

<p>Non-Executive Report of the:</p> <p>Pensions Committee</p> <p>24 July 2018</p>		 <p>TOWER HAMLETS</p>
<p>Report of: Zena Cooke, Corporate Director, Resources</p>		<p>Classification: Unrestricted</p>
<p>Draft Pension Fund Annual Report and Accounts 2017/18</p>		
<p>Originating Officer(s)</p>	<p>Bola Tobun, Investment and Treasury Manager</p>	
<p>Wards affected</p>	<p>All wards</p>	

Summary

There is a Statutory Requirement to prepare Pension Fund Annual Report and Accounts

This report updates members on the arrangements for the preparation of the Pension Fund Annual Report and Accounts 2017/18 in accordance with regulations and the arrangements for the separate audit engagement, opinion and certificate for the Fund.

External audit resulting in the auditor's opinion and certificate for the Fund.

The Draft Pension Fund Accounts 2017/18 are attached in annex 1 to this report. The Pension Fund Accounts are subject to the normal audit of accounts process, which is in progress at the time of writing this report as it forms part of the overall external audit programme for the Council.

Audit to be completed before 31st July 2018

Fund assets increased by £112.979m over the year

The net asset statement represents the net worth (£1,481m) of the Fund.

The improvement results from the increase in investment values plus the pre-payment of 2 years deficit lump sum contributions of £28m by the Council.

The return on investment for the Fund was 6% in 2017/18 placing it 7th in the performance league table for local authority pensions funds

The average local authority Pension Fund return in 2017/18 was 4.5%. This is significantly lower than 2016/17 where there was an average return of 21.4%.

In 2016/17, the Tower Hamlets Fund had a return on investment of 20.7% which was 51st in the performance league.

Overall returns for all funds over the year have gone down but the performance of the Tower Hamlets

fund has improved.

In longer term comparisons over 3, 5 and 10 year periods, the Fund was ranked in the 37th (71st), 35th (71st) and 75th (79th) percentile respectively. Equivalent rankings for 3, 5 and 10 year for 2016/17 are shown in brackets.

Funding level at 31st March 2018 increased by 5.4% to 88.2%

At the last formal valuation (31st March 2016) the Fund assets were £1,126m and the liabilities were £1,361m. This represents a deficit of £235m and equates to a funding level of 82.8%. Since the valuation the funding level has increased by 5.4% to 88.2%.

Recommendations:

The Committee is recommended to:

- Note the contents of this report and the Annual Report for 2017/18 attached as Appendix A to this report;
- Note the Tower Hamlets Pension Fund position and outcome of the Pensions & Investment Research Consultants Ltd (PIRC) UK Local Authority League table for 2017/18, set in section 3.5 of this report; and
- Note the Tower Hamlets Pension Fund Funding Level as at 31st March 2018, prepared by the Fund actuary as set in section 3.6.

1. REASONS FOR THE DECISIONS

- 1.1 The Committee acts as quasi-trustee to the Pension Fund and as such acts in the capacity of the Administering Authority of the Pension Fund. The Committee's terms of reference requires that the Annual Report and Accounts on the activities of the Fund are presented and approved prior to their publication. The Local Government Pension Scheme Regulations 2013, Regulation 57 require the Pension Fund to publish its report and accounts by 1st December following the financial year end and for the Report to contain a number of standard items.
- 1.2 The publication of the Pension Fund Annual Report and Statement of Accounts helps to keep Fund members informed, shows good governance and also helps to demonstrate effective management of Fund assets

2. ALTERNATIVE OPTIONS

- 2.1 There are no alternative options in so far as the publication of the Statement of Accounts and Annual Reports is a legislative requirement.

3. DETAILS OF REPORT

- 3.1 The Council as an administering authority under the Local Government Pension Scheme Regulations and is therefore required to produce a separate set of accounts for the scheme's financial activities and assets and liabilities.

- 3.2 The contents and format of the accounts are determined by statutory requirements and mandatory professional standards as established by the Chartered Institute of Public Finance (CIPFA) in their Service Code of Recommended Practice (SERCOP). The annual report has been prepared in accordance with the Local Government Pension Scheme Regulations 2013 and includes all the items required.
- 3.3 The London Borough of Tower Hamlets is the Administering Authority for the London Borough of Tower Hamlets' Pension Fund and the Pensions Committee act as trustees of the Pension Fund which includes overseeing the accounting and financial management of the Pension Fund.
- 3.4 **The Annual Report and Statement of Accounts**
- 3.4.1 The Accounts comprise two main statements with supporting notes. The main statements are:
- Dealings with Members Employers and Others which is essentially the fund's revenue account; and
 - The Net Assets Statement which can be considered as the fund's balance sheet.
- 3.4.2 The return on investment section of the accounts sets out the movement in the net worth of the fund in the year by analysing the relevant financial transactions and movements in the market value of the investment portfolio. The statement has two main sections:
- The financial transactions relating to the administration of the fund; and
 - The transactions relating to its role as an investor.
- 3.4.3 The fund income section of the report principally relates to the receipt of contributions, from employers and active members, and the payment of pensions benefits. The section indicates that the Fund is cash positive in that the receipt of contributions exceeds the pension payments which were £31.5m for 2017/18 compared to £8.56m in 2016/17.
- 3.4.4 The Fund net cash flow position at the end of financial year 2017/18 was 268% more than the previous year. Investment income increased slightly over the year by £0.5m. Transfer Values received (amounts paid over when a fund member transfers their benefits from one fund to another) was relatively static. It is not possible to predict the value of transfer value payments as they are dependent on an individual's length of service and salary and as such may vary significantly. The total employee contributions fell by £330k. Total employer contributions went up significantly by £24.3m. This can be attributed to 3 years prepayment deficit lump sum contribution of some £43m paid by the Council into the Fund in December 2017.
- 3.4.5 In 2017/18 the overall expenditure increased substantially by £4.8m. The major contributors were the overall benefits paid including the lump sum benefits paid that increased substantially by £4.1m and an increase in transfers out of the fund by £1.2m over the year. The investment management costs slightly went up by £372k whilst the administration costs went down significantly by £463k. The reduction was due to costs being paid by the

London CIV rather than the Council demonstrating one of the benefits of being part of a pooled arrangement.

- 3.4.6 Overall, fund membership has decreased from 21,969 to 20,659, a decrease in membership number of 1,310. The number of active members reduced by 620 (9%) whilst deferred members increased by 417 (5%). Retired membership increased moderately by 244 (5%). This reduction in membership is due to auto enrolment rules which means that individuals who are automatically enrolled into the scheme as per the changes to pension regulations can opt out of the scheme.
- 3.4.7 The investment performance section of the report details returns on the investment portfolio, the impact of managers' activities and investment markets on the value of investments. The Fund achieved a return of 6% in 2017/18 on its investment portfolio outperforming the benchmark return of 4.1% by 1.9%. The Fund posted a 3 year return of 8.1% which is marginally above the benchmark return of 7.9% and also delivered a 5 year return of 8.9% outperforming the benchmark return of 8.4% by 0.5%.
- 3.4.8 Overall, fund assets increased by £112.979m. The improvement was due to the performance of the financial markets in which the Fund held its investments plus the pre-payment of 2 years deficit lump sum contributions of some £28m by the Council.
- 3.4.9 The net asset statement represents the net worth (£1,481m) of the Fund as at the 31st March 2018. The statement reflects how the transactions outlined in the other statement have impacted on the value of the Fund's assets.
- 3.4.10 The annual report also includes three key statements (Funding Strategy Statement, Investment Strategy Statement that replaced Statement of Investment Principles and Governance Compliance Statement) relating to the management and governance of the scheme and each statement serves a different purpose.
- 3.4.11 The Funding Strategy Statement undergoes a detailed review and was updated after the triennial valuation. The 2016 triennial valuation outcome was reported, discussed and approved at the Pensions Committee meeting of 16th March 2017.
- 3.4.12 The purpose of the Funding Strategy statement is threefold:
- To establish a clear and transparent fund specific strategy which will identify how employers' pension liabilities are best met going forward;
 - To support the regulatory framework to maintain as nearly constant employer contributions rates as possible; and
 - To take a prudent longer-term view of funding those liabilities.
- 3.4.13 The Investment Strategy Statement (ISS). The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require administering authorities to formulate and to publish a statement of its investment strategy, in accordance with guidance issued from time to time by the Secretary of State.
- 3.4.14 This ISS is designed to be a living document and is an important governance tool for the Fund. This document sets out the investment strategy of the Fund,

provides transparency in relation to how the Fund investments are managed, acts as a risk register, and has been designed to be informative but reader focused. This document was last reviewed and approved by the Committee at its meeting of 14th March 2018.

- 3.4.15 The Governance Compliance Statement sets out the Council's policy as the administering authority in relation to its governance responsibilities for the Fund.
- 3.4.16 The Audit Plan for the Pension Fund and any reports arising from the audit will be reported to the Pensions Committee. However, as the pension fund accounts remain part of the financial statements of the Council as a whole, the Audit Committee retain ultimate responsibility for receiving, considering and agreeing audit plans as well as receiving any reports arising from the audit.
- 3.4.17 The External Auditor provides an independent assessment of the Council's Pension Fund financial statements, systems, procedures and performance.
- 3.4.18 The audit plan outlines their intended work on the financial statements for 2017/18, and is in progress at the time of writing this report. This work is due to be concluded before 31st July 2018 and it is part of the Audit programme for the Council. The outcome of this will be reported to this Committee later in the year.
- 3.4.18 KPMG, as external auditor, is required to issue an ISA 260 report and opinion on the Council's accounts and this will include an opinion on the Pension Fund accounts. The ISA 260 report sets out their opinion and any issues which they believe the Committee should be aware of.
- 3.4.19 The Pension Fund audit is being undertaken by KPMG and the audit fee has been maintained at £21,000 which is charged to the Pension Fund.

3.5 PIRC League Table Performance

- 3.5.1 PIRC measures the performance of the Fund against its benchmark and against the Local Authority Universe data. The PIRC Local Authority Universe is an aggregation of Funds within the LGPS sector that is used for peer group comparisons. The performance results set out in this section are from the league tables.
- 3.5.2 The average local authority Pension Fund was just positive in 2017/18 with a fund return of 4.5% compared to an exceptional return of 21.4% in 2016/17. This has brought the 3-year performance down to 8.3% per annum from 11.2% per annum in 2016/17.
- 3.5.3 The Fund was ranked in 7th place with a Fund return of 6% in the PIRC Local Authority Universe League Table compared to 51st position in 2016/17 with a Fund investment return of 20.7%. However, over the longer 3, 5 and 10 year period, the Fund is ranked in the 37th (71st), 35th (71st) and 75th (79th) place respectively. 2016/17 equivalent rankings for 3, 5 and 10 year are shown in brackets.

3.6 Funding Update

- 3.6.1 This funding update has been provided to illustrate the estimated development of the funding position from 31 March 2016 to 31 March 2018. At the last formal valuation the Fund assets were £1,126m and the liabilities were

£1,361m. This represents a deficit of £235m and equates to a funding level of 82.8%. Since the valuation the funding level has increased by 5.4% to 88.2%, with Fund assets of £1,442m and liabilities of £1,636m, producing a deficit of £194m.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

- 4.1 The Council as Administering Authority has the responsibility of ensuring that the Pension Fund is administered effectively and efficiently and that arrangements for financial management are properly scrutinised. The performance of the fund affects the level of employer's contribution to the fund
- 4.2 Paragraph 3.4.4 above details the additional employer contributions made during 2017/18. This was as a result of making payments in advance for 3 years deficit contributions which helped maximise return on investment for the Pension Fund.

5. LEGAL COMMENTS

- 5.1 Regulation 57 of the Local Government Pension Scheme Regulations 2013 imposes a duty on the Council as an administering authority to prepare a pension fund annual report. The report must be published by 1st December following the financial year end.
- 5.2 The report should deal with the following matters:
- (a) management and financial performance during the year of the pension;
 - (b) an explanation of the investment policy for the fund and a review of performance;
 - (c) a report on arrangements made during the year for administration of the fund;
 - (d) a statement by an actuary who carried out the most recent valuation of the fund and the level of funding disclosed by that valuation;
 - (e) a Governance Compliance Statement;
 - (f) a Fund Account and Net Asset Statement;
 - (g) an Annual Report dealing with levels of performance set out in the pension administration strategy and any other appropriate matters arising from the administration strategy;
 - (h) the Funding Strategy Statement;
 - (i) the Investment Statement Strategy;
 - (j) statements of policy concerning communications with members and employing authorities; and
 - (k) any other material which the authority considers appropriate.
- 5.3 When performing its functions as administrator of the LBTH pension fund, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty).

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The Pension Fund Accounts demonstrate financial stewardship of the fund's assets. A financially viable and stable pension fund is a valuable recruitment and retention incentive for the Council.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The monitoring arrangement for the Pension Fund and the work of the officers, advisers and consultants should ensure that the Fund optimises the use of its resources in achieving the best returns for members of the Fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

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

9. RISK MANAGEMENT IMPLICATIONS

9.1 Accounts provide an effective mechanism to safeguard the Council's assets and assess the risks associated with its activities.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no any Crime and Disorder Reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- NONE

Appendices

- Appendix A – Draft Pension Fund Annual Report and Accounts 2017/18
- Appendix B - PIRC UK Local Authority League table for 2017/18
- Appendix C – Funding Level Update as at 31st March 2018

Local Government Act, 1972 Section 100D (As amended)

List of “Background Papers” used in the preparation of this report

- NONE

Officer contact details for documents:

Bola Tobun(Investment & Treasury Manager) x4733