PENSION BOARD

MINUTES of a meeting of the Pension Board held at County Hall, Lewes on 4 August 2016.

PRESENT	Richard Harbord (Chair) Councillor Kevin Allen, Angie Embury, Sue McHugh, Councillor Brian Redman and Tony Watson
ALSO PRESENT	Cllr Richard Stogdon, Chair of Pension Comittee Marion Kelly, Chief Finance Officer Ola Owolabi, Head of Accounts and Pensions Brian Smith, Regional Operations Manager Jason Bailey, Pension Services Manager Wendy Neller, Pensions Strategy and Governance Manager John Shepherd, Finance Manager (Pension Fund) Harvey Winder, Democratic Services Officer

10 MINUTES

10.1 The Board agreed that the minutes were a correct record of the meeting held on 12 May 2016.

11 APOLOGIES FOR ABSENCE

11.1 There were no apologies for absence.

11.2 It was noted that David Zwirek had resigned as a scheme member representative meaning that there was currently a vacancy on the Board. A new GMB member is expected to be nominated to this position in due course.

12 DISCLOSURE OF INTERESTS

12.1 There were none.

13 PENSION COMMITTEE AGENDA

13.1. This item was introduced by Ola Owolabi (OO).

13.2. In reference to **Item 9 Petition – Divest East Sussex Pension Fund from fossil fuels** Councillor Brian Redman (BR) said that during his time as a member of the Pension Fund Investment Panel, the Panel had worked actively to ensure that investment managers working for the East Sussex Pension Fund (ESPF) influenced the companies in which they had invested ESPF funds to behave in an ethical way.

13.3. BR said that he had been to a Local Authority Pension Fund Forum (LAPFF) meeting in December in Bournemouth and had been reassured that the issue of ethical investment for Local Government Pension Schemes (LGPS) was being taken seriously by the Forum – a considerable amount of the meeting was spent on the matter. BR was confident that ethical behaviour would benefit the companies themselves as they could absorb the costs of behaving more ethically whilst being reassured that investors would still be willing to invest in them. He recommended that other Board members attend the next LAPFF meeting in December.

13.4. Councillor Kevin Allen (KA) welcomed the appearance of the issue of fossil fuel disinvestment on the Pension Committee's agenda. KA informed the Board that the issue of fossil fuel disinvestment had been debated at the Brighton & Hove City Council (BHCC) Full Council meeting. He speculated that had the notice of motion been as straightforward as the one that passed at Hastings Borough Council it would have been passed (in the event, it was not). He said that individual councillors will continue to receive requests to endorse disinvestment and the Board should take disinvestment seriously, provided that it does not interfere with the ESPF administering authority's fiduciary duties. KA added that it was important that the petitioners were informed of this fiduciary duty. Marion Kelly (MK) said that the issue of disinvestment was higher on the priority list of LGPSs than it had been 10 years ago.

13.5. Sue McHugh (SM) recommended that any analysis of the value in fossil fuel disinvestment ought to include a quantified cost to the ESPF of disinvestment – be it over the short or long term. SM felt that only presenting the argument that investment allowed the ESPF to influence the ethical behaviour of companies was unlikely to be sufficient to convince people of the value of investing in those companies. OO confirmed that the ESPF's investment consultant (Hymans Robertson) had been approached to provide analysis of the costs of disinvestment for the Pension Committee meeting in September. MK added that it was a complex task to calculate the financial outcome of disinvestment.

13.6. The Chair said that it was right that the ESPF embraced the principle of ethical investment. However, he cautioned that a policy of disinvestment was complicated by the need to ensure that employers and council tax payers were not adversely affected; the fact that the Fund invests in large multinational companies that may produce products considered by others to be unethical – such as alcohol and tobacco; and the fact that large multinationals may have a complex web of subsidiary companies, some of which may behave unethically. The Chair added that pension fund members in Canada were involved in an $18bn class action law suit for lost earnings through tobacco disinvestment.

13.7. Councillor Richard Stogdon (RS) the Chair of the Pension Committee said that the Committee would consider the issue of disinvestment carefully, but he cautioned that it would be difficult for the Committee to justify to the 69,000 members in the ESPF the underperformance of the Fund compared to its neighbouring pension funds – should that be an outcome of disinvestment. RS reiterated the Chair's concern over the difficulty in deciding what is and is not an ethical company; and he added that disinvestment carried the additional risk of reducing the spread of investments and making the Fund more susceptible to market fluctuations.

13.8. KA said that he understood analysis had been undertaken, and was available online, of the extent to which the LGPSs invested in fossil fuels. KA said that the website showed that some funds have performed well despite reducing investment in fossil fuel, in particular Lancashire County Pension Fund.

13.9. In reference to **Item 10 – Statement of Investment Principles**, the Board was satisfied that there had been no major changes to the Statement of Investment principles over the last year.

13.10. The Board RESOLVED to note the report.

14 REVIEW OF FUND MANAGERS FEE ARRANGEMENTS

14.1. This Item was introduced by OO.

14.2. Angie Embury (AE) questioned whether the increase in investment management fees of 2% in 2015/16 offered value for money when the ESPF fund value had only increased by 1%. OO said that these increases needed to be considered in terms of their monetary value; the increase in fees had been £0.2m but this had led to an increase in the fund value of £24.9m in 2015/16.

14.3. AE asked whether there was a breakdown available of the assets held by ESPF that showed the transaction costs of those assets, as this was available in Holland and UNISON had conducted a breakdown of its own pension fund investment transactions. OO explained that analysing the cost to the fund of each transaction fee would be very complex given how the cost of transacting private equities was very varied. However, the Investment Management Agreement (IMA) between ESPF and investment managers includes an agreement of the acceptable range of transaction charges the investment manager should be willing to pay when buying or selling assets. The ESPF's external auditor, KPMG, has access to these agreements.

14.4. The Chair asked whether the external auditor looked for any evidence of unnecessary 'churn' of equities as this would indicate that investment managers were making additional money through transaction fees. He added that he did not expect there to be any evidence of this kind of behaviour. OO said that KPMG only look at ESPF. However, the complexity and variety of the market and the funds' strategies means that it would be very difficult to meaningfully compare two different funds, for example, they may be investing in equities with higher transaction costs, or investing in more long term equities and so would make fewer transactions.

14.5. AE suggested that transaction fees could be lowered if ESPF invested more in passive managers than active managers, even if that resulted in lower returns. MK said that active fund managers do not have a high amount of churn as they more often than not opt for long term equities, and the ESPF strategy is to opt for long term equities. Passive managers, on the other hand, have more churn because they are looking to replicate the performance of the markets.

14.6. SM asked for confirmation that the figures in appendix 1 – showing the value of each investment managers' portion of the ESPF – took account of the transaction costs. MK confirmed that the value of the fund was net of the cost of the transaction fees, and the fees paid to the investment managers did not include the transaction fees.

14.7. SM noted that the investment managers were being paid regardless of performance and asked if there was any value in a fee structure for investment managers that incentivised performance. The Chair observed that the idea of incentivised payments had been around for a long time but had not always been successful due to the fact that they encouraged investment managers to take unnecessary risks.

14.8. MK said that at the moment it was difficult to negotiate lower fees because investment managers operate on the principle that they won't provide lower fees than those that they provide to other LGPS. However, the ACCESS pooling group may have sufficient negotiating power to reduce fees in the future.

14.9. The Board RESOLVED to 1) note the report; and 2) request a report to be circulated by email providing a breakdown of the number of transactions investment managers make on a quarterly basis.

15 PROGRESS REPORT ON THE 2016 ACTUARIAL VALUATION

15.1. This item was introduced by OO.

15.2. OO said that the actuarial valuation timetable called for the submission of employer data, accounting data, and membership data to the actuary (Hymans Robertson) by 29 July 2016 and that both the employer and accounting data had been supplied. OO advised that this deadline would now slip due to the membership data and passed to Jason Bailey (JB) to update the Board. JB advised that the reason for the delay was the discovery of 13,000 validation queries regarding the membership data. JB said that the vast majority of the queries resulted from differences between the software suppliers (that supply the new universal data capture software used by LGPSs) and the actuarial firms regarding the data specification; this was a national issue affecting all LGPS funds as the triennial valuation is the same date for all funds (though some actuarial firms may take a slightly different approach to validation) and beyond Orbis Business Operation's control.

15.3. JB was confident that this discovery of the 13,000 validation queries was related to validation differences rather than incorrect data being held on the pensions data; and the queries were now being processed by Orbis Business Operations – with 8,000 already processed – prior to the submission to the actuary, so the quality of the data will be higher when it is submitted.

15.4. The Chair expressed concern that the difference in the data being asked for and being supplied had not been noticed during the testing period. He asked for confirmation that this would not come at a cost to the ESPF; JB said that it would not.

15.5. The Chair said that it was critical that this issue did not affect the availability of the draft employer results in time for the Employers' Forum on 18 November, as failure to reach this milestone would cause reputational damage to the administrative authority of the ESPF. Tony Watson (TW) added that this would affect the credibility of the ESPF. JB said that he was confident that the actuary's draft results would be available before then. Wendy Neller (WN) added that the actuary has advised that the delay in the submission of 'clean' membership data by up to three weeks will impact the agreed timescales for the delivery of the initial whole fund valuation results; this was scheduled to be issued during September, but is now expected to move to October. The time that the Fund has to discuss the results with the actuary in detail in relation to each employer will consequently be reduced. WN advised that delivery of membership data on a date later than 19 August 2016 will further impact the valuation timescales.

15.6. The Board RESOLVED to note the report.

16 <u>LEGAL POSITION OF PENSION BOARDS</u>

16.1 This item was introduced by the Chair.

16.2 The Chair explained that the opinion of James Goudie QC regarding the legal status of pension boards does not affect how the East Sussex Pension Board has been set up. However, a considerable number of other pension boards were exercising the functions of the pension committee, i.e., the management and administration of their pension fund; and were constituted as if they were local authority committees, i.e., the members of the boards were local authority elected members rather than scheme member and employer representatives.

16.3 The Board RESOLVED to note the report.

17a <u>OFFICERS' REPORT - BUSINESS OPERATIONS</u>

17a.1 This item was introduced by Brian Smith (BS) and JB.

17a.2 The Chair asked why the current result for the key performance indicator (KPI) "the number of estimates provided within the specified timescale of 7 days" had fallen. JB said that this was due to a 50% increase in the volume of LGPS requests in June. JB added that the KPI itself was more stringent than the industry average of 10-20 days, and the volume of requests for estimates was expected to fall as the self-service facility become available online later in the year.

17a.3 BS said the new KPIs were more customer focussed and more in line with the industry standard for other schemes, meaning that they were no longer targeted at 100% compliance. However, achieving them would still ensure that the pension fund administration service was one of the highest performing in the country. The first data would be available in November 2016.

17a.4 BR asked whether the new KPIs were in line with CIPFA standards. JB said that CIPFA does not publish nationally agreed KPIs and different pension funds tended to adopt different KPIs. There is, however, a reasonable consistency in some areas – for example, the timescales for the calculation of spouse's benefits within five days. JB said that it was questionable whether it was necessary to have a KPI target of 100% with a stringent timescale for items that had no material impact on members, and that this could lead to an increase in resourcing requirement.

17a.5 The Chair asked for assurance that the new KPIs had been set rationally and not low enough that they could be comfortably achieved each month. JB said that activity 10 and 11 – 'Employer survey satisfaction' and 'Member survey satisfaction' would give a clear indication of how the service was performing.

17a.6 AE asked whether the recruitment issues in the pension administration team had been resolved. JB said that they had been following the recruitment of four new graduates, and the team was now looking to recruit an apprentice through East Sussex County Council's apprentice scheme.

17a.7 The Board RESOLVED to note the report.

17b <u>OFFICERS' REPORT - GENERAL UPDATE</u>

17b.1 This item was introduced by OO.

17b.2 OO added that the Government has informed ACCESS that it cannot form a joint committee as part of its operator structure and so must look at a Common Investment Vehicle (CIV) alternative. OO said ACCESS could either build its own CIV – which would require significant time and investment – or rent from two possible organisations currently being considered. OO said that the Chairs of ACCESS will meet to consider and agree the preferred option on 2 September 2016 with an expectation that it will be in place by April 2018. SM asked why only two organisations were being considered. OO understood that there were only two organisations with sufficient resources to accommodate a CIV for ACCESS, which will have in excess of £30bn of assets.

17b.3 The Chair asked when the Government would respond to the ACCESS proposal that was submitted on 15 July. OO said that the Government had indicated that feedback would take place at the end of September. The Chair was sceptical about this deadline given that the Government was on recess and would soon be embarking on the Conservative Party Conference, so there would be little time to analyse the submissions.

17b.4 KA asked why – in the letter to Marcus Jones MP – the ACCESS group expected to achieve savings only "eventually". OO said that the savings projections were based on analysis by Hymans Robertson; he confirmed that ESPF was expected to benefit from these savings.

17b.5 KA expressed concern that there seemed to be no prospect of maintaining local decision making and accountability once the pension funds are pooled into ACCESS. KA said it was vital that Marcus Jones MP addresses this concern when he responds to the ACCESS Chair's letter submitted alongside their proposals on 15 July 2016. The Chair observed that this issue had been raised previously and there had been little apparent sympathy. RS shared KA's view and added that, in effect, the elected Pension Committee's role would be handed over to an unelected organisation. AE added that local accountability was part of Unison's campaign around pension fund pooling.

17b.6 The Board RESOLVED to 1) note the report; 2) request that a draft of the Pension Board's annual report be circulated to the Board prior to its presentation at the Employers' Forum

18 <u>PENSION BOARD FORWARD PLAN 2016/17</u>

18.1 This item was introduced by OO.

18.2 The Board RESOLVED to 1) note the report; and 2) request a future update on the progress of the actuary valuation at its November meeting.

19 ANY OTHER BUSINESS

19.1 There was none.

The meeting ended at 11.55 am.

Richard Harbord
Chair