskier growth strategy could be more beneficial. The Committee needed to review the Strategy at both its March and June 2019 meetings to determine its risk appetite and the strategy it wished to pursue

- In response to a query, Philip Hebson advised that the Fund did not want to be in a position where employer contributions had been reduced as a result of a high funding level but subsequently needed to be raised again as circumstances changed. It was important to achieve a balance between risk appetite and investment returns in whatever strategy was adopted.

RESOLVED that the presentation provided by River and Mercantile on the update to the existing Equity Protection Strategy and potential future options be noted.

148 Administering Authority - Administration Update (Agenda item 6)

The Committee considered the Administering Authority - Administration Update. The details were set out in the report.

In the ensuing debate, the following points were raised:

- Bridget Clark explained that as a result of the GMP Reconciliation exercise a total of 152 records had been identified where HMRC had stated that no GMP was payable as there was ‘no qualifying spouse’. The impact of accepting the HMRC position would be that some of the 152 members had received (an overpayment) incorrect pension. Of the 2 records, none were in excess of £1,000 per annum and only 24 were between £10 and £1,000 per annum
- What would be the additional cost to the scheme of accepting the HMRC record? Bridget Clark indicated that the cost would be £70k but there would also be the added burden on the administering authority of updating records and notifying dependents. Michael Hudson added there was the reputational impact on the Council of pursuing dependents who might be elderly and infirm.
- In response to a query, Bridget Clark confirmed

that as the Fund records did not hold whether a state bereavement benefit was ever claimed from HMRC a further file review to challenge HMRC was not recommended

- Michael Hudson drew the Committee's attention to a recent court case involving Lloyds relating to the equalisation of pay between men and women which could have an impact on the GMP Reconciliation
- Rob Wilson indicated that the cut-off date for the response from employers to the request for information for the covenant review was imminent. It was intended to report the outcome of the review to the extraordinary Committee meeting on 21 January 2019.

RESOLVED that:

a) **Option 1 – Accept Admin Records for Dependants ineligible for GMP be supported;**

b) **the update on the Guaranteed Minimum Pension (GMP) Reconciliation exercise be noted; and**

c) **the general update from the Administering Authority be noted.**

149 Pensions Investment Update (Agenda item 7)

The Committee considered the Pensions Investment Update. The details were set out in the report.

In the ensuing debate, the following points were raised:

- Rob Wilson reported that as a result of volatility in the market, the current funding level of the Pension Fund had fallen to 95%. It was intended to report the latest funding level to each Committee meeting in the future
- Was the benchmark target for JP Morgan – Emerging Markets fair? Philip Hebson advised that it was the Fund's right to set the benchmark target as it sought fit and he considered it to be fair. The issue for JP Morgan and other Emerging Market managers was that the investment universe was skewed towards the market in China and a small number of large stocks therefore a small change in those markets had a big impact on their performance
- Rob Wilson undertook to circulate a breakdown of the Councils set out in the report in Table 1 of the Covenant Review to members of the Committee.

RESOLVED that:

a) **The Independent Financial Adviser's fund performance summary and market background be noted;**

b) **The update on the Investment Managers placed 'on watch' by the Pension Investment Advisory Panel be noted;**

c) **The update on the Property and Infrastructure commitments be noted;**

d) **The update on the cashflow management be noted; and**

e) **The funding position compared to the investment performance be noted.**

150 Government Actuary Department (GAD) Pension Review Update (Agenda item 8)

The Committee considered the Government Actuary Department (GAD) Pension Review Update. The details were set out in the report.

In the ensuing debate, the following points were made:

- It appeared that the assumptions made by each fund's actuary had a significant impact on the calculation of funding levels. Michael Hudson responded that it was a question of balancing the Pension Fund objectives against employer objectives. The actuary had to take a view based on these potentially competing interests
- Michael Hudson commented that meetings would be held this time next year with employer and district council representatives to discuss the actuarial assumptions going forward. Issues to be discussed would include the tendering process and where the Fund would wish to be in 4 years time.

RESOLVED that the Government Actuary Department (GAD) Pension Review update be noted.

151 Risk Register (Agenda item 9)

The Committee considered the Risk Register. The details were set out in the report.

In the ensuing debate, Michael Hudson informed the Committee that Ian Kirk had left Mercers, the Fund's actuary and succession arrangements were being

discussed with Mercers. It was understood that internal arrangements were to be proposed and was not considered to be a risk.

RESOLVED that:

a) **The updated Risk Register be noted; and**

b) **The Committee particularly note and comment on the amber risks identified in the risk evaluation table within the Appendix.**

152 Stewardship Compliance Statement (Agenda item 10)

The Committee considered the Stewardship Compliance Statement. The details were set out in the report.

RESOLVED that:

a) **The Stewardship Compliance Statement be agreed;**

b) **The Responsible Investment activities be noted; and**

c) **The key areas of the Local Authority Pension Fund Forum (LAPFF) quarterly engagement report be included in the Committee's future pension's investment updates.**

153 Forward Plan (Agenda item 11)

The Committee considered its Forward Plan. The details were set out in the report.

In the ensuing debate, the following points were raised:

- Rob Wilson indicated that the Equity Protection Strategy would need to be considered at the March and June 2019 Committee meetings
- Bridget Clark welcomed any suggestions for items to add to the pensions training event scheduled for 18 December 2018.

RESOLVED that the Forward Plan be approved.

154 LGPS Central Update (Agenda item 12)

The Committee received a presentation from Callum Campbell, Head of Client Services and Investor Relations and Jason Fletcher, Chief Investment Officer of LGPS Central.

In the ensuing debate the following points were raised:

- Philip Hebson highlighted a concern expressed by

member funds that savings were being prioritised by LGPS Central at the expense of good investment returns going forward. Jason Fletcher responded that 80% of the score allocated to any investment bid related to quality assurance and therefore price was only a small part of the consideration. He argued that LGPS Central had assembled a good mix of innovative investment managers with the ability to maximise returns for member pension funds

- Philip Hebson highlighted a further concern expressed by member funds about the lack of transparency in terms of the ability of member funds to review the performance and fees of the investment managers. Jason Fletcher gave an assurance that LGPS Central was committed to being open and transparent. However there were certain aspects that by nature needed to remain confidential, for example investment manager's fees
- Michael Hudson queried the basis for the investment allocation across the three proposed investment managers. He argued that the arrangements lacked transparency with member funds unable to exert influence or assess performance and value for money. Jason Fletcher indicated that LGPS Central could skew the funding of the three managers to a maximum of plus or minus 10%. The decision would rest with the Investment Committee. There was no scope for individual Funds to have a greater or smaller exposure to each of the three managers, with their differing investment styles
- When was the decision taken and by whom to adopt a multi-manager approach to investment management because this approach had not been agreed by the Shareholders Forum? It was not an approach that this Fund had ever supported. Jason Fletcher responded that meetings had taken place with all partner funds in February to discuss investment management. By necessity there had had to be some form of compromise in the agreed approach
- Concern was expressed that Worcestershire Pension Fund would lose its ability to influence how it wished to invest member funds. Jason Fletcher commented that the danger was that in taking account of each individual member fund's investment requirements, the Pool would be operating nine separate investment management strategies with the resultant additional costs and

loss of economies of scale as well as a negation of the benefits of the pooling arrangements

- Given that the investment funds would be split equally between the three investment managers, what would happen in terms of the investment mix if one of the managers performed particularly well and how would performance be reviewed? Jason Fletcher responded that the Investment Committee had some scope to be able to change the mix of investments to a limit of 2% over the 33% allocation. He argued that a rebalancing on the investment mix was a positive action for the pool
- A degree of caution was expressed about the rebalancing approach to investment management in that it tended to reward failure especially where the partner fund had no say in the investment manager appointments. Jason Fletcher indicated that there was scope for over-performance by fund managers of up to 7%
- In response to a query about the difficulties appointing a Global Equities Manager, Jason Fletcher commented that salary and location appeared to be a stumbling block for candidates. The introduction of more flexible working arrangements was being considered to attract potential candidates. He was confident that an appointment would be made soon
- It was queried whether the location of LGPS Central in Wolverhampton had had a negative impact on recruitment and whether the Pool could consider locating elsewhere. Jason Fletcher indicated that it was important for the Pool to be located within its region but it was acknowledged that Birmingham would be a greater attraction for candidates
- In response to a query about the progress made in the appointment of the Chief Executive, Jason Fletcher commented that the recruitment process was on track and an appointment was likely to be made by the end of the year
- Concern was expressed that without a cost-sharing agreement, the breakeven point for partner funds could end up being further away. This agreement was vital for this Fund so that ongoing costs were known. Jason Fletcher indicated that the way in which the cost-saving model worked meant that there needed to be an initial investment of funds. As a result it would take some time for the cost savings to come through
- Callum Campbell welcomed any feedback from

member funds. LGPS Central would be circulating a monthly update bulletin to partner funds and an Annual Shareholders meeting would be held at the end of February

- Philip Hebson indicated that the newly appointed Chief Executive would have an important role in engaging with officers and members from partner funds in a more constructive way than was currently being undertaken
- There appeared to be a level of disquiet amongst partner funds, including this Fund about the lack of transparency and the investment management approach being taken by LGPS Central.

RESOLVED that presentation provided by LGPS Central be noted.

The meeting ended at 1.10pm.

Chairman …….