Bath and North East Somerset Council

AVON PENSION FUND COMMITTEE

Minutes of the Meeting held

Friday, 23rd September, 2016, 2.00 pm

Bath and North East Somerset Councillors: David Veale (Chair), Cherry Beath, Shaun Stephenson-McGall and Lisa O'Brien

Co-opted Voting Members: Councillor Steve Pearce (Bristol City Council), Councillor Mary Blatchford (North Somerset Council), Councillor Mike Drew (South Gloucestershire Council), William Liew (HFE Employers), Ann Berresford (Independent Member), Shirley Marsh (Independent Member) and Wendy Weston (Trade Unions)

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

Advisors: Tony Earnshaw (Independent Advisor), Julie Masci (Grant Thornton), Paul Middleman (Mercer), Steve Turner (Mercer) and Sarah Wilson (Manifest)

Also in attendance: Tony Bartlett (Head of Business, Finance and Pensions), Liz Woodyard (Investments Manager), Matt Betts (Assistant Investments Manager), Geoff Cleak (Pensions Benefits Manager) and Martin Phillips (Finance & Systems Manager (Pensions))

26 EMERGENCY EVACUATION PROCEDURE

The Democratic Services Officer read out the procedure.

27 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

Apologies were received from Councillor Chris Pearce.

28 DECLARATIONS OF INTEREST

There were none.

29 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

There was none.

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

There were none.

31 ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

There were none.

32 MINUTES: 24TH JUNE 2016 AND 30TH JUNE 2016

The public and exempt minutes of the meetings of the 24th and 30th June 2016 were approved as a correct record and signed by the Chair.

33 APPROVAL OF FINAL ACCOUNTS

The Finance and Systems Manager presented the report. He introduced Julie Masci of Grant Thornton.

Ms Masci presented the Audit Findings for the Avon Pension Fund for year ended 31 March 2016. She drew attention to the summary of findings set out on page 6 of Appendix 2. The lack of separation of the journal entries for the APF and the Council identified in 2014/15 was not achieved in 2015/16, so it remained an issue for the 2015/16 audit. However, it was understood that complete separation had been achieved from 1st April 2016. There were two recommendations about minor issues.

A Member asked about section 9 on page 41 of the accounts (Change in Market Value of Investments), which appeared to show that the Fund had lost £85.5m during the year. The Investments Manager explained that Sterling had depreciated toward the end of the year, so some money had been lost on the currency hedge. The loss is offset by an increase in the value of hedged assets. In addition there was a timing issue relating to the sale of equity for reinvestment in infrastructure. The proceeds of the sale of the equities were invested on 1st April 2016, so that on 31st March they were still in the cash balances.

A Member asked why members' contributions to additional benefits were lower in 2015/2016 than in 2014/15. The Acting Pensions Manager suggested that as 2015/16 was the first year of the Career Average Revalued Earnings (CARE) scheme, there might have been an increase in Fund members deciding to pay for additional benefits in anticipation of this.

The Finance and Systems Manager (Pensions) invited the Committee to approve the Committee's Annual Report. He asked Members to note that figures would need to be inserted on agenda pages 107 and 109 when the CIPFA benchmarking data became available on 30 September. A Member suggested that information about TPR Trustee Toolkit training undertaken by Members should be included, as it was in the Pension Board Annual Report.

A Member asked about the increase in payments to and on account of leavers in of £2.86m in 2015/16 (agenda page 34). The Finance and Systems Manager (Pensions) explained that this was because of the transfer of Probation Service employees to the Greater Manchester Pension Fund.

RESOLVED:

1. To note the final audited Statement of Accounts for 2015/16.

2. To note the issues raised in the Annual Governance Report.

3. To approve the draft Avon Pension Fund Annual Report 2015/16.

34 APPROVAL OF FUNDING STRATEGY STATEMENT

The Investments Manager presented the report. She reminded Members that the draft FSS had been presented to the June Committee. It had then gone to employers for consultation. The Committee was now invited to approve the final FSS.

A Member asked whether it was normal to receive so few responses to a consultation on the FSS. The Investments Manager replied that it was a reasonable number of responses and that they came from a good selection of employers.

A Member asked about the insurance of ill-health costs referred to in paragraph 5.4 of the report (agenda page 143). The Investments Manager replied that the work had been started, but progress had been limited because of workload. She had had a conversation about it with the Actuary the previous day as how to progress the project.

A Member asked about the apparent conflict between 5.3(3), “the medium term recovery period will be held as 15 years rather than reduced to 12 years”, and 5.3(1)(b) “shorten the deficit recovery period by at least 3 years”. The Investments Manager explained that the aim was to manage affordability. If deficit recovery contributions should remain at the same level as determined in the 2013 valuation, this would lead to some employers’ deficits reducing by more than 3 years.

A Member suggested that with over 200 employers in the Fund the proposal in 5.3(2) for “employer specific” short term pay assumptions might be impracticable. Mr Middleman responded that he needed feedback from employers about their pay assumptions, which differed for different types of employer. This did not mean that there would be individual pay assumptions for each individual employer. Pay assumptions needed to be refined to maintain affordability and there might be two or three different options for employers.

RESOLVED:

1. To note the feedback responses received, and the proposed modifications to the draft FSS.

2. To approve the Funding Strategy Statement as set out in Appendix 1, subject to the insertion of information which can only be included when the actuarial valuation is complete, for general publication and distribution to the Fund’s employing bodies.

3. To delegate the refinement and finalisation of the draft FSS to Fund Officers, with the assistance of the Fund Actuary.

35 GAD SECTION 13 REPORT

The Investments Manager presented the report, which she said was for information only.

A Member noted that GAD had flagged up the long-term cost-efficiency of the Somerset County Council Pension Fund as something about which they might have engaged with the administering authority under section 13 of PSPA 2013, had it been in force at the time the dry run had been undertaken. He asked whether the Committee should be concerned now that Somerset was a member of Project Brunel. The Head of Business, Finance and Pensions replied that the issue with Somerset CC Pension Fund was funding; it was a strategic issue which should concern only the Somerset CC Pension Fund Committee. Pooling only related to operational issues; the pool managers would implement the strategies of the member funds.

A Member asked whether the maturity rank of the Fund, 5.9(82) was something to be worried about. Mr Middleman said that this indicated the Fund had a lot of pensioners and was cashflow negative, but it was only one of a number of measures and was not by itself a cause for concern. The result of the valuation was more important.

A Member asked about the level of non-statutory employees in the Fund, which at 6% was quite high. Mr Middleman said that he did not think that the number was really the right measure of risk. The Fund had for some years insisted on covenants and bonds for admitted bodies. There was also a need for the right sort of monitoring between valuations.

RESOLVED to note the Section 13 Dry Run Report.

36 ANNUAL RESPONSIBLE INVESTING REPORT

The Assistant Investments Manager presented the report.

Sarah Wilson presented the Manifest Monitoring Review of Shareholder Voting 2015 for the Avon Pension Fund. She reported that the number of meetings voted at by the Fund's managers in 2015 was 905, down from 1,166 in 2014, comprising a total of 13,532 resolutions (compared with 17,711 in 2014). The bulk of the meetings took place in the period April-June. The Fund's managers supported 96.25% of the recommendations of company management. She drew attention to the comparison of manager voting patterns in section 5.1 of the report (agenda pages 267-269).

[Councillor Mike Drew joined the meeting.]

A Member said that he was concerned that some companies might be overvaluing their assets, which might include stranded assets, and that they should be challenged to demonstrate that the asset values they were claiming were justified. Ms Wilson said this was an important issue, but it should be remembered that accounting standards were set by independent organisations, such as the International Accounting Standards Board. Therefore, the first thing on which to seek assurance was that companies were properly audited and that they were complying with accounting standards. As far as stranded assets were concerned, it should be noted that these were not covered by current accounting standards, which relate only to financial assets. There were initiatives to encourage companies to address the issue of stranded assets. The Member said that he thought that the important influence on companies was the bottom line, and that investors should keep probing and not let companies think they were going to forget about this issue.

A Member asked how companies could be encouraged to address the challenges and opportunities arising from environmental change. The Assistant Investments Manager said this would be taken into account in the review of responsible investing; there would be two more meetings on the review with the outcome reported to the Committee in December. The Member asked whether the fact that Jupiter was fossil free at the time the report was written was due to accident or design. The Assistant Investments Manager replied that it was by design; the Jupiter mandate was the only mandate that had exclusions. It should be noted, however, that while Jupiter had achieved their performance targets over the recent period, because of the exclusions they have in the UK index they have had volatile performance versus the benchmark over time; this will be taken into account in the review. Ms Wilson pointed out that under Regulations issued in 2013 under the Companies Act 2006 all companies now have to report their greenhouse gas emissions, so that is possible to calculate the carbon impact of portfolios.

A Member asked whether it was acceptable that there was such a wide variation in managers' voting against the Template for Management and that so many managers did not publish how they had voted. Ms Wilson replied that Manifest did not expect all managers to follow best practice 100%; they had to exercise their individual judgments. As far as disclosure of their voting was concerned, they might not do this in public, but they did disclose to the Fund.

In conclusion Ms Wilson said that in the UK constructive dialogue with company boards was encouraging them to be more open, whereas in the United States, where companies had faced an aggressive environment, legislation was going through the House to prevent discussion of company failings and shortcomings. It should be remembered that some fund managers had no training in ESG and SRI issues and were on a learning curve.

RESOLVED:

1. To approve the annual Responsible Investing Report for 2015/16;

2. To approve the Fund's Statement of Compliance with the Stewardship Code in section 3 of Appendix 1.

37 REPORT ON INVESTMENT PANEL ACTIVITY

The Assistant Investments Manager informed the Committee that the Panel had made no decisions or recommendations.

RESOLVED to note the minutes of the Investment Panel meeting on 5 September at Appendix 1 and the summary of the Meet the Managers Workshop at Exempt Appendix 2.

38 REVIEW OF INVESTMENT PERFORMANCE

he Assistant Investments Manager presented the report. He said that it had been a positive quarter, though managers had struggled in a volatile environment. Depreciation of Sterling had had a negative impact. The funding level had risen to 85% because of asset performance. The Statement of Investment Principles (SIP) had been updated to reflect changes made to the bond portfolio and the funding of the IFM infrastructure mandate; the Committee was invited to approve the revised SIP.

Mr Turner presented the Mercer Investment Performance Report. He said that it in general had been a good quarter. He expected that the effect of Brexit would not be clear for a few years. Equities had recovered after an initial sharp fall. Sterling had fallen by 15% and he believed there was still a strong rationale for maintaining the currency hedging policy. Because of the new way of calculating the deficit, there was less reason to be concerned about gilt yields. He was comfortable with the performance of the majority of fund managers. The development of the proposals for a liability-driven investment framework was on track and that Mercer would soon be able to recommend a manager.

A Member said that she was concerned to see that the relative 3 year return (agenda page 350) was sinking ever lower and that so many managers had not achieved their targets on 3-year performance (agenda page 353). She asked whether there were any actions that the Fund could take to improve returns. Mr Turner said that he expected recent underperformance to correct itself. There was uncertainty in the market because of the US election. Much of the current underperformance of managers was due to currency. JP Morgan (Fund of Hedge Funds) had delivered a massive return because of currency. Extreme movements of currency can take place in a very short period of time. The rationale for currency hedging had been accepted at the last Panel meeting.

RESOLVED:

1. To note the information set out in the report.
2. To note LAPFF Quarterly Engagement Report at Appendix 4;
3. To approve the revised Statement of Investment Principles at Appendix 5.

39 APPROVAL OF COMMITTEE'S ANNUAL REPORT TO COUNCIL AND TO NOTE PENSION BOARD REPORT TO COUNCIL

The Investments Manager presented the report. She invited the Committee to approve the Committee’s Annual Report and to note the first Annual Report of the Local Pension Board. These would be submitted to Council in November.

A Member was struck by the large amount, £2.21 per member against the CIPFA average of £0.78, invested by the Fund in communications (agenda page 394). She wondered whether this level of spend was justified by the benefits, particularly since the uptake of electronic services by members had not increased as much as had been hoped. The Head of Business, Finance and Pensions responded that it was true the Fund had invested heavily in IT and communications, and was trying to expand electronic communications as much as possible. This was a painful process, because there were so many employers and members in the Fund. Other funds were beginning to invest more in IT and he felt that the CIPFA figures did not accurately reflect the true position. Another Member said that she thought it was important to invest in communications with Fund members. She was not sure that at present members were reading and understanding information sent to them by the Fund and suggested that thought needed to be given to how to target information relevant to specific categories of member. The Acting Pensions Manager said that a key part of the IT Strategy was to increase the uptake of Member Self-Service.

RESOLVED:

1. to approve the 2016 Annual Report to Council 2016;

2. to note the Local Pension Board Annual Report.

40 BUDGET AND CASHFLOW MONITORING 2016/17

The Finance and Systems Manager (Pensions) presented the report.

RESOLVED to note:

1. the administration and management expenditure incurred for 4 months to 31 July 2016.

2. the budget for stage 3a of the pooling project;

3. the Cash Flow Forecast to 31 March 2017.

41 PENSION FUND ADMINISTRATION

The Acting Pensions Manager presented the report.

A Member said that she was impressed by the progress of the Data Improvement Plan; the Annual Report, covering the year up to 31 March, reported data as 96% complete, whereas the figure at 30 June was 99.36% complete.

A Member said that the Actuary would need to take into account the big fall in the number of employees that would follow redundancies at Bristol City Council. The Head of Business, Finance and Pensions said that this would be picked up in the impact on payroll contributions. What was important for the valuation was the amount coming in contributions, not the number of employees in any employer.

A Member praised the two APF staff who worked non-stop for 4 hours at an Options Day, and thanked them for the fantastic job they had done.

A Member said that the table of key performance indicators did not show by how much the targets had been missed and what the size of backlogs were. The Acting

Pensions Manager said that the new form of performance report to be introduced would show this and would comment on the reason for failing to achieve the target.

RESOLVED to note:

1. Summary Performance Report and Performance Indicators to 30 June 2016.

2. Progress on the Data Improvement Plan.

3. Risk Register.

42 LGPS REGULATORY UPDATE

The Acting Pensions Manager presented the report.

The Investments Manager gave an update on pooling. She advised that the Government has established a review panel to consider all pooling proposals. Representatives from the Brunel partnership had met the panel and though no formal feedback had been received, information had been received from the LGA that the panel had been had been assured by the thoroughness of the proposal and by the detailed legal work that had been done. The deadline for presenting the proposals to all the Councils in the partnership was February 2017, and the target date for the investment company to begin operations was 1st April 2018. The DCLG had indicated that the revised Investment Regulations will be presented to the Secretary of State for signing in September, and should be laid before the House of Commons by the end of October or early November.

The Head of Business, Finance and Pensions said that it had been hoped that a special meeting of the Council could be convened to approve the creation of the investment company, but this did not now appear possible. It appeared that the proposal would now have to go to Council in February 2017, as the first item on the agenda of the annual budget meeting. Bath and North East Somerset would the last Council in the partnership to consider the proposal. The proposal would be put to the Committee in December. The Committee’s comments and decision would be reported to Council in February.

A Member asked if, given the complexity of the issues, briefings could be arranged for all Councillors before the February meeting. The Head of Business, Finance and Pensions said that briefings would have to be arranged for Cabinet and the Group Leaders and consideration would be given to how these could be extended to other Councillors.

RESOLVED to note:

1. the current position regarding the potential changes that would affect the administration of the Fund;

2. the current position regarding HM Treasury consultations and pending commencement dates.

3. the verbal update on the pooling of assets.

43 WORKPLANS

The Investments Manager presented the report.

RESOLVED to note the workplans and training programme for the relevant periods.

The meeting ended at 3.53 pm

Chair(person) ....

Date Confirmed and Signed ....

Prepared by Democratic Services