Bath and North East Somerset Council

AVON PENSION FUND COMMITTEE

Minutes of the Meeting held

Friday, 9th December, 2011, 2.00 pm

Bath and North East Somerset Councillors: Paul Fox (Chair), Gabriel Batt, Nicholas Coombes, Charles Gerrish and Katie Hall

Co-opted Voting Members: Councillor Mary Blatchford (North Somerset Council), Councillor Mike Drew (South Gloucestershire Council), Councillor Mark Wright (Bristol City Council), Bill Marshall (HFE Employers), Rowena Hayward (Trade Unions) and Ann Berresford (Independent Member)

Co-opted Non-voting Members: Richard Orton (Trade Unions), Steve Paines (Trade Unions) and Paul Shiner (Trade Unions)

Advisors: John Finch (JLT Benefit Solutions) and Paul Middleman (Mercer)

Also in attendance: Andrew Pate (Strategic Director – Resources), Tony Bartlett (Head of Business, Finance and Pensions), Liz Feinstein (Investments Manager), Matthew Betts (Assistant Investments Manager), Steve McMillan (Pensions Manager), Alan South (Technical and Development Manager) and Martin Phillips (Finance & Systems Manager (Pensions))

39 EMERGENCY EVACUATION PROCEDURE

The Democratic Services Officer read out the procedure.

40 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

Apologies were received from Carolan Dobson and Councillor Clive Fricker.

41 DECLARATIONS OF INTEREST

There were none.

42 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

There was none.

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

A statement and two questions were received from Councillor David Willingham of Bristol City Council. A copy of these together with the Chair's replies is attached as an Appendix to these minutes.

A Member thought that it was not acceptable for the Fund to delegate voting decisions to its external investment managers and that it should have a policy on executive pay. Another agreed. The Chair commented that the Fund had two managers who voted on the Xstrata remuneration package, one of whom had abstained. He said that the issue of delegation of voting would be picked up in the Committee's review of Socially Responsible Investment.

Statement and questions from Cllr David Willingham, Bristol City Council

44 ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

There were none.

45 MINUTES: 23 SEPTEMBER 2011

The public and exempt minutes were approved as a correct record and signed by the Chair.

46 INTERIM ACTUARIAL VALUATION

Members had considered this item at the workshop that had immediately preceding the meeting.

A Member asked why gilt yields were used in the valuation process, as it was hardly likely that the whole fund would be sold in order to buy gilts. Mr Middleman replied that gilts were used as the basis to assess the value of the Fund in case of insolvency. At present gilt yields were driving up liabilities.

RESOLVED to note the information set out in the report.

47 RESPONSE TO CLG CONSULTATION ON SCHEME CHARGES

The Technical Development Manager presented the report.

The Department of Communities and Local Government had published a consultation paper on 7 October 2011 on achieving the savings required by the Comprehensive Spending Review of October 2010. The document covered scheme changes covering the period 1 April 2012 to 31 March 2015. In November 2011 the Treasury had released to Trade Unions basic proposals arising from the recommendations of the Hutton Review. Appendix 1 to the report contained a draft response to the DCLG consultation. It was also proposed that a letter be sent in response to the Treasury proposals highlighting a number of issues.

The Strategic Director of Resources and Support Services said that the DCLG consultation gave an opportunity to make a number of points clearly to the Government, namely that that public sector pensions should be sustainable and affordable and that the Local Government Pension Scheme was a funded scheme and so different from other public sector pension schemes.

A Member suggested that the Committee's response should accept an increase in the retirement age; this would be better than a rise in contributions or a decrease in benefits. Another Member, however, pointed out that if people worked longer, there would be fewer opportunities for young people to enter the work force and become Fund members. Another Member commented that while it was true that on average that people were living and remaining fit and healthy longer, it was difficult for pension schemes to cope with those who were below average.

A Member expressed concern that the changes in employees' contributions were being made to boost the revenue of the Treasury. The Chair pointed out that employers' contributions were being increased as well, and that in fact all contributions would be retained within the Fund. The Director of Resources and Support Services pointed out that while contribution levels were set by Government regulations, the LGPS was managed by the local government employers. There was no way the Treasury could take money out of the Fund.

The Director of Resources and Support Services suggested that access to pensions was an issue that should be emphasised in the response.

The Chair proposed that authority be delegated to him in consultation with officers to allow him to make presentational changes to the draft response and to incorporate points made by Members during the discussion. He also proposed that the words in paragraph 2.2 of the recommendation be deleted and replaced by

> "To copy the letter to the Fund employers and to invite them to consider whether they wished to respond to the consultation."

RESOLVED

1. To delegate to the Chair authority to amend the draft response letter to the DCLG consultation to include a summary of points made by Members during discussion and to incorporate presentational changes.

2. To copy the letter to the Fund employers and to invite them to consider whether they wished to respond to the consultation.

48 COMMUNITY ADMISSION BODIES

The Investments Manager presented the report. She pointed out that the Committee would need to go into exempt session before discussing Appendix 1.

It was noted that unguaranteed liabilities of Community Admission Bodies (CABs) is a legacy issue, because since December 2005 the Fund's policy has been only to admit a CAB if a guarantee has been put in place by a scheme employer.

A Member commented that it was reassuring that the liabilities of the CABs without guarantees and the consequent risk to the Fund were relatively low.

RESOLVED to note the information set out in the report.

49 INVESTMENT PANEL DRAFT MINUTES

RESOLVED to note the draft minutes of the Investment Panel meeting held on 22 November 2011.

50 REVIEW OF INVESTMENT STRATEGY

The Investments Manager presented the report. She said that the Investment Panel at their meeting on 22 November 2011 had received an update on the Eurozone situation from John Finch (contained in Appendix 2 of the report) and felt that Mr Finch's recommendation of a tactical switch from gilts to corporate bonds as a means of mitigating risk should be considered by the Committee at the earliest opportunity, as they felt they did not have sufficient information to make a substantive recommendation.

Mr Finch said that the situation in the Eurozone was changing by the day, if not by the minute. 18 months ago there had been talk of a downgrading of the UK's credit rating now the UK was the only major country whose AAA rating was not questioned. Gilt yields had fallen over the last 2-3 months, and could go lower. However, good companies had strong balance sheets. Though corporate bond yields had fallen, gilts had fallen even more and the gap between them had increased. A switch of 3.2% of the Fund's assets could be implemented quickly, giving flexibility in a volatile market.

Several Members spoke in favour of the proposal, but one Member expressed concerns about the desirability of switching in a highly volatile market.

[Councillor Batt left the meeting at this point.]

It was moved by Councillor Coombes and seconded by Councillor Gerrish and **RESOLVED** by 9 votes, with 1 abstention that having considered the proposal from JLT the Committee agrees:

i. the recommendation from JLT to tactically switch from UK government bonds (gilts) to sterling corporate bonds;
ii. the value to be switched is £80million (c. 3.2%) of the Fund's assets;
iii. the trigger point to reverse the tactical switch is when the corporate bond yield spread over the gilt yield falls to 1.2%.
iv. to delegate implementation to officers, subject to current conditions prevailing.

51 RECOMMENDATIONS FROM THE INVESTMENT PANEL

RESOLVED to agree the recommendation from the Investment Panel.

52 REVIEW OF INVESTMENT PERFORMANCE FOR QUARTER ENDING 30 SEPTEMBER 2011

The Assistant Investments Manager presented the report. He drew attention the information about cash management contained in paragraphs 7.5 and 7.6.

A Member suggested that the percentage of the Fund invested in emerging markets, which were likely to be the main drivers of world growth over the next five years, was quite low. The Investments Manager responded that the Investment Strategy had been reviewed in 2007 and the allocation to emerging markets had been increased. It was true that emerging markets were growth markets and that thought should be given to how the Fund could reflect this. However, there were issues in relation to emerging markets, such as the depth of the market for investors and how the growth potential translated into investment opportunities. A Member said that she recognised there was growth potential in emerging markets, but felt that because of volatility the Fund should not change any individual allocations without reviewing its whole strategy. Mr Finch suggested that the key was to look at the exposure of the global companies in which the Fund was invested; much depended on how these companies are exposed to emerging markets. A Member said that he had been surprised to learn of some of the countries in which the Fund was involved; what mattered was the quality of the companies invested in, not the countries. The Member who had raised the issue of emerging markets acknowledged that they could be volatile markets, but thought the Fund could benefit from growth in these markets while spreading its exposure. Another Member felt that there was a need to be careful about corporate governance issues in these markets.

RESOLVED to note the information set out in the report.

53 PENSION FUND ADMINISTRATION - BUDGET MONITORING FOR YEAR TO OCTOBER 2011 AND PERFORMANCE INDICATORS FOR QUARTER ENDING 30 OCTOBER 2011

The Finance & Systems Manager (Pensions) presented the budget report. He asked Members to note the increased forecast underspend for investment managers' fees, which reflected current market conditions.

The Pensions Manager presented the performance reports. He drew attention to the paragraph 5.5 (performance against target), noting that performance was acceptable, although marginally below target in some areas. Customer satisfaction was good. The level of opt-outs from the Fund had been low. Paragraph 8.2 gave information about how administration processes were amended in June 2011 to identify opt-outs in a reportable field; the current annual opt-out rate was only 0.29%, which was reassuring. There had been no complaints about service in the period.

Before the discussion of Appendix 7, which summarised the performance of Scheme Employers during the first 2 quarters of 2011, the following resolution was passed by 6 votes with 5 abstentions:

> *Having been satisfied that the public interest would be better served by not disclosing relevant information, the Committee resolves, in accordance with the provisions of Section 100(A)(4) of the Local Government Act 1972, that the public be excluded from the meeting for this item because of the likely disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Act as amended.*

Summarising the discussion on Appendix 7, the Chair said that the Committee's views should be communicated to underperforming employers when officers next met them, and that they should be told that it might be necessary to discuss their performance in open session if there was no improvement. The Pensions Manager observed that under the Administration Strategy there was a power to charge employers for any disproportionate work they caused for Pensions staff in comparison with other Fund employers.

The meeting returned to open session.

A Member congratulated Pensions staff for an excellent quarter's work, with costs significantly below budget. However he was concerned about outstanding workload being so close to target, and wondered whether this was due to failure to fill a staff vacancy. The Pensions Manager said that the post had not been deliberately left unfilled, but there had been recruitment difficulties.

Members noted the list of Academies given in Appendix 8. The Investments Manager said that the pensioner and deferred liabilities and sufficient assets to cover these liabilities are retained by the Unitary Authority employers. A Member asked the Investments Manager to report back to the Committee how the "old" Academies were treated on leaving the UAs.

RESOLVED to note the expenditure for administration and management expenses incurred for the year to 31 October 2011 and Performance Indicators for the 3 months to 31 October 2011 and Summary Performance report for the first two quarters 2011.

54 ANNUAL REVIEW OF INTERNAL CONTROL REPORTS OF EXTERNAL SERVICE PROVIDERS

The Investments Manager presented the report. She said that no issues had been identified and that these reports are also reviewed by the external auditors. The issue identified last year in relation to RLAM had been remedied.

RESOLVED to note the report and to request officers to continue to review the internal control reports and report to Committee on at least an annual basis.

55 WORKPLANS

The Pensions Manager drew attention to the strategy for communicating the proposed changes to LGPS benefits resulting from the Hutton review and the increase in contribution rates proposed by the Treasury (Appendix 2). The Chair asked that copies of communication plans be distributed to Members.

A Member asked what the timescale was for moving to electronic delivery of information to Fund members (Appendix 2). The Pensions manager said that every Fund member would be given three opportunities to state that they wished to continue to receive paper documents; it would take a couple of years to complete this process.

The Investments Manager agreed to include a review of investment strategy in the workplans, to be undertaken once the impact of the new scheme on the investment strategy can be assessed. This review will include infrastructure.

RESOLVED to note the workplans.

The meeting ended at 4.00 pm

Chair(person) ....

Date Confirmed and Signed ....

Prepared by Democratic Services

AGENDA ITEM 5: ITEMS FROM THE PUBLIC

Statement and questions from Cllr David Willingham, Bristol City Council, with responses to the questions from the Chair, Cllr Paul Fox

Statement – Avon Pension Fund Committee 2011-12-09

I am making this statement both as a member of the Avon Pension Fund, and as a Councillor on Bristol City Council.

I would like to start by thanking Officers at Bath & Northeast Somerset Council for their help and for providing me with information about voting activity of the fund, and to apologise that due to a prior Council commitment, I am unable to be present in person to present this statement.

I doubt that any member of this committee can be unaware of the Occupy protest in Bristol and the current zeitgeist against corporatism. This pension fund holds investments in many of the companies that have allowed their directors' remuneration packages to buck the current economic trend towards austerity.

Whilst in general there is little that Local Authorities can do to tackle corporate irresponsibility and excessive boardroom remuneration; through engagement with these companies, and by voting against excessive director remuneration, this pension fund does have some influence and could voice the frustration of its ordinary members at the extraordinary inflated remuneration packages of directors. The decision is whether you will choose to direct our pension fund to use that influence, or whether the status quo will be allowed to continue by inaction on this matter.

I suspect that most modestly salaried members of the Avon Pension Fund would be extremely angry if they were to discover that their pension fund voted in favour of a directors' remuneration report that saw a director's remuneration package soar to £18,426,105, but this has been allowed to happen!

Questions – Avon Pension Fund Committee 2011-12-09

Question 1 *It was reported by the BBC that Mick Davis of Xstrata received a remuneration package worth £18,426,105; it also appears that through TT International, the Avon Pension Fund voted to approve the Xstrata directors' remuneration report of 4.5.11. How does the Chair think that ordinary members of the Avon Pension Fund, on ordinary salaries will feel about their pension funds' involvement in approving this astronomical remuneration package?*

Response:

I recognise this is an important issue and whilst not knowing how all members feel, I can imagine some members would be very concerned about this level of remuneration and would want to know the Avon Pension Fund (APF or Fund) is looking after their interests as members of the Fund.

The Fund’s voting policy is to delegate the voting decision to the Fund's external investment managers. These managers have the knowledge, skills and resources to fully understand the context in which a company operates and therefore are better placed to be able to vote in the best interests of shareholders. In the UK, we request that managers vote in line with the UK Corporate Governance Code issued by the Financial Reporting Council and explain where they don't vote in line with it.

When deciding how to vote on the remuneration report, managers take into account how the remuneration policy is aligned with shareholder interests and the context in which the company operates (i.e. the business model and competitive environment in which it operates). APF’s investment managers have voted against remuneration reports proposed by various companies on several occasions.

In addition to voting, the APF can also seek to influence corporate behaviour through engagement with companies. The APF is a member of the Local Authority Pension Fund Forum (LAPFF) which actively engages with companies on behalf of local authority pension funds and uses the combined asset holding to influence company boards.

You will appreciate that the knowledge, skills and resources required to make informed decisions on every voting decision and to undertake effective engagement are considerable and that when the Committee decides on how to allocate its own resources it must take into account the best way of effectively influencing company behaviour whilst fulfilling its fiduciary duty to scheme employers to meet the financial obligations of the Fund.

Specifically in the case of Xstrata, TT provided a response to the Fund explaining that the remuneration report did not contain anything outside their voting guidelines and therefore they voted in favour. The Fund is looking into this as part of the current review of the Fund’s Responsible Investment Policy.

The Fund's other investment manager with a holding in Xstrata abstained when voting on the remuneration report because the manager was (and still is) actively engaging with the company on this issue.

Question 2 *Could the Chair please advise what actions the Avon Pension Fund will take to ensure that its voting record on director remuneration looks less like a corporate love-in, and instead reflects the “efficiency savings”, “austerity measures” or cuts, that Councils and their Officers are being forced to make?*

Response:

The Fund believes that by having a voting policy that seeks to maximise company value and returns, and by delegating this decision to those who are best placed to make it, it is acting in a way that minimises the potential financial burden on Employer bodies of meeting future pension benefit payments and therefore fully reflects the current drive for efficiency savings and austerity measures at Councils.

The Fund is also undertaking the following actions:

- The Fund has recently put in place a vote monitoring service that seeks to analyse voting activity at the aggregate Fund level, increasing disclosure and transparency and enabling better analysis of the voting activity undertaken by the managers on the Fund's behalf.

- The Fund is currently reviewing its Responsible Investment Policy including how the Fund can maximise its influence through voting and engagement with management on issues that affect shareholder value. For a Fund of our size, our ability to influence corporate behaviour is limited, thus greater collaboration on issues (for example via LAPFF) could be the most effective way for the Fund to influence corporate behaviour. It is anticipated this review will report to Committee during 2012 and any decision by the Committee will be taken within the context of the fiduciary duty of the Fund to employers to meet future benefits payments.

- You may be aware that there are a number of initiatives that are looking at the issues surrounding executive remuneration such as the Department for Business Innovation and Skills' discussion paper which provides a range of proposals to link executive pay more closely to company performance. LAPFF (of which the Fund is a member) is actively involved in this issue and will be submitting a response on behalf of members. In addition, LAPFF will continue to engage with individual companies on this issue.

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