BATH AND NORTH EAST SOMERSET

AVON PENSION FUND COMMITTEE

Friday, 17th March, 2023

Bath and North East Somerset Councillors: Paul Crossley (Chair), Shaun Stephenson-McGall (Vice-Chair), Bruce Shearn, Chris Dando and Paul May

Co-opted Voting Members: Councillor John Cato (North Somerset Council), Councillor Steve Pearce (Bristol City Council), Councillor Toby Savage (South Gloucestershire Council), Charles Gerrish (Academies), William Liew (HFE Employers), Richard Orton (Trade Unions), Pauline Gordon (Independent Member), John Finch (Independent Member) and Jackie Peel (Independent Member)

Co-opted Non-voting Members: Wendy Weston (Trade Unions), Michael Rumph (Trade Unions) and Cllr John Goddard (Parish and Town Councils)

Advisors: Steve Turner (Mercer), Paul Middleman (Mercer) and Nick Page (Mercer)

Also in attendance: Nick Dixon (Head of Pensions), Liz Woodyard (Group Manager for Funding, Investment & Risk), Nathan Rollinson (Investments Manager), Geoff Cleak (Pensions Manager), Carolyn Morgan (Governance and Risk Advisor), Nicky Russell (Technical & Compliance Advisor), David Richards (Finance & Systems Manager (Pensions)), Jeff Wring (Director, One West) and Charlotte Curtis (Governance & Risk Officer)

45 EMERGENCY EVACUATION PROCEDURE

The Chairman drew attention to the emergency evacuation procedure.

46 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

There were none.

The Chairman informed the Committee that Geoff Cleak, Pensions Manager was due to retire soon and asked the Head of Pensions to address them.

Nick Dixon, Head of Pensions said that Geoff had worked for Local Government for 40 years and had been responsible for creating a strong culture of service within the Fund. He added that he will be greatly missed as part of the team.

Geoff Cleak addressed the Committee and said that it had been a pleasure to have worked for the Fund for the last 35 years. He added that he welcomed the commitment and resource that has been given to the Fund during his time.

The Head of Pensions informed the Committee that Claire Newbury, Digital Services Project Manager would become the new Pensions Manager in due course.

47 DECLARATIONS OF INTEREST

There were none.

48 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

There was none.

49 ITEMS FROM THE PUBLIC - TO RECEIVE STATEMENTS, PETITIONS OR QUESTIONS

Elaine Ashley had submitted the two following questions to the Committee.

Question 1

You state that you support the Engagement rather than an urgent Divestment strategy with Fossil Fuel companies (and presumably also Fossil Fuel investors such as Black Rock). I would like to know what evidence you have to suggest that this strategy is likely to work and what detailed plans you have in place to monitor what progress is being made and at what point you disengage due to lack of progress.

The divestment campaign has been developing for more than 10 years and many bodies have been pursuing a strategy of engagement for many years, even though we have seen some considerable green-washing in the fossil fuel sector, some of which has been very publicly exposed and legally challenged. We have also seen fossil fuel companies continuing with very major plans for continuing expansion and increasing output, when we know that this is disastrous for the future of life of earth, which requires 45% reduction in carbon emissions before the end of this decade, with fossil fuels being the source of the vast majority of those emissions. We have also seen major financial institutions sometimes respond to shareholder pressure one year, only to quietly reverse the changes the following year.

In terms of whether divestment works better than engagement, there is an expert review of a range of evidence that suggests that divestment does work, with further robust evidence published since that review also coming to the same conclusion.
Additionally, one very recent report raises *the risks of failing to divest* very seriously indeed, while another author suggests that '…the financial debate about divestment is as settled as the ethical one…' as a result of research and analysis by Black Rock.

So there would seem to be evidence to show that Engagement does not work and the other there is major expert evidence to show that divestment does work, and, further, that *failure to divest* presents a very major risk. This risk is very high, and increasing all the time, in regard to Avon Pension Fund – although it has done more than many funds to move away from Fossil Fuel investments it still looks as if there is a serious danger of being left behind with stranded assets.

"ABP (Dutch Civil Service fund) are divesting over the next 10 years, while 1,500 asset managers are offloading more than $40 trillion in fossil fuel holdings," says

Shandal (Partner and Managing Director at BCG). “The trend is clearly focused on divestment rather than on engagement.”

“Investments in fossil fuel assets need to decline rapidly, because they work against the clean energy transition now and lock in GHG emissions for decades to come, leading to stranded assets in the future (Campiglio *et al.* 2018; Mercure *et al.* 2018; Kreibiehl *et al.* 2 022).

…Together with societal and litigation risks, these technological and policy risks cause a “transition risk” that should be managed to avoid financial instability (Campiglio *et al.* 2018). The bursting of a carbon bubble cannot be ruled out (Griffin *et al.* 2015).” UN Emissions Gap Report 2022

Question 2

How closely are you monitoring the risk of being left with stranded assets of Fossil Fuels that will have to remain in the ground?

The Head of Pensions thanked her for her questions on behalf of the Committee and said that they would reply to the points raised in writing.

50 ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

There were none.

51 MINUTES: 16TH DECEMBER 2022

Pauline Gordon advised the Committee that she had emailed the Democratic Services Officer regarding two minor amendments.

With those amendments in mind the Committee **RESOLVED** that the minutes of the meeting on 16th December 2022 be confirmed as a correct record and signed by the Chair.

52 STRATEGIC INVESTMENT REVIEW

The Committee, having been satisfied that the public interest would be better served by not disclosing relevant information, **PROPOSES**, in accordance with the provisions of the Section 100(A)(4) of the Local Government Act 1972 that the public should be excluded from the meeting for this item of business, because of the likely disclosure of exempt information as defined in paragraph 3 of Part I of Schedule 12A of the Act as amended.

53 2023 - 26 SERVICE PLAN AND BUDGET

The Head of Pensions introduced the report to the Committee and highlighted the following points from within it.

- The Ukraine conflict and other global challenges have adversely impacted the Fund in 2022. Markets have experienced elevated volatility, with UK government bonds for example declining in value by c.30%.

- Even though the Fund's portfolio declined by 11% during 2022 to £5,231m, we enter 2023 in a robust financial position with a c.97% funding level.

- Operationally the Fund has had more mixed success during 2022-23. Service performance in aggregate is below required levels, with only 5 of 19 service measures completed within target timescales. This is a result of high staff vacancy rates of c.13%, churn of leavers and joiners, regulatory change, and slow progress in digitising administration.

- Administration Strategy - At its heart is a strategic change programme of projects to meet regulatory needs, raise operational efficiency, and improve member experience. To be implemented over 2023-26, this will raise our capacity and enable us to serve members and employers more effectively over time. The plan is being developed and will be shared in detail with the Committee in June 2023.

- Funding Strategy - The Fund already has captive group-wide insurance for Ill-health retirement given that this can result in significantly liabilities. The main new funding project in 2023 is to explore similar groupwide captive insurance options for Death in Service, at minimal extra cost to employers. Officers will come back to the Committee with a proposal for their approval later in 2023.

- Communications Strategy - Stakeholder engagement: the Fund needs to clearly communicate with key stakeholder groups, e.g. councillors, scheme members, trades unions, etc. on investments and climate change. This will encourage broad feedback and input to influence the Committee's decisions on revised climate targets in September 2023.

- The Fund's overall budget for 2023-24 of £31.9m is £2.1m lower than in the previous year's budget of £34.0m. There are two core budget components:

    - The administration budget of £7.0m for 2023-24 is £1.1m higher than 2022-23.

    - 2023-24 investment fees of £24.9m are £3.2m (11%) lower than the £28.1m of 2022-23. The difference is driven by: asset values lower than 2022-23 budget, raising the proportion of passive equities from 39% to 50%, and changes in portfolio allocations.

Wendy Weston referred to page 139 and asked what sectors were increasing their active membership.

The Pensions Manager replied that there had been quite an increase in part-time workers and these were mainly within Academies / Multi Academy Trusts.

Pauline Gordon asked how our costs relate to other Funds in terms of benchmarking.

The Head of Pensions replied that there is an annual benchmarking report produced and he believed that the Fund was broadly in the middle of the pack in terms of cost per member and cost per asset. He added that most importantly they are looking to improve service levels and then seek to bring down unit costs.

Councillor Paul May asked how the review of pay scales for the Fund is dealt with by B&NES as an overall organisation in terms of its employees.

The Head of Pensions replied that a report would be submitted to the Council's HR and Finance departments for them to advise / approve on how any changes can be implemented alongside other salaries across the Council.

The Director, One West added that the Fund has to work within the same processes as all other areas of the Council. He said that a Hay evaluation and grading scheme will take place as part of this exercise and assured the Committee that all governance procedures will also be followed.

Jackie Peel asked if there is a 'Plan B' if the recruitment of additional staff does not come to fruition as is hoped.

The Head of Pensions replied the Fund is open minded about the option to outsource any functions to consultants / partners as it already does so in some cases. He added though that they were not anticipating the need to do so with regard to the administration of the service.

Richard Orton asked if the figure of £0.4m would be enough to address the salary reviews.

The Head of Pensions replied that they do believe that this figure will be sufficient.

Richard Orton commented that the number of participating employers had decreased from 484 in 2021 to 331 in 2022 and asked if it was known why this had occurred.

The Group Manager for Funding, Investment and Risk replied that it was because many of the Admission Bodies have short term contracts for elements of their outsourcing, catering etc. She added though as Multi Academy Trusts have begun to pool more resources this will have seen a decline in those overall numbers.

Charles Gerrish asked for clarification if the Hay evaluation would cover all market parameters or just the public sector.

The Head of Pensions replied that they will be looking across both the private and the public sectors.

The Director, One West said that this had so far been one of the most extensive analysis that he had seen. He added that Aon were acting on behalf of the Fund and were gathering a deep level of evidence for every role within the Fund.

Charles Gerrish asked if there was to be any regional pay influence.

The Head of Pensions replied that other LGPS such as Somerset, Wiltshire and Gloucestershire have been included in their benchmarking and some of the private sector evidence has been from companies in and around the Bristol area. He added that the competitive dynamics have become more complex now that the majority of employees can work from home.

Wendy Weston referred to Appendix 4 and asked if the reduction in forecast budget for the Pension Board in 2022/23 could be explained.

The Governance & Risk Advisor replied that it had been because a number of meetings and training had taken place remotely over the past year. She added that in the coming years some of these elements would return to being in person and a recruitment exercise was also expected for roles within the Board.

Councillor John Cato referred to Appendix 2a and asked if there was a known completion date target for the ‘Review disaster recovery / business continuity plan’ and ‘Review of Committee Reports’.

The Governance & Risk Advisor replied that officers were in the process of re-prioritising projects and it was anticipated that this programme would be revised by June.

The Committee **RESOLVED** to approve the 3 Year Service Plan and Budget for 2023-26 for the Avon Pension Fund.

54 ACTUARIAL VALUATION 2022 & UPDATED FUNDING STRATEGY STATEMENT

The Group Manager for Funding, Investment & Risk introduced the report to the Committee. She said that it was anticipated that the Actuary will finalise the actuarial valuation report next week, before the 31 March 2023 deadline. She added that this was the first time that Climate Risk had been included within the report.

Paul Middleman, Actuary, Mercer said that the report would consider the impact of Climate Risk under three different temperature scenarios and it draws out how the strategy that the Committee has put in place aligns with those scenarios.

The Committee **RESOLVED** to:

i) Note the outcome of the 2022 actuarial valuation exercise.

ii) Delegate the finalisation of the Funding Strategy Statement to Officers.

55 TREASURY MANAGEMENT POLICY

The Finance & Systems Manager introduced the report to the Committee. He explained that the Committee is asked to approve the Fund's Treasury Management Policy each year and that it was last approved in March 2022.

He added that the Policy closely mirrors the Council's policy set out in the Councils' Annual Treasury Management Strategy.

The Committee **RESOLVED** to approve the Treasury Management Policy set out in Appendix 1.

56 PENSION FUND ADMINISTRATION

The Pensions Manager introduced the report to the Committee and highlighted the following areas to them.

<u>KPI's</u>

Incoming case work is generally increasing per quarter and the Fund continues to operate below its desired target of >90% for most case types. Although there has been a marginal improvement overall with previous quarters, generally, KPI benchmarking performance has remained below target.

A complex mix of challenges have contributed to the continued downturn including increased member churn and acceleration of scheme employers providing data monthly.

Once in place, the agreed new Admin Operating Model will embrace available systems technology to bulk process the majority of leavers, reducing the amount of manual intervention.

<u>McCloud</u>

97% of our employers have supplied their data to us including one of the two outstanding Unitary Authorities. We are continuing to chase this unitary and the 13 employers who have not provided the data to us. The team are checking the data and will be shortly contacting employers with any missing information or queries in readiness for the rectification method anticipated to arrive in the summer, delayed from end of the year.

We continue to be in engagement with Aon Consultants in respect of the McCloud project for data Remedy. The McCloud Data scoping group are awaiting guidance from Scheme Advisory Board to enable us to deal with poor/missing data.

<u>i-Connect – Monthly Data Returns</u>

In the last quarter 30 employers have gone live with i-Connect equating to 78% of all active employers now supplying data monthly. A further 14 employers have now been onboarded since the agenda papers have been published.

Recruitment

Recruitment and retention remain a key factor impacting business operations with both member and employer services carrying vacancies (including maternity cover). Overall, the administration is approximately 88% resourced.

The Committee **RESOLVED** to note the Fund performance for the three months to 31st December 2022.

57 UPDATE ON LEGISLATION

The Technical & Compliance Advisor introduced the report to the Committee. She informed them of the two following recent announcements.

CARE Revaluation Date

A short consultation had been issued in February 2023 to move the annual in-service CARE revaluation date from 1 April to 6 April to align with the tax year and reduce the number of members who would potentially breach the annual allowance as a result of the 10.1% CPI increase being awarded.

This change will now come into force from 31st March 2023 and means that the revaluation of CARE will not be taken into account as part of the annual allowance calculation.

Our system provider, Heywood, have said that they are looking to have a procedure in place from May 2023 regarding this.

The change will impact a small number of members that change status between 1st – 5th April which may require some manual calculations from the Admin team. The LGA are due to provide guidance on this matter imminently.

Lifetime / Annual Allowance

It was announced by the Chancellor in the Spring Budget that the Lifetime Allowance would be abolished from 2024.

From April 2023 the Annual Allowance has been increased from £40,000 - £60,000.

Awaiting further information from the Treasury on both matters.

William Liew commented that he was aware that the NHS Pensions Team had already written to their members regarding the CARE revaluation and had updated their website.

The Technical & Compliance Advisor replied that they were awaiting further guidance from the LGA as to whether this was seen as a material impact and then a decision would be made on how this will be communicated to members.

Councillor Chris Dando commented that the Judicial Review (brought by the British Medical Association and the Fire Brigades Union) over the government proposed method of paying for costs incurred by the McCloud Judgment has now been dismissed.

The Committee **RESOLVED** to note the current position regarding the developments that could affect the administration of the fund.

58 RISK MANAGEMENT PROCESS & RISK REGISTER

The Governance & Risk Advisor introduced the report to the Committee. She outlined that a new risk framework had been introduced to assist risk owners to assess the risk and score, this was attached as Appendix 1, a high level matrix showing the distribution of risks by score was attached as Appendix 2 and the complete risk register was attached as Appendix 3.

She stated that following feedback from the Committee and Pension Board members pre-mitigation scores have also been added to the risk register.

She highlighted that the most critical risks were currently:

NR01 – 'Ability to deliver admin service to members and employers within agreed standards' - The current factors impacting this risk are set out in item 13 – Pension Fund Administration report.

NR12 – 'Failure to achieve decarbonisation targets in the required timescales in accordance with climate change priorities' - Government climate policies not moving fast enough or sufficiently enforced.

Councillor Shaun Stephenson-McGall said that he welcomed the changes that had been made to the risk register and thanked officers for their work on it.

The Committee **RESOLVED** to note the report.

59 GOVERNANCE

The Governance & Risk Advisor introduced the report to the Committee. She explained that there is an intention to move the Committee meetings to Friday mornings on the same dates as outlined in the report.

She said that the Committee are being asked to approve the proposal that members study and complete all Hymans Learning Academy modules within twelve months of becoming a Committee member.

The Chairman commented that he would like it to be made sure that any new Committee member receives robust training and induction.

The Committee **RESOLVED** to:

i) Approve the proposal for Committee members to study and complete all Hymans Learning Academy modules within twelve months of becoming a Committee member.
ii) Approve the proposal for Committee members to restudy and repeat the completion of the modules every three years.
iii) Note the Committee & Investment Panel workplans and training programme.

The meeting ended at 11.27 am

Chair(person) ....

Date Confirmed and Signed ....

Prepared by Democratic Services

Avon Pension Fund

Local Government Pension Scheme

Post: Avon Pension Fund, Bath & North East Somerset Council,
Lewis House, Manvers Street, Bath, BA1 1JG

Web: www.avonpensionfund.org.uk **Tel:** 01225 395100
Email: avonpensionfund@bathnes.gov.uk **Fax:** 01225 395258

23 March 2023

Dear Elaine,

May I thank you for the statement and questions submitted in person at the Avon Pension Fund Committee on 17 March 2023. I have addressed your questions below and expanded on some of the information I shared with you in my last letter.

1. **At what point you disengage due to lack of progress?**

We do not have a specific timeframe for divestment. However our investments are governed by Brunel's[1] Climate Policy which stipulates 100% of assets in high impact sectors in developed equities should be either i) achieving net zero or ii) meeting criteria considered to be aligning[2] by 2030. **Companies with a mere verbal commitment to achieving net zero by 2050 without a credible delivery plan or companies with no commitment will not form part of the portfolio beyond 2030.**

The challenge we face is complex and requires us to work with like-minded investors influencing companies to accelerate net zero ambitions and better manage climate change risks. We leverage our collective voice via Brunel and its appointed fund managers to assess the adequacy of company responses to the climate emergency using empirical tools such as the Transition Pathway Initiative, ClimateAction100+ Net Zero Company Benchmark and SBTi, accepting that many companies with credible decarbonisation pathways may still exhibit high carbon intensity today. Avon Pension Fund will update its position statement (enclosed) on the exclusion of investments on ESG grounds as part of its revised climate targets later in 2023.

2. **What evidence do you have to suggest that this strategy [engagement] is likely to work and what detailed plans you have in place to monitor progress?**

We have seen material success from ongoing engagement with the banking sector. Barclays published its updated climate plan in 2022 and gave shareholders an opportunity to vote on the bank's climate strategy. The bank has since adopted 2030 targets to reduce financed emissions across high impact sectors and aligned remuneration of executive directors with climate commitments.

Similarly Brunel's engagement with HSBC has led to targets and policy commitments designed to limit access to capital for companies unable to evidence net zero transition plans. The implementation of public commitments increases transparency and enables shareholders to hold banks, such as HSBC, to account for their actions.

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1 *Brunel Pension Partnership – through which Avon invests its assets*

2 Per the IIGCC Net Zero Investors Framework

However progress is not linear. External factors – such as the energy crisis – may create volatility in emissions. This is borne out by the case you cite in your letter of HSBC financing a temporary increase by RWE to use coal-fired power to shore up energy supply. It will take time for industries to implement technologies required to achieve net zero and we accept there will be years when financed emissions in some sectors temporarily rise. Brunel is continuing to engage positively with banks, and indeed high emitting sectors and companies more broadly, and notes material improvements in public commitments and policies.

3. **How closely are you monitoring the risk of being left with stranded assets of fossil fuels that will have to remain in the ground?**

The Fund holds c.£90m in fossil fuels overall, representing 1.4% of total assets. A large proportion of this capital is invested in companies and projects able to evidence credible decarbonisation pathways, hence limiting our exposure to stranded assets as such companies increasingly invest in climate resilient assets.

The Fund undertakes an independent annual review which seeks to identify companies that have both proven and probable fossil fuel reserves across the portfolio. Taking the reserves exposures, we can estimate future emissions that may result from these reserves being realised. Due to the nature of our investment strategy we would fully expect companies with legacy fossil fuel assets to be pivoting into new, sustainable revenue streams in order to generate the attractive risk-adjusted returns we seek for our members.

We enclose links below to the Brunel Climate Policy, along with a copy of the Fund's annual Responsible Investment Report, which contain further information on engagement efficacy and escalation and stranded asset risk.

Our climate objectives are kept under review and over the next year we will be assessing how we build on progress made to drive meaningful real-world impact whilst achieving the appropriate risk/return to meet our overriding objective to pay pensions. We will consult with a broad base of stakeholders throughout this process.

Thank you

Nathan Rollinson, Investments Manager, Avon Pension Fund
(On behalf of Cllr Paul Crossley, Chair of Avon Pension Fund Committee)

Brunel Climate Policy

APF Annual Responsible Investment Report

APF: Exclusion of Investments on Environmental, Social and Governance Grounds