LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE PENSIONS COMMITTEE

HELD AT 7.05 P.M. ON MONDAY, 31 JULY 2017

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

Members Present:

Councillor Clare Harrisson (Chair)
Councillor Andrew Wood
Councillor Candida Ronald

Union and Admitted Bodies, Non-Voting Members Present:

None –

Other Councillors Present:

None

Apologies:

Councillor Andrew Cregan
Councillor Md. Maium Miah
Councillor Rabina Khan
Councillor Shiria Khatun
Kehinde Akintunde
Apologies was noted from Raymond Haines, Investment Specialist

Others Present:

Steve Turner	– Mercer
Sam Yeandle	– Mercer

Officers Present:

Neville Murton	(Divisional Director, Finance, Procurement & Audit)
Suzanne Jones	(Support to Neville Murton, Resources)
Ngozi Adedeji	(Team Leader Housing Services, Legal Services, Law Probity & Governance)
George Bruce	(Interim Pensions Manager, Resources)
Kevin Miles	(Chief Accountant, Resources)
Bola Tobun	(Investments and Treasury Manager, Resources)
Stuart Young	(Workforce Development, Resources)
Georgina Wills	(Committee Officer, Governance)

1. APPOINTMENT OF VICE-CHAIR

The Chair proposed that Councillor Candida Ronald be appointed Vice-Chair of Pensions Committee for the duration of the municipal year. The proposal was seconded by Councillor Andrew Wood and, there being no other nominations, it was

RESOLVED:

That Councillor Candida Ronald be appointed Vice-Chair of Pensions Committee for the duration of the municipal year.

2. DECLARATIONS OF DISCLOSABLE PECUNIARY INTEREST

The Chair declared a personal interest in item 6.8, Pension Fund Administration Update by virtue of her being Chair of the Tower Community Housing Board. The Chair remained in the meeting and took part of the discussion whilst the item was being discussed.

3. MINUTES OF THE PREVIOUS MEETING

The minutes of the previous Pensions Committee held on 16 March 2017 was approved as a correct record, subject to the following amendments.

Minute item 10, Election of Chair for the Pensions Committee – the word 'some' be included in the first bullet point to read:

'Some Members expressed concerns about the need to re-elect to the position of Chair of the Committee on the grounds that previous Chair of the Committee Councillor Andrew Cregan had changed political groups'.

4. PETITIONS

None received.

5. SUBMISSIONS / REFERRALS FROM PENSION BOARD

Suzanne Jones, Support to the Divisional Director Finance, Procurement and Audit, provided the following feedback from the Pensions Board meeting held on Monday 31 July 2017.

The Board considered reports and held discussions about the Administration of the Pensions Funds and the quality of data received.

Members also reflected on their work programme, in particular how they conduct their business and agreed that their members should attend the Pensions Committee.

The Board has a vacant post, Representative for Admitted Bodies – Employers. Admitted Bodies will be contacted about the vacancy and requested to nominate a representative.

The Chair thanked Suzanne for the feedback and agreed that members of Pensions Committee should attend the Pensions Board.

6. REPORTS FOR CONSIDERATION

6.1 Pensions Committee Terms of Reference, Membership, Quorum and Dates of Meetings

The Clerk presented a report which set out the Terms of Reference, Membership and Quorum of the Pensions Committee for the Municipal Year 2017/2018. The Committee agreed that 7pm was the preferred start time for their scheduled meetings.

RESOLVED:

1. That the contents of the report be noted.

2. That all scheduled meetings start at 7pm.

6.2 Investment Strategy Review

The Committee received a presentation from Steve Turner of Mercer, on the Investment Strategy Review. The aim of the review is to consider the allocation between asset classes; risk and returns, ensure that there is a reasonable balance between the two objectives and to identify improvements to the investment strategy to help achieve these objectives.

There are a number of reasons to undertake a review and these range from funding changes, legislation change, new solutions, consolidation, Liabilities change, outlook change, change to employee and providing a clear plan.

When making investment decision the Committee will need to remain cognisant of pooling and options that are available on the current Collective Investment Vehicle (CIV) platform. The review will be the key determinant of overall investment performance. The Committee during a question and answer session: Noted:

- That there was an opportunity to reduce risk and volatility of their past deficit by £26m or more.
- That more diversification of their portfolio would potentially lead to better returns and reduce their exposure and that their Investment Policy must be aligned
- The forward looking equity market returns were unlikely to be as strong as they have been over the last 7 years and that it was a good opportunity to address the equity risk; the reduction will help the funding position.

- That Bonds accounted for 18% of their Portfolio and was divided into two distinctive types; return seeking bonds and liability hedging bonds.
- The best estimate expected return for Gilts was + 4.1% p.a. and this return surpassed the requirements of their Actuaries. There is a 73% probability of achieving Gilts +2.0%
- The Level of liability hedging was 7% and that currency hedging should be considered.
- That their Asset Portfolio should be increased; this is linked to inflation. A long term strategy would need to be agreed and should be guided by the CIV, the asset allocation would need to be determined as this will have the biggest impact on the CIV.
- That the current funding level had improved over a 5 year period and at current was at 86%, this was attributed to strong asset returns. As funding levels approach nearer to 100% this period should be used as an opportunity to decrease risks.
- The assessed Value at Risk (VaR) indicates that there is a 5% chance that the current deficit £223m could be increased by at least £329m over a 1 year period to £552m. This is based on the deficit as at March 2017.
- Equities are expected to provide 75% of the Funds excess returns and account for 56% of the Fund's risk on the VaR.
- That they consider reducing the allocation to equities by 10%, in light of strong performance, an increase in the funding level and level of risk concentration in equities.
- That an increase in allocation to both Ruffer and Baillie Gifford be considered; they are 'best in class' managers and this would achieve additional diversification and would be relatively quick and easy to achieve. Members raised questions about both managers and asked what percentage was driven by their equity. Baillie Gifford had 40% in their portfolio and Ruffer 50%. The Committee were reminded that allocations should be reduced from poor performing managers.
- That investments in high grade and long-lease properties be considered; it is anticipated that between 66% - 80% of returns will come from income and will be linked to inflation rather than capital appreciation, which at current is poor. Members questioned whether these investments would be at risk from potential government changes to housing and were advised that portfolio would comprise of 'extremely high quality commercial properties' and that the UK Fund have performed ok. The income expected will account for 60 – 80% of total return and a high portion of the income will act as a cushion. The assets are resilient to both financial and economic shocks.
- That half of Absolute Return Bonds (ARB) be allocated to Multi-Asset Credit (MAC), this will ensure returns are driven by markets and not wholly reliant on investment managers and are multi-based. The returns which have been based on the decisions of current investment managers have been poor.
- That current allocation to Index-linked gilts be continued and be increased over a period if current actuarial valuation approach is maintained.

- That a review of their current equity portfolio be undertaken and that the Fund invest more globally over a period of time. The passive global equity fund at LGIM should be utilised in the interim and the usage of the new global equity strategies available from the CIV should also be considered to achieve the above.
- That the fund has materially benefited from the fall in sterling and that consideration should be made to bank gains by hedging. Currency hedging would allow the Fund to bank a portion of these gains and move to a more neutral position of a 50% hedge. This move will slightly reduce the risk of the portfolio, relative to sterling based liabilities.
- That the Pensions Committee interest in low carbon investing was welcomed and that support would be given to incorporate this into the investment strategy. MSCI Low Carbon Target index was identified as the most appropriate index for the fund as it reduces the carbon (relative to the MSCI World) by around 70%. A 30% investment as a starting point was viewed as appropriate; other clients have used this percentage as their starting point. The long term tracking error target is 0.3%.
- That overall expected return of the portfolio would be expected to increase by 0.1% to gilts + 4.2 % p.a. following the proposed changes, predominately as a result of increased exposure to MAC.
- That there was a loss of confidence with GMO and that this matter could be reviewed with the CIV and noted recommendation on moving the passive global equity fund. This could be implemented in the new year(?)
- Asked about, Multi Asset Credit (MAC) and was advised that it was an unconstrained strategy which invests in a wide range of the credit markets. These include investment credits, high yield debts, bank loans and emerging market bonds. Returns are driven by market allocation plus active management from market and security selection. The target return; cash + 3 – 5% and the expected volatility; 5 – 10%. It was recommended that 12% of the Fund’s assets be split between absolute return bonds and Multi Asset Credit.
- Noted that the Pension Fund has included Multi Asset Credit for the last 4 – 5 years and that MAC was a government solution to address access to the credit market following the financial crisis and encourage diversification and mitigates risk. MAC has performed above expectation.
- Members were supportive of Multi Asset Credit and agreed that they should receive further information and training in this area.
- Members commented on the recommendation to disinvest from UK equities and the poor performance of the GMO mandate and were advised that the transition from UK Equity to Global Equity was relatively easily and was a sensible way of achieving strategies and objectives.
- Members raised questions about currency hedging and its effect on cash flows and were advised that Legal and General manages funds and that contracts to sell currencies are taken out every 3 months and rolled over. During increases the currency will be held and equities are sold when there are loses. The Committee was advised that they could

review the currency hedging as part of their 3 years strategy and that this was a good strategic policy to have in place.

- Members commented that they had received a presentation about diversity and investment and at their previous committee had agreed to consider investing 5% of the fund in a sustainable / low carbon or clean agenda fund(s) and highlighted that the recommended initial investment in this area was below this percentage. In reply, it was noted that the returns for Low Carbon Funds may vary and other clients had invested the recommended amount as part of their risk mitigation strategy. An investment in renewable energy was advised to be preferred and it was estimated that it would take between 3 to 4 years to get a full return on investment. The Committee was advised that they should reduce their funding risk and be in a stable position before considering further investment. Investments should be phased and preferably be undertaken when oil prices are low. A 15% would be considered as a good return over a 3 year period, this percentage is equal to 30% of the equity portfolio. This can be reviewed annually or part of their 3 year strategy review. At current the oil market is outperforming low carbon market.
- That it was an ideal time for the Committee to bank equity and balance their portfolio.

Members thanked Steve Turner for his presentation and agreed that the presentation be converted into a strategy and implementation plan and that preliminary discussion be held with Mercer on achieving this.

RESOLVED:

1. Following consideration of the draft Investment Strategy and in the light of the committee's decision to terminate the Global Equities mandate for GMO the Committee agrees to:

   a) Appoint LGIM to manage the GMO portfolio on a transitional basis;

   b) Increase the investment in the Council's Diversified Global Funds mandate from 10% to 20% by topping up the existing DGF fund mandates (Bailie Gifford and Ruffer) by 5% each; to be achieved through a reduction to the GMO Global Equities mandate as part of the LGIM transitional management arrangements;

   c) Reviews further all other aspects of the draft Investment Strategy at their September meeting.

2. Receive training on Multi Asset Credit.

6.3 Update on Market Outlook and Investments by the Independent Advisor

The item was deferred to the next meeting.

6.4 Draft Pension Fund Annual Report and Accounts 2016/17

Bola Tobun, Investment and Treasury Manager, presented a report which updated members on the arrangements for the preparation of the Pensions Fund Annual Report and Accounts 2016/17 in accordance with regulations and the arrangements for the separate audit engagements, opinion and certificate for the Fund.

Members were informed that assets had increased by over £200 million in the year and that funding levels had increased from 83% to 86%.

The Committee was advised that an updated version of the report will be circulated to members, prior to the report being submitted to Audit. The Pensions Fund Accounts are subject to the normal audit of accounts process; which is carried out in July and August 2017.

RESOLVED:

1. That the contents of the report be noted
2. Approve the Draft Pension Fund Accounts prior to submission for audit;
3. Agree publication and distribution to interested parties once approved; and
4. Delegate authority to the Corporate Director, Resources to make any amendments to the Pension Fund Statement of Accounts that arise as a result of the audit, in advance of the publication of the accounts.

6.5 Future Pension Administration Options

George Bruce, Interim Pensions Manager presented a report which detailed the current Pension Administration Services to the Tower Hamlets Pension Scheme, the advantages and challenges to the current arrangements and compared these with alternative arrangements.

Members sought clarification on whether the item should be considered by the Pensions Committee and was advised that initial feedback was being sought.

The current administrative service in place for Tower Hamlets Pension Scheme has been in operation since the Borough was established. At current services are delivered by the Council's HR and Finance Departments and comprises of small teams. This in-house service enables the direct control over the quality of service, ensures there is a direct relationship with scheme managers, avoids conflicts of needs of other clients and ensures certainty of staff.

The LGPS is becoming increasingly complex due to frequent changes in regulation and best practice guidelines and is now under greater scrutiny. Maintaining awareness of and implementing new regulations is a challenge to a small team; in conjunction the size of the current Team faces inherent risks from losing key staff.

Two main alternative means of delivering pension administration services to the scheme have been identified, co-operation with other Local Authorities or appointing an external third party administrator. The former option will grant the Pension Scheme access to more resources, access to a larger and diverse pool of specialist staff, encourage standardised client reporting and reduce IT cost.

The above mentioned will enable more focus to be given to daily tasks and also be adaptive to the needs of the Scheme. The Committee noted the risks of switching from an in-house to a local authority grouping could result in the reverse of advantages that are found in retaining an in-house team.

The third option, appointing a third party administrator would be undertaken via a commercial tender. An appointment of a third part administrator will magnify both the advantages (cost and resilience) and disadvantages (compromise and loss of control) of local authority groups. Third Party administrators can be accessed through the National LGPS Framework.

Members noted all the proposals presented and the size of the administrative team and specialties of officers. The option to collaborate with other Local Authorities was discussed further and Members preferred this option to over the other options presented and agreed that further research be undertaken to ascertain what administrative systems were in place in neighbouring boroughs. Members agreed that if the option to co-operate with other Local Authorities is chosen; the other scheme participants should have a shared interest with Tower Hamlets.

Members were advised that the Pension Board had recommended that all options are fully explored and that resilience of the service remains paramount. The Committee were informed established networks would be used to gage views and experiences. Members can forward comments about the various options to Lead Officers.

RESOLVED:

That a further detailed evaluation of the options outlined in the paper, including discussion with other local authorities is undertaken and that the findings are analysed and presented at the next Committee.

6.6 Investment Performance Review for Quarter Ending 31 March 2017

Bola Tobun, Investment and Treasury Manager presented a report which informed Members of the Performance of the Fund and its investment managers for the quarter and year ending 31 March 2017.

The fund delivered a positive return of 4.4%, by outperforming its benchmark return of 3.6% by 0.8% for the reporting quarter. In addition 7 out of the 9 mandates matched or achieved returns above the benchmark in the quarter end. Ruffer and Goldman mandates lagged behind their respective benchmarks. Overall the Fund performance was ahead of its benchmark.

RESOLVED:

That the contents of the report be noted.

6.7 LGPS Latest Development and Update

Bola Tobun, Investment and Treasury Manager presented a report which provided an update on the general developments in the Local Government Pensions Scheme arena and the progress of the London CIV

Members commented and welcomed the Local Government Pension Scheme (LGPS) Scheme Advisory Board issue of the LGPS Investment Code of Transparency. The purpose of the Code is to improve the reporting and understanding of investment management charges and costs.

The Committee noted that the LCIV during the first quarter of 2017/18 was positive and that a majority of their quarterly KPI targets had been met.

RESOLVED:

That the contents of the report be noted.

6.8 Pension Fund Administration Update

George Bruce, Interim Pensions Manager, presented the report which covered current issues affecting scheme members and employers participating in the Tower Hamlets Pension Scheme.

The Committee was advised that Anant Dodia, Pensions Manager had retired In the interim, Team Leaders will be responsible for overseeing the daily operation of the Team; in addition an experienced Pensions Manager from Surrey Council will provide support to the Service and act as a Mentor. Suzanne Jones, Deputy to the Divisional Director, will continue to attend Committees and assist with employee matters and act as link to team management. The Project Team will continue to work on the Member Self-Service Project.

The following Admin data was reported:-

During the period between April - May 2017 service standards increased and improved from 78% to 86% from the previous quarter. There has been steady progress made in relation to compliance.

Internal Disputes Resolution Procedures, an outstanding appeal has gone to an external reviewer; this is due to contractual information.

The Committee were advised that at their meeting in December 2016 they had discussed and agreed the recommendation to admit Energy Kidz into Pension Scheme and that the discussion and committees resolution was not included in the minutes meeting of 7 December 2017. This recommendation has again been repeated.

Members were advised that Compass Catering had recently advised that that they had employed over a dozen staff in September 2015 and that their request for admitted body status had not been processed. The meeting was informed that deductions from employees have been made since 2015 and that Compass Catering was to be granted admitted body status.

Internal Audit are scheduled to return and will be reviewing the service as part of the 2016 /2017 agreed internal audit plan. Members were advised that the earnings of Active Members will need to be checked to ensure that benefits received are correct. The addresses of these individuals have been checked.

The Actuary has issued a report on the quality of data that was provided during the triennial actuarial valuation in March 2016. A total of 700 members were noted as not having a home address; to rectify this, a company has been commissioned to undertake searches to identify addresses. A charge of £12 will be levied for each address; this cost was viewed as justifiable and good use of budget. The Inland Revenue Service was liaised with.

At the recent Pensions Board, discussions were held about undertaking a formal review of data control and also a benchmarking exercise.

The Committee were reminded that two data matching exercises are carried out on annual basis to ensure that pensions are only paid to surviving scheme members; these include the National Fraud Initiative for UK pensioners and Life certificates for overseas pensions.

The HMRC will be writing to all persons who are entitled to a GMP (Guaranteed Minimum Pensions) to advise what amount and pension scheme will be paid. The GMP is part of the LGPS pension; the government pays the annual inflation increases on the GMP as part of the state pension and the pension funds awards pension increases on that element of the pensions that is not GMP. HMRC are giving schemes an opportunity to agree records prior to their notifications to individuals. There is consideration for the service to purchase external resources to undertake the above. The Committee was advised that the completion of the above would be a valuable exercise and was estimated to be of a value of a six figure sum.

The Committee noted that George Bruce was to leave the Service and thanked him for his work and contributions to the Pensions Committees.

Resolved:

1. That Energy Kidz Ltd. be admitted as an employer within the pension fund

2. That Compass Contract Services (UK) Ltd be admitted as an employer within the pension fund.

3.

7. TRAINING EVENTS

None

8. ANY OTHER BUSINESS CONSIDERED TO BE URGENT

None.

9. EXCLUSION OF THE PRESS AND PUBLIC

The Chair moved and it was

RESOLVED

That press and public be excluded from the remainder of the meeting in that under the provisions of Section 100A of the Local Government Act 1972, as amended by the Local Government (Access to Information) Act 1985, the press and public be excluded from the remainder of the meeting for the consideration of the Section Two business on the grounds that it contains information defined as Exempt in Part 1 of Schedule 12A to the Local Government Act, 1972." which relates to information relating to a particular employee, former employee or applicant to become an employee of, or a particular officeholder, former office-holder or applicant to become an office-holder under, the authority.

9.1 Pension Fund Procurement Plans and Update 2017/18

The meeting ended at 9.00 p.m.

Chair, Councillor Clare Harrisson
Pensions Committee