PENSION BOARD

MINUTES of a meeting of the Pension Board held at County Hall, Lewes on 9 February 2017.

PRESENT	Richard Harbord (Chair) Councillor Kevin Allen, Angie Embury, Bernadette Carlyle, Sue McHugh and Councillor Brian Redman
ALSO PRESENT	Councillor David Elkin, Lead Member for Resources Councillor Richard Stogdon, Pension Committee Chair Brian Smith, Regional Operations Manager Ola Owolabi, Head of Accounts and Pensions John Shepherd, Finance Manager (Pension Fund) Graham Devenish, Pensions Operation Manager Harvey Winder, Democratic Services Officer

33 MINUTES

33.1 The Board agreed that the minutes were a correct record of the meeting held on 3 November 2016.

34 APOLOGIES FOR ABSENCE

34.1 Apologies for absence were received from Tony Watson.

35 DISCLOSURE OF INTERESTS

35.1 There were none.

36 URGENT ITEMS

36.1 There were none.

37 PENSION COMMITTEE AGENDA

37.1 The Board considered a report on the Pension Committee's agenda for its 27 February meeting. The reports were introduced by Ola Owolabi (OO), Head of Accounts and Pensions.

37.2 In reference to **Item 9: Investment Strategy Statement (ISS),** the Chair invited representatives of Divest East Sussex to speak about their document titled "Managing Climate Risk: Proposed Additions for ESPF's new Investment Strategy".

37.3 Councillor Kevin Allen (KA) and Angie Embury (AE) questioned why under the section "How social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments" the fund appears to be excluded from divesting, boycotting or sanctioning foreign governments or UK defence industries when the funds' members may object to investing in UK defence industries. OO said that the wording was in line with the requirements of the LGPS Management & Investment of Funds Regulations 2016 which prohibits funds from being able to disinvest from UK defence industries and foreign governments for non-financial reasons.

37.4 KA said that the Pension Committee should consider acting as a front runner in reducing investment in fossil fuels if it can be done whilst upholding its fiduciary duty.

37.5 Sue McHugh (SM) said that the Pension Committee's fiduciary duty towards the ESPF means it cannot take a blanket decision to not invest in an any industry without strong enough evidence that it will not impact negatively on investment returns. The financial risk sits with the ESPF and employers rather than individuals, so the Committee members should not take a decision that they might do in their capacity as an individual if it causes financial risk to the pension fund and its employers.

37.6 OO explained that the investment managers working on behalf of the ESPF will invest according to the Fund's beliefs as set out in the ISS. The Local Authority (LAPFF) has a strong ethical stance and also helps to guide where investments should be made on behalf of other local government pension funds.

37.7 SM asked, in reference to the section "Investment of money in a wide variety of investments", how much of the total value of all investments was in entities which are connected with East Sussex County Council (noting that the legal maximum was 5%). OO confirmed that no investments were in entities connected to the Council. He added that the viability of local investment had previously been looked at but none were found to yield a reasonable return.

37.8 AE asked how ACCESS fund pooling would affect the varied investment strategies of individual member funds. OO explained that all 11 funds will retain their strategies and invest in the same asset classes as decided by their respective Pension Committee. The difference will be that each asset class, e.g., absolute return or property, will be managed by a single investment manager – instead of 11 individual managers – who will invest on behalf of all of the ACCESS members that allocate funds into that asset class. This will deliver benefits of scale by reducing the investment manager fees.

37.9 The Chair asked what infrastructure projects ESPF is investing in. John Shepherd (JS) said that the 2% of the fund allocated to infrastructure is held by investment mutual funds that hold a portfolio of worldwide infrastructure investments, rather than holding a large stake in an individual infrastructure project.

37.10 In reference to **Item 10: Funding Strategy Statement (FSS)**, the Chair asked whether there was a significant difference between the new FSS and the previous strategy. OO confirmed that there was no significant difference but the employer contribution rate has reduced since the outcome of the triennial valuation and the FSS needed to be amended to reflect that.

37.11 Councillor Brian Redman (BR) questioned whether the salary growth projections up to 2019 in the triennial evaluation were an underestimate given the potential higher inflation and the increasing demand for public sector wage rises it will create. OO said that the projection took into consideration not just the next three years but also long term projections to help ensure that the ESPF will not be underfunded by 2019. The Chair added that the Institute of Fiscal Studies had recently reported that the percentage of GDP spent on the public sector had reached an all time low, there has been a retrenchment of the overall number of public sector workers in the past few years, and austerity is expected to continue for the next 6-8 years. This meant that it is unlikely that there would be an excessive increase in public sector pay.

However, the report also projected tax increases in the next few years, and AE suggested that this could put pressure on demands for pay increases.

37.12 In reference to **Item 11: Pension Fund Cost Analysis**, the Chair observed that it was difficult to know whether the pension administration was good value for money because of the imprecision of benchmarking. He added that there was not a lot of variation in the costs since 2012/13 but it appeared that performance was going in the right direction.

37.13 Brian Smith (BS), Head of Operations, said that the CIPFA benchmarks were a comparison of 38 local authorities that had volunteered their performance figures and were not a complete picture; however, they were the best available comparison.

37.14 In reference to **Item 14: Pension Fund Budget for 2017/18,** the Chair asked how the budget would remain exactly the same for the next financial year. OO explained that this would be achieved by renegotiating fees with investment managers and the increase in the value of the fund.

37.15 The Chair asked whether the budget outturn for this financial year would be in line with the budget projections. OO expected that there would be an underspend as the Guaranteed Minimum Pension (GMP) reconciliation money committed for 2016/17 will not be committed this year.

37.16 BR asked whether the £100,000 committed to GMP reconciliation this year would be carried over to next year. OO said the £100,000 will be reinvested into the fund and the £120,000 for 2017/18 was a separate amount.

37.17 The Chair said that the £66,000 reduction in actuarial fees next year would be due to the fact that there was a triannual valuation during 2016/17. The £30,000 reduction in specific actuarial work on behalf of employers would be for the same reason.

37.18 OO noted that there was an error in the variance in the cost of investment consultancy for 2017/18 which was £0 and not £8,000.

37.19 The Board RESOLVED
1) to note the Pension Committee reports; and
2) to recommend that the Pension Committee approve the Investment Strategy Statement (ISS) subject to the addition of an expanded description of how the ESPF influences investment managers to consider ESG factors when making investments.

38 <u>EXTERNAL AUDIT PLAN FOR EAST SUSSEX PENSION FUND 2016/17</u>

38.1 The Board considered a report on the External Audit Plan for East Sussex Pension Fund for 2016/17.

38.2 The Chair commented that a materiality of 1% of net assets seemed very high given that this equated to £27 million. He said it would make more sense to make it 1% of the pension administration costs. OO said that although the materiality level was high, non-trivial and trivial errors would still be recorded and reported by the external auditors. Furthermore, the materiality is classified as “creeping materiality”, so the £27 million trigger would be a cumulative figure of all errors discovered in the accounts, at which point the external auditor could issue a qualified opinion.

38.3 SM asked whether the external auditor was in a position to comment on investments and not just accounts. OO said that there were statutory requirements for the external auditor to discuss concerns about investments with pension fund officers, the Committee and the Pension Board.

38.4 The Board RESOLVED to note the report.

39 PENSION BOARD INSURANCE ARRANGEMENTS

39.1 The Board considered a report on the Pension Board Insurance Arrangements.

39.2 The Chair explained that although the Board did not take decisions, it could still be considered negligent if it failed in its duty to report breaches of the law to the Pension Fund Regulator. However, only two of 89 pension boards had so far opted to acquire an insurance premium to cover potential liability. He recommended that the Board defer this recommendation to the Committee until such time as more pension boards had opted for the insurance premium.

39.3 SM observed that as only Aon Risk Solutions was offering this insurance policy, the value of the asking price could not be verified against a market average. This made it more prudent to wait until the market matured.

39.4 The Board RESOLVED to:
1) note the report; and
2) defer the recommendation to the Pension Committee to approves the Pension Board Insurance premium for payment until the next meeting on 26 June 2017.

40 REPORTING BREACHES POLICY

40.1 The Board considered a report on the Reporting Breaches Policy.

40.2 The Chair observed that, in light of the legal advice about the potential risk to pension boards for failure to report breaches, all breaches, even those that the Monitoring Officer and Chief Finance Officer do not consider material, should be reported to the Board.

40.3 The Board resolved to:
1) note the report; and
2) recommend that all material and non-material breaches are reported to the Pension Board.

41 BUSINESS OPERATIONS SYSTEMS - UPDATE

41.1 The Board considered a report providing an update on the effectiveness of the current LGPS administration system used by Business Operations and market alternatives.

41.2 The Chair asked for confirmation that, in line with the Pension Committee’s decision in March 2016, there was still an opportunity to activate the 3-year break clause in the contract with Heywood if necessary. . BS confirmed that with the assistance of procurement, who will provide an independent view, a review of the alternative LGPS administration system provided by Civica would be completed by December 2017, allowing time for a procurement process to be completed before the 3-year break clause period is reached in March 2019.

41.3 The Board RESOLVED to note the report.

42 OFFICERS' REPORT - BUSINESS OPERATIONS

42.1 The Board considered a report providing an update on the work of the Business Operations Team.

42.2 Graham Devenish (GD), Pension Operations Manager, said that the Pension Regulator is recommending GMP reconciliation tolerance level of £2, although the impact this will have on individual scheme members will vary. There is also the possibility that scheme members may owe the Fund and in theory this money could be clawed back. The cost of pursuing individual cases to the nearest penny may cost ESPF more than accepting a tolerance level of £2. GD added that HMRC's deadline for closing their GMP records in December 2018 is very unlikely to change and only a limited service will continue after that date.

42.3 BR asked for clarity about whether the budget of £120,000 for 2017/18 will be sufficient to cover GMP reconciliation costs. GD said that ITM provided a stage 1 report for both Surrey and East Sussex at a lower cost due to the benefits of scale. The report compared a database of scheme members against HMRC records to find where there were mismatches; 15-20,000 people may be liable for GMP reconciliation but it is not clear yet the cost of this liability to ESPF. ITM's involvement in the process is expected to cost £160,000 for both funds, which is well within the ESPF budget for 2017/18 or £120,000.

42.4 BR asked why the audit, actuary and ICT costs were around 60-70% higher than the benchmark. BS clarified that the CIPFA ICT benchmarking was a year behind and did not account for the reduced costs realised by the new pension administration system procured in April 2016. The Chair said that the audit fee was only £19,000 and so the fact it was comparatively higher did not have a significant impact.

42.5 BR observed that the overall cost of actuarial work was considerable when taking into consideration the work performed by the actuary on the behalf of specific employers, which is recharged to the Fund. SM said that the process of having the actuary produce bespoke financial statements for employers that are then independently checked was inefficient and there was no national discount rate. OO said that the ongoing savings at district, borough and unitary authorities involved redundancies that might have pension implications and so it was necessary for the actuary to check for these.

42.6 The Board resolved to note the report.

43 OFFICERS' REPORT - GENERAL UPDATE

43.1 The Board considered a general update on pension issues.

43.2 The Board RESOLVED to note the report.

44 FORWARD PLAN

44.1 The Board considered its forward plan.

44.2 The Board RESOLVED to note the report.

45 EXCLUSION OF THE PUBLIC AND PRESS

45.1 The Board RESOLVED to exclude the public and press from the meeting for the remaining agenda item on the grounds that if the public and press were present there would be disclosure to them of exempt information as specified in paragraph 3 of Part 1 of the Local Government Act 1972 (as amended), namely information relating to the financial or business affairs of any particular person (including the authority holding that information).

46 <u>PENSION COMMITTEE AGENDA - EXEMPT REPORT</u>

46.1 The Board considered the exempt report of the Pension Committee agenda: LGPS Asset Pooling – ACCESS Inter Authority Agreement.

46.2 The Board RESOLVED to note the report.

The meeting ended at 12.04 pm.

Richard Harbord (Chair)
Chair