



Meeting of the

PENSIONS COMMITTEE

Thursday, 17 February 2011 at 7.30 p.m.

A G E N D A

VENUE

C1, 1ST FLOOR, TOWN HALL, MULBERRY PLACE

Members:

Chair: Councillor Anwar Khan
Vice – Chair: Councillor Shafiqul Haque

Councillor Craig Aston
Councillor Mohammed Abdul Mukit
MBE
Councillor Shiria Khatun
2 Vacancies
1 Vacant Post - Non-Voting Member
(Trade Union)
1 Vacant Post - Non-Voting Member
(Admitted Body)

Deputies (if any):

Councillor Tim Archer, (Designated
Deputy representing Councillor Craig
Aston)
Councillor David Snowdon, (Designated
Deputy representing Councillor Craig
Aston)
Councillor Zenith Rahman, (Designated
Deputy representing Councillors Anwar
Khan, Shafiqul Haque, Shiria Khatun and
Mohammed Abdul Mukit, MBE)

[Note: The quorum for this body is 3 Members].

If you require any further information relating to this meeting, would like to request a large print, Braille or audio version of this document, or would like to discuss access arrangements or any other special requirements, please contact: Daniel Hudson, Democratic Services
Tel: 020 7364 4881, E:mail: daniel.hudson@towerhamlets.gov.uk

LONDON BOROUGH OF TOWER HAMLETS

PENSIONS COMMITTEE

Thursday, 17 February 2011

7.30 p.m.

1. APOLOGIES FOR ABSENCE

To receive any apologies for absence.

2. DECLARATIONS OF INTEREST (Pages 1 - 2)

To note any declarations of interest made by Members, including those restricting Members from voting on the questions detailed in Section 106 of the Local Government Finance Act, 1992. See attached note from the Chief Executive.

3. UNRESTRICTED MINUTES (Pages 3 - 6)

To confirm as a correct record of the proceedings the unrestricted minutes of the meeting held on 18th November 2010.

4. DEPUTATIONS & PETITIONS

To receive any deputations or petitions

5. UNRESTRICTED REPORTS FOR CONSIDERATION

5.1 Report of the Investment Panel - Quarter Ending 30/09/10 (Pages 7 - 14)

5.2 Hutton Commission (Pages 15 - 22)

6. ANY OTHER UNRESTRICTED BUSINESS CONSIDERED TO BE URGENT

Agenda Item 2

DECLARATIONS OF INTERESTS - NOTE FROM THE CHIEF EXECUTIVE

This note is guidance only. Members should consult the Council's Code of Conduct for further details. Note: Only Members can decide if they have an interest therefore they must make their own decision. If in doubt as to the nature of an interest it is advisable to seek advice **prior** to attending at a meeting.

Declaration of interests for Members

Where Members have a personal interest in any business of the authority as described in paragraph 4 of the Council's Code of Conduct (contained in part 5 of the Council's Constitution) then s/he must disclose this personal interest as in accordance with paragraph 5 of the Code. Members must disclose the existence and nature of the interest at the start of the meeting and certainly no later than the commencement of the item or where the interest becomes apparent.

You have a **personal interest** in any business of your authority where it relates to or is likely to affect:

- (a) An interest that you must **register**
- (b) An interest that is not on the register, but where the well-being or financial position of you, members of your family, or people with whom you have a close association, is likely to be affected by the business of your authority more than it would affect the majority of inhabitants of the ward affected by the decision.

Where a personal interest is declared a Member may stay and take part in the debate and decision on that item.

What constitutes a prejudicial interest? - Please refer to paragraph 6 of the adopted Code of Conduct.

Your personal interest will also be a prejudicial interest in a matter if (a), (b) and either (c) or (d) below apply:-

- (a) A member of the public, who knows the relevant facts, would reasonably think that your personal interests are so significant that it is likely to prejudice your judgment of the public interests; AND
- (b) The matter does not fall within one of the exempt categories of decision listed in paragraph 6.2 of the Code; AND EITHER
- (c) The matter affects your financial position or the financial interest of a body with which you are associated; or
- (d) The matter relates to the determination of a licensing or regulatory application

The key points to remember if you have a prejudicial interest in a matter being discussed at a meeting:-

- i. You must declare that you have a prejudicial interest, and the nature of that interest, as soon as that interest becomes apparent to you; and
- ii. You must leave the room for the duration of consideration and decision on the item and not seek to influence the debate or decision unless (iv) below applies; and

- iii. You must not seek to improperly influence a decision in which you have a prejudicial interest.
- iv. If Members of the public are allowed to speak or make representations at the meeting, give evidence or answer questions about the matter, by statutory right or otherwise (e.g. planning or licensing committees), you can declare your prejudicial interest but make representations. However, you must immediately leave the room once you have finished your representations and answered questions (if any). You cannot remain in the meeting or in the public gallery during the debate or decision on the matter.

LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE PENSIONS COMMITTEE

HELD AT 7.30 P.M. ON THURSDAY, 18 NOVEMBER 2010

**C1, 1ST FLOOR, TOWN HALL, MULBERRY PLACE, 5 CLOVE CRESCENT,
LONDON E14 2BG**

Members Present:

Councillor Anwar Khan (Chair)
Councillor Craig Aston
Councillor Shafiqul Haque

Others Present:

John Gray (Unison)
Frank West (GMB)

Officers Present:

Alan Finch – (Service Head, Corporate Finance, Resources)
Oladapo Shonola – (Chief Financial Strategy Officer, Resources)
Alan Ingram – (Democratic Services)

1. ELECTION OF VICE-CHAIR FOR THE MUNICIPAL YEAR 2010/2011

Councillor Shafiqul Haque **moved**, the Chair **seconded** and it was

RESOLVED

That Councillor Shafiqul Haque be elected Vice-Chair of the Pensions Committee for the remainder of the Municipal Year 2010-2011.

2. APOLOGIES FOR ABSENCE

Apologies for absence were received on behalf of Councillor Mohammed Abdul Mukit MBE.

3. DECLARATIONS OF INTEREST

No declarations of interest were made.

4. UNRESTRICTED MINUTES

The Chair **Moved** and it was

RESOLVED

That the unrestricted minutes of the ordinary meeting of the Pensions Committee held on 5th August 2010 be approved and signed by the Chair as a correct record of the proceedings.

5. DEPUTATIONS & PETITIONS

Nil items.

6. UNRESTRICTED REPORTS FOR CONSIDERATION**6.1 LGPS (Management and Investment of Funds) Regulation 2009**

The Chief Financial Strategy Officer introduced the report. In response to queries he confirmed that proposals to co-mingle cash assets would ensure the best possible returns on investments.

RESOLVED

- (1) That the operation of a separate bank account be approved to hold monies held and received on behalf of the Pension Fund to ensure pension fund cash assets are clearly ring-fenced from other monies of the Council.
- (2) That pension fund cash assets continue to be co-mingled with Council Treasury assets to ensure efficient and effective treasury management.
- (3) That pension fund cash assets be invested on a co-mingled basis to ensure that pension fund cash enjoys the same economic rights and return as Council cash assets.

6.2 Absolute Return Manager Interviews

The Service Head, Corporate Finance, Resources introduced the item and clarified the process and reasons for the appointment of an absolute return manager for the Pension Fund.

RESOLVED

- (1) That Ruffer LLP and Baillie Gifford be appointed to manage absolute manager portfolios for the Fund and that £70m (£35m each) be transferred from cash held and existing equity holdings to fund the mandates.
- (2) That the contracts referred to in (1) above be completed to the satisfaction of the Assistant Chief Executive (Legal Services).

6.3 Investment Panel for Quarter Ending 30 September 2010

The Service Head, Corporate Finance, Resources presented the report and commented that references to the quarter ending 30 September should be replaced throughout the report by the quarter ending 30 June. The results of the quarter ending 30 September would be reported to the next meeting of the Committee.

He then commented on the performance of the Fund and, in response to queries, confirmed that volatility in the economies of Ireland and Portugal had the potential to have a knock-on effect on other economies which would not be a positive effect on markets. However, all efforts would be made to minimise losses in that scenario.

RESOLVED

That the report be noted.

6.4 2009/10 Local Government Pension Fund Annual Report

The Chief Financial Strategy Officer introduced the Pension Fund Annual Report, which had been audited and contained minor amendments to the version presented to the Committee on 5th August 2010. The report would now be published before the due date of 1st December 2010.

RESOLVED

That the report be noted.

7. ANY OTHER UNRESTRICTED BUSINESS CONSIDERED TO BE URGENT

7.1 LAPFF Annual Conference

The Chair stated that this conference would be held from 1st to 3rd December in Bournemouth and would be attended by the Chief Financial Strategy Officer. The Chair regretted that he would be unable to attend but pointed out that two further places were available for representatives of the Council.

Mr John Gray (Unison) indicated that he would be prepared to attend and agreed to provide an update at the next meeting of the Committee.

7.2 Awards Evening

The Chair indicated that he would provide an update of the event at the next meeting of the Committee.

The meeting ended at 8.00 p.m.

Chair, Councillor Anwar Khan
Pensions Committee

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Agenda Item 5.1

COMMITTEE: Pensions Committee	DATE: 17 February 2011	CLASSIFICATION: Unrestricted	REPORT NO.	AGENDA NO.
REPORT OF: Corporate Director of Resources		TITLE: Report of Investment Panel for Quarter Ending 30 September 2010.		
ORIGINATING OFFICER(S): Oladapo Shonola – Chief Financial Strategy Officer		Ward(s) affected: N/A		

Lead Member	
Community Plan Theme	All
Strategic Priority	One Tower Hamlets

1. SUMMARY

- 1.1 This report informs Members of the activities of the Investment Panel and the performance of the Fund and its investment managers for the period ending 30 September 2010.
- 1.2 In the quarter to the end of September 2010 the Fund achieved a return of -8.2% which is 0.9% above the benchmark. The twelve month Fund return of 9.0% slightly underperformed the benchmark return at 10.0%. For longer periods, performance continued to lag behind the benchmark with the three years return of 0.3% underperforming the benchmark return of 1.0% by 0.7% and the five years return of 4.1% underperforming the benchmark return of 4.8% by 0.7%.
- 1.3 The performance of individual managers although varied, was mostly positive this quarter. Five managers matched or achieved returns above the benchmark whilst the remaining two were below. The variability of returns does however partially reflect the management structure of the fund where complementary investment styles reduce the volatility of returns.
- 1.4 The distribution of the Fund amongst the different asset classes is broadly in line with the benchmark.

2. DECISIONS REQUIRED

- 2.1 Members are recommended to note the contents of this report.

3. REASONS FOR DECISIONS

- 3.1 There are no decisions to be made as a result of this report. The report is written to inform panel members of the performance of pension fund managers and the overall performance of the Tower Hamlets Pension Fund. The report also updates the Committee on the activities of the Investment Panel.

4. ALTERNATIVE OPTIONS

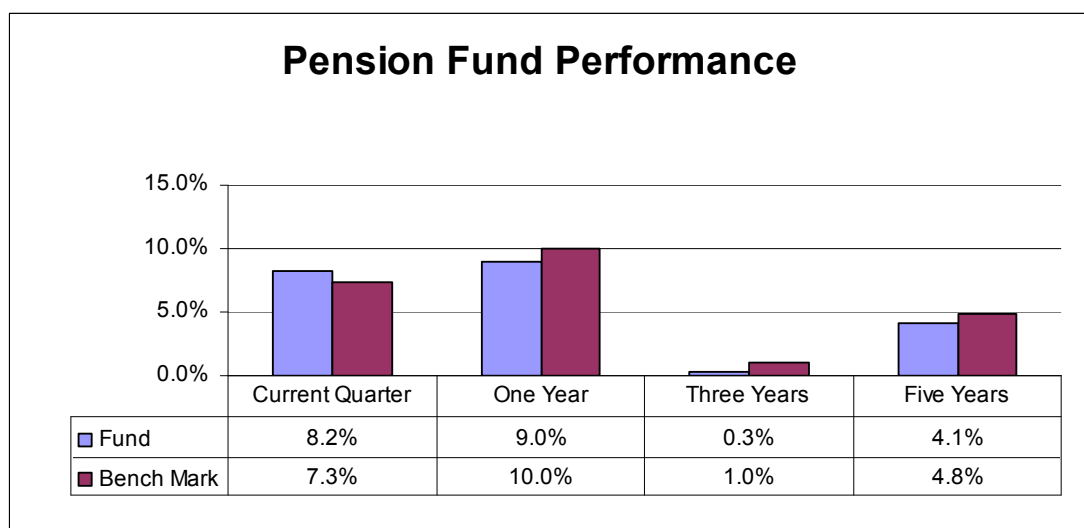
- 4.1 The Pension Fund Regulations requires that the Council establishes arrangements for monitoring the investments of the Pension Fund.

5. BACKGROUND

- 5.1 The Pension Fund Regulations require that the Council establish arrangements for monitoring the investments of the Fund and the activities of the investment managers and ensure that proper advice is obtained on investment issues.
- 5.2 This Committee has established the Investment Panel, which meets quarterly for this purpose. The Panel's membership comprises all Members of the Pensions Committee, an Investment Professional as Chair, an Independent Financial Adviser, and the Corporate Director of Resources represented by the Service Head Corporate Finance, two trade union representatives and one representative of the admitted bodies. The Investment Panel is an advisory body which makes recommendations to the Pensions Committee which is the decision making body.
- 5.3 This report informs Members of the activities of the Investment Panel and performance of the Fund and its investment managers for the period ending 30 September 2010.

6 INVESTMENT PERFORMANCE

- 6.1 The Fund achieved a return of 8.2% which is 0.9% above the benchmark.
- 6.2 The performance of the fund over the longer term is as set out in table 1.



- 6.3 The chart clearly demonstrates the volatility and cyclical nature of financial markets, but the outcomes are within the range of expectations used by the Fund actuary in assessing the funding position. The Fund can take a long term perspective on investment issues principally because a high proportion of its pensions liabilities are up to sixty years in the future. Consequently it can effectively ride out short term volatility in markets.

7. MANAGERS

7.1 The Fund currently employs seven specialist managers with mandates corresponding to the principal asset classes. The managers are as set out below:

Table 2: Management Structure

Manager	Mandate	Value £M	Target % of Fund	Actual % of Fund	Difference %	Date Appointed
GMO	Global Equity	194.5	25.0%	26.0%	1.0%	29 Apr 2005
Baillie Gifford	Global Equity	133.0	16.0%	17.8%	1.8%	5 Jul 2007
L & G UK Equity	UK Equity	164.8	22.5%	22.0%	-0.5%	02 Aug 2010
L & G Index Linked-Gilts	UK Equity	52.8	7.0%	7.0%	0.0%	02 Aug 2010
Investec Bonds	Bonds	96.0	14.0%	12.8%	-1.2%	26 Apr 2010
Schroder	Property	88.2	12.0%	11.8%	-0.2%	30 Sep 2004
Record	Currency	5.4	1.5%	0.7%	-0.8%	2 Sep 2008
Cash	Currency	14.3	2.0%	1.9%	-0.1%	
Total		749.0	100.0%	100.0%	0.0%	

7.2 The fund value of £749.0 million held by the managers has increased by £69.7 million (10.26%) over the quarter.

7.3 The performance of the individual managers relative to the appropriate benchmarks over the past five years is as set out in table 3.

Table 3: Manager Investment Performance relative to benchmark

Manager	Current Quarter	One Year	Three Years	Five Years
GMO	0.80%	0.20%	0.00%	-0.30%
Baillie Gifford	2.30%	6.10%	3.10%	2.70%
L & G UK Equity	0.00%	N/A	N/A	N/A
L & G Index Linked-Gilts	0.00%	N/A	N/A	N/A
Investec Bonds	1.50%	-3.00%	N/A	N/A
Schroder	-0.40%	-4.30%	-1.10%	0.60%
Record	-3.30%	-31.20%	-25.20%	N/A
Total Variance (Relative)	0.90%	-1.00%	-0.70%	-0.70%

7.4 **GMO's** performance over the quarter was strong in absolute terms as global equity markets posted strong gains. GMO also outperformed their benchmark in relative terms by 0.8%. Country allocation had a mixed effect with gains, particularly from the overweight position to Emerging Markets and also the UK, offset by being overweight Japan and underweight Australia. Stock selection was also positive, with the value-oriented and momentum driven strategies contributing positively.

- 7.5 **Baillie Gifford** Performance continues to be strong, significantly ahead of benchmark over the quarter (2.3%), year and since inception. Baillie Gifford continue to have a strong belief in the theme of emerging markets growth and that structural changes in emerging markets will continue for several years. This exposure continues to be a significant driver of performance. They are optimistic about technological change and scientific progress and have added holdings to capture this such as Roche (new drug technologies), Namco Bandai (new gaming technology).
- 7.6 **L & G (UK Equity)** performance has been in line with the index benchmark (FTSE-All Share) since inception, as expected.
- 7.7 **L & G Index Linked Gilts** performance has been in line with the index benchmark (FTSE-A Index-Linked Over 15 Years Gilts) since inception.
- 7.8 **Schroder (property)** the key drivers of recent underperformance have been costs of acquisitions and the cash holding during the investment phase. The Continental European Fund has also underperformed in comparison to the UK (over the last year but actually outperformed last quarter). The cash balance is now below 5%.
- 7.9 **Investec (Bonds)** recovered in quarter 3 following a disappointing start to the appointment outperforming the benchmark by 1.5%. Exposure to emerging market debt was a positive and currency selection was also beneficial.
- 7.10 **Record** performance for Q3 2010 was disappointing again. Although Record still believes in the strategy for the long-term, it is unable to give any indication as to when we are likely to see a turnaround in performance. Their view is that as developed countries are trying to reduce their deficits through raising taxes and becoming more self-sufficient they are unlikely to allow their currencies to appreciate.

The Panel decided at its last meeting to disinvest funds from Record and use the receipt to fund the newly awarded absolute return mandates. Officers have prepared a transition plan which details transfer assets between managers and how the new mandate will be funded. It is expected that disinvestment from Record will be complete by the end of the month.

8 ASSET ALLOCATION

- 8.1 The allocation of investments between the different asset classes was determined in conjunction with the Councils professional advisors in 2004 and is subject to periodic review by the Investment Panel. Recent reviews have led to the appointment of a passive manager and the Fund is the process of appointing an absolute manager. Asset allocation is determined by a number of factors including:-
- 8.1.1 The risk profile. Generally there is a trade-off between the returns obtainable on investments and the level of risk. Equities have higher potential returns but this is achieved with higher volatility. However, as the Fund remains open to new members and able to tolerate this it can seek long term benefits of the increased returns.
- 8.1.2 The age profile of the Fund. The younger the members of the Fund are the longer the period before pensions become payable and investments have to be realised for this purpose. This enables the Fund to invest in more volatile asset classes because it has

the capacity to ride out adverse movements in the investment cycle.

8.1.3 The deficit recovery term. All Council funds are in deficit because of falling investment returns and increasing life expectancy. The actuary determines the period over which the deficit is to be recovered and considers the need to stabilise the employer's contribution rate. The actuary has set an eighteen year deficit recovery term for this Council which enables a longer term investment perspective to be taken.

8.2 The benchmark asset distribution and the position at the 30 Sept 2010 are as set out below:

Table 4: Asset Allocation

	Benchmark 30 Sep 2010	Fund Position	Variance as at 30 Sep 2010	Variance as at 31 Mar 2010
	%	%	%	%
UK Equities	26.5%	27.5%	1.0%	1.1%
Global Equities	37.0%	37.6%	0.6%	1.0%
Total Equities	63.5%	65.1%	1.6%	-2.1%
Property	12.0%	12.4%	0.4%	1.1%
UK Bonds	14.0%	12.8%	-1.2%	-0.7%
Overseas Bonds	0.0%	0.0%	0.0%	-2.0%
UK Index Linked	7.0%	7.0%	0.0%	-1.3%
Cash	2.0%	1.9%	-0.1%	2.8%
Currency	1.5%	0.8%	-0.7%	0.1%
Total Equities	100.0%	100.0%	0.0%	0.0%

8.3 Individual managers have discretion within defined limits to vary the asset distribution.

8.4 In addition the distribution will vary according to the relative returns of the different asset classes. Equity markets have been recovering over the past several months and indexes are now nearing pre-recession levels. This has corrected the temporary distortion in the distribution of assets, so that the actual distribution of assets is similar to targets.

9. COMMENTS OF THE CHIEF FINANCIAL OFFICER

9.1. The comments of the Corporate Director Resources have been incorporated into the report.

10. CONCURRENT REPORT OF THE ASSISTANT CHIEF EXECUTIVE (LEGAL)

10.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 require the Council, as an administering authority, to invest fund money that is not needed immediately to make payments from the Pensions Fund. The Council is required to have a policy in relation

to its investments and a Statement of Investment Principles. The Council is required to take advice about its investments.

- 10.2 The Council does not have to invest the fund money itself and may appoint one or more investment managers. Where the Council appoints an investment manager, it must keep the manager's performance under review. At least once every three months the Council must review the investments that the manager has made and, periodically, the Council must consider whether or not to retain that manager.
- 10.3 One of the functions of the Pensions Committee is to meet the Council's duties in respect of investment matters. It is appropriate, having regard to these matters, for the Committee to receive information about asset allocation and the performance of appointed investment managers.

11. ONE TOWER HAMLETS CONSIDERATIONS

- 11.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.
- 11.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

12. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

- 12.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

13. RISK MANAGEMENT IMPLICATIONS

- 13.1 Any form of investment inevitably involves a degree of risk.
- 13.2 To minimise risk the Investment Panel attempts to achieve a diversified portfolio. Diversification relates to asset classes and management styles.

14. CRIME AND DISORDER REDUCTION IMPLICATIONS

- 14.1 There are no any crime and disorder reduction implications arising from this report.

15. EFFICIENCY STATEMENT

- 15.1 The monitoring arrangement for the Pension Fund and the work of the Pension Fund Investment Panel should ensure that the Fund optimises the use of its resources in achieving the best returns for members of the Fund.

LOCAL GOVERNMENT ACT 1972 (AS AMENDED) SECTION 100D LIST OF "BACKGROUND PAPERS" USED IN THE PREPARATION OF THIS REPORT

Brief description of "background papers"

Review of Investment Managers' Performance for the 3rd Quarter Report – prepared by Hymans Robertson LLP

***Name and telephone number of holder
And address where open to inspection***

*Oladapo Shonola Ext. 4733
Mulberry Place, 4th Floor.*

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Agenda Item 5.2

Committee/Meeting: Pensions Committee	Date:	Classification: Unrestricted	Report No:
Report of: Corporate Director Resources		Title: Hutton Commission: Interim Report	
Originating officer(s) Alan Finch, Service Head Corporate Finance		Wards Affected: All	

Lead Member	Cllr Anwar Khan, Chair of Pensions Committee
Community Plan Theme	All
Strategic Priority	All

1 **SUMMARY**

- 1.1. At the last meeting of the Committee, Members requested an update on the work of the Independent Public Service Pensions Commission, led by the former Cabinet Minister John Hutton. This report provides that information.
- 1.2. The Hutton Commission was established by the Chancellor of the Exchequer in June 2010 to undertake a fundamental review of public service pensions provision by the time of the next Budget in April 2011. Having issued an interim report in October, the Hutton Commission is currently continuing its work and is expected to report within the next few weeks.

2 **DECISIONS REQUIRED**

The Committee is recommended to:-

- 2.1 Note the report into the work of the Independent Public Service Pensions Commission and that officers will report back further when the Commission issues its final report.

3 **REASONS FOR THE DECISIONS**

- 3.1 Members requested this report in order to update themselves on the work of the Hutton Commission.

4 ALTERNATIVE OPTIONS

4.1. No decision is required at this stage.

5 BACKGROUND

5.1. The issue of public sector pension provision has moved up the political agenda in recent years, largely because;

- The cost of all pension schemes has increased substantially due to increased longevity.
- The closure of many Company defined benefits schemes increasingly makes public sector schemes seem generous in comparison to the provision available to other workers.
- The nature of the schemes is such that responsibility for any deficit rests with the taxpayer and not with the beneficiary, so that the cost of the schemes for the taxpayer, whether now or in the future, has increased.

5.2. The Coalition Agreement committed the Government to establishing an independent commission to review the long term affordability of public sector pensions, while protecting accrued rights. Subsequently, in June, the Chancellor announced that the Commission would be set up, under Lord Hutton of Furness (John Hutton), the former Labour Secretary of State for Work and Pensions, to undertake a fundamental structural review of public service pension provision. The commission was asked to “make recommendations on how public service pensions can be made sustainable and affordable in the long-term, fair to both the public service workforce and the taxpayer, and ensure that they are consistent with the fiscal challenges ahead”.

5.3. The Commission was asked to consider a range of issues including:

- the disparity between public service and private sector pension provision;
- the need to ensure that future pension provision is fair across the workforce;
- how risk should be shared between the taxpayer and employee; and
- wider Government policy intended to encourage adequate saving for retirement and longer working lives.

5.4. The Commission was asked to report in time for the next Budget, which has been announced for 23rd March 2011, and to issue an interim report in time for the Spending Review in October. The interim report was duly published on 7th October.

Interim Report

5.5. The interim report sets out the findings of the Commission to date and, although it does not make any firm recommendations, it points the way to the options that will be addressed in the final report.

5.6. The report emphasises the importance of public service pensions but points out that most schemes were last substantially reformed in the 1970s, since which time the context within which they operate has changed substantially. In the early 1970s, the life expectancy at age 60 was 18 years, now it is 28 years. In addition, many more people reach the age of 60. A man who retires at 60 can now expect to live more than 40% of his adult life in retirement and the figure is higher for women.

5.7. Some limited reforms have taken place in recent years. These include;

- The change in indexation from Retail Prices Index (RPI) to Consumer Prices Index (CPI), which in the run will increase pension benefits by a lesser amount year on year.
- Increases in pensionable age, which in the Local Government Scheme means that staff will ultimately not receive access to their pension until the age of 65 (previously 60).
- Introduction of differential employee contribution rates in the Local Government scheme so that rates now increase from 5.5% to 7.5% with increasing pay (replacing the previous 6% standard rate).

5.8. The drawback is that most of these measures will not affect the costs of the schemes for many decades.

5.9. The Commission has set a number of principles for future public service pension provision;

- Affordability and sustainability

The question of affordability is ultimately a matter for political choice, but this decision needs to be taken in the context of a sustainably affordable scheme (ie not one that simply shunts costs onto later generations).

- Adequacy and fairness

Pensions should provide an adequate retirement pension for public sector workers, maintaining a balance of fairness between workers, and between pensioners and taxpayers.

- Supporting Productivity

The pension schemes should offer value for money and should not be a barrier to measures that improve productivity and efficiency, such as outsourcing or mutualisation.

- Transparency and simplicity

Schemes should be widely understood by beneficiaries and taxpayers

5.10. The interim report identifies only one option that could be implemented to provide short term savings, which is to increase contribution rates for scheme members. The Commission said this should be done in such a way as it protects the low paid and does not impact significantly on opt out rates. There is a danger that any significant increase in rates would simply lead to more staff leaving the schemes, which would be counter-productive in terms of the Commission's principles.

5.11. The report has come down against pure defined contribution schemes which it says would not necessarily be cheaper to fund, result in uncertainty of benefits for scheme members, including the low paid, and not make the best use of the ability of the Government, as a large employer, to manage some of the schemes' risks

5.12. The report identifies a number of possible longer term options which the Commission has now gone on to explore;

- defined benefits based on a career average salary, as opposed to final salary as at present.

- hybrid defined benefit/ defined contribution schemes which are used successfully in some countries.
- consider further the details of scheme design such as retirement ages.

5.13. The Interim Report is available in full at the following website:

http://www.hm-treasury.gov.uk/indreview_johnhutton_pensions.htm

Officers Remarks

- 5.14. It is important to note that the Hutton Commission is reviewing pension provision across the public sector as a whole and not just in Local Government. The Local Government Pension Scheme (LGPS) differs from most other public sector schemes in that it is a funded scheme, although the majority of funds are not currently fully funded, and it is managed locally by trustees within each local authority (the Pensions Committee in Tower Hamlets). Some of the criticism of the public sector pension schemes has been levelled at 'pay as you go' schemes such as the civil service, teachers and NHS schemes, and the LGPS is not in the same category. Nevertheless it is a statutory, defined benefits scheme based on final salary and its costs have risen over the years as longevity has risen. In most particulars it complies with the Hutton Commission's stereotype public sector scheme.
- 5.15. There can also be little doubt that change needs to take place in order to adapt the scheme to the conditions of the 21st Century. For example, the use of a final salary scheme in an era when senior public sector salaries have increased far beyond what they were when the schemes were established no longer seems tenable. Much of the bad publicity for the scheme arises from the apparent generosity of so-called 'gold plated' pensions for 'fat cats', which has skewed debate and distracted from the fact that most local government pensions are small amounts. (The average annual pension payment in the Tower Hamlets scheme in 2009/10 was £7,400). For higher paid staff, a higher contribution rate than that paid by lower paid staff seems perfectly compatible with the benefits they receive.
- 5.16. The alternative to reform along the lines of the Commission's principles would be to allow the schemes to be adapted piecemeal by successive Governments in a bid to control costs. For example the switch from RPI to CPI indexation has reduced the benefits that existing pensioners would otherwise have received in a way that is not very transparent. A reform

package that establishes a fair, affordable and sustainable scheme for the foreseeable future is arguably preferable to employers, scheme members and taxpayers than a series of marginal changes to the scheme that lack clear accountability.

- 5.17. The Government has promised to protect accrued rights, (although changing indexation from RPI to CPI is a grey area). This is an important principle in terms of natural justice, since staff entitled to accrued benefits have already undertaken the work that earned them those benefits. Furthermore the Hutton Commission has recognised that it is not an option to reduce public service pension provision to the level of a lowest common denominator if the state is to attract a suitably motivated and trained workforce.
- 5.18. The outcome of the review remains to be seen although it seems likely that the final report will recommend a change to a career average salary, better reflecting earnings over a person's career, and a rebalancing of contributions between employees and employers, in favour of the taxpayer. Both of these measures would theoretically allow low paid staff to be protected.
- 5.19. Officers will report further to the Committee when the final report becomes available.

6 COMMENTS OF THE CHIEF FINANCIAL OFFICER

The Council contributes £39m a year to the Pension Fund which supports current and future benefits to around 5,100 existing members of staff and 9,600 former employees. At the time of the 2010 actuarial valuation, the scheme liabilities were valued at £1,077m and these were 70% funded by the market valuation of assets.

7 CONCURRENT REPORT OF THE ASSISTANT CHIEF EXECUTIVE (LEGAL SERVICES)

- 7.1 The Local Government Pension Scheme (LGPS) is a national scheme, administered locally. The scheme is closely governed by a suite of regulations made pursuant to section 7 of the Superannuation Act 1972. The LGPS (Administration) Regulations 2008 are particularly significant in the context of the Hutton Commission's work, as they deal with matters such as membership, contribution and payment of benefits. Any reform of the LGPS flowing from the Commission's recommendations would involve amendment of the statutory scheme. Advice can be provided about any such amendments as and when the details become available.

8 ONE TOWER HAMLETS CONSIDERATIONS

All employees of the London Borough of Tower Hamlets are entitled to join the Pension Scheme.

9 SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

There are no direct SAGE implications.

10 RISK MANAGEMENT IMPLICATIONS

The governance of the Pension Fund has its own risk management arrangements. These are not directly affected by the issues raised in this report.

11 CRIME AND DISORDER REDUCTION IMPLICATIONS

There are no direct crime and disorder reduction implications.

**Local Government Act, 1972 Section 100D (As amended)
List of “Background Papers” used in the preparation of this report**

No “background papers” were used in writing this report

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