



Surrey Local Pension Board 18 July 2019

Summary of the Pension Fund Committee meeting of 7 June 2019

Recommendations:

The Board is asked to **note** the content of this report.

Detail:

Introduction

1. The Pension Fund Committee met on 7 June 2019. This report provides a summary of this meeting and any resolutions made.

Forward Plan

2. The latest approved Pension Fund Committee Forward Plan is shown as Annex 1.

Local Pension Board report

3. The Pension Fund Committee (Committee) received the report from the Local Pension Board (Board) (shown as Annex 2).
4. The Committee heard from the Chairman of the Board, who presented a summary of the administration and governance issues reviewed by the Board at its last meeting on 25 April 2019. He ran through the key issues that the Board had considered, which included the Pensions Administration problems highlighted at the last meeting of the Committee, the processing of death cases, the reconciliation project and the contract entered into with Jardine Lloyd Thompson to handle the backlog processing.
5. The Chairman of the Board informed the Committee that the Board had received a positive report on the annual benefit statement and that officers were on track to meet the 31 August 2019 deadline.
6. Members were directed to paragraph 19 of the report, which dealt with the Administration Risk Register and the changing of many residual risks from amber to green. The Chairman of the Board explained that there were plans in place to

remedy the problems and that this had resulted in these risks being reduced from ratings of 3 to 2. However, he asked the Committee to treat this with caution as there was still work to do.

7. The Pensions Lead Manager stated his agreement with the points made by the Chairman of Board. He told the Committee that Pensions Administration was in a phase of stabilisation and recovery, and that this would be the case for the next 12 to 15 months.
8. A discussion was had about the Chartered Institute of Public Finance and Accountancy benchmarking report after a Member of the Committee expressed their shock that the cost per member remained below average. The Chairman of the Board suggested that under investment could have affected the quality of the service. However, he went on to explain that the number of complaints received from members had remained at a low level despite the problems exhibited.
9. The Director of Corporate Finance informed the Committee that it would receive further clarity on the standards of pension administration later in 2019, as Internal Audit would be undertaking a follow-up review in the autumn.
10. The Committee resolved the following:
 - To approve all the recommendations from the Board
 - Note the progress and developments in improvements in the Pension Administration department, but also note that the service improvement plan is in its infancy
 - Endorse relying on the legal opinion on the recovery of overpaid guaranteed minimum pensions prepared by Squire Patton Boggs for the Local Government Association
 - Agree that there are currently no projects or processes that the Board should be commissioned to undertake on behalf of the Committee

Company engagement and voting

11. The Chairman introduced the report and explained that the Committee took seriously all environment, social and governance (ESG) issues. He said that it was reasonable for people to query what had come out of the engagement the Fund had been involved in and that this was one of the questions the report attempted to address.
12. The Committee heard from the Strategic Finance Manager, who directed Members' attention to the section on the Border to Coast (BCPP) Climate Change Working Party. These laid out the considerations the Surrey Pension Fund were working on and offered an explanation for its policy of engaging rather than divesting. The Responsible Investment Policy of BCPP has been adopted by the Fund. This is reviewed annually and any future changes would be brought to the Committee.
13. A discussion was had about the Fund's voting record, with a Member asking for more detailed information to be provided about the impact and outcome of each vote. The Senior Accountant highlighted the fact that the success of the Fund's voting varied depending on the specific resolution and that paragraph 25 of the report mentioned votes that had been defeated.

14. The Committee resolved the following:

- Noted the main findings of the report, the outcomes achieved for the quarter ending 31 December 2018 by Robeco/LAPFF, by engaging with multinational companies on various ESG issues
- Noted the findings from the Fund's share voting process for the quarter ending 31 March 2019
- Noted the ESG outcomes achieved by Fund managers
- Reaffirmed focus on ESG issues and the Fund's policy on engagement

Investment Manager Issues and Asset/Liabilities Performance Update

15. The Strategic Finance Manager informed the Committee that the total value of the Fund was approximately £4.3 billion, which represented an increase of around 30% since 2016 against the actuarial assumption in the 2016 valuation of 13%. Members heard that the average increase across the Local Government Pension Scheme (LGPS) universe was approximately 25%.

16. A Member queried a section on page 100 of the report, which referred to an answer being given from Marathon to the Independent Advisor that he "was not expecting". In response, the Independent Advisor explained that his conversation with Marathon had led him to the opinion that they were stock pickers and chose the companies they liked, no matter what sector or country they were in. He went on to say that the second generation had a more relative than absolute approach to investing and that this year's second quarter returns were a mirror image of first.

17. Referring to the information on page 86, the Chairman said that the table gave a mixed message, as it looked as if Fund managers were not performing well. However, the double-starred paragraph stated that each manager needed to be viewed in isolation and, as a whole, included managers which the Fund no longer employed and should also take in to account managers who had been with the Fund for a short time. The Chairman asked that the reporting format be reviewed. Officers agreed to action this in consultation with the Chairman.

Investment Strategy Review

18. The Committee heard from the representative from Mercer, who directed their attention to the illustrative portfolio graphics outlined on page 147 of the report. He explained that an overall return of 5% was expected over a 10-year timeframe and that equities would drive around 70% of that return. He went on to say that there was a 5% chance that the value of the asset could fall by £900m due to a 20% downturn in equity markets. However, it was important that the Committee did not panic if this came to fruition, as long-term investors needed to stick to the strategy outlined.

19. Responding to a question about whether the estimated 5% return took into consideration the 20% fall in equity markets, the representative from Mercer told the Committee that this was a best estimate and that they would be looking to maintain the 5% return. Cashflow was positive for the near- and medium-term and there was plenty of scope for investing in more long-term liquid assets.

20. A discussion was had about a training session on illiquid assets that would be conducted before the next Committee meeting on 13 September 2019. The Strategic Finance Manager informed the Committee that this would take place in either July or August and Members would be invited to attend.
21. The representative from Mercer went on to explain that the area in which they had least confidence was in diversified growth funds (DGF), and as a result they were proposing to use these assets elsewhere. These would be redeployed to more illiquid assets, as outlined in the proposed strategy pie chart on page 147 of the report, and would result in a risk reduction of approximately £35m.
22. Asked by the Chairman for more information about the work in progress, the representative from Mercer explained that they were undertaking more engagement with BCPP and that there would be a tweak within the structure of equities, with emerging market equities increasing to around 15%.
23. A Member of the Committee questioned the logic behind the increase in illiquid assets and was told by the representative from Mercer that the recommendations outlined would still comprise over 70% of liquid assets. He went on to explain that new illiquid classes were estimated to result in returns of around 8% which compared to DGFs.
24. The representative from Mercer confirmed to a Member of the Committee that the expected return outlined in the proposal had taken into account costs and fees expected.
25. The Chairman of the Board questioned what progress had been made with regards to the potential introduction of employer-related investment strategies. In response, the Strategic Finance Manager explained that strategies had been agreed by the Committee. The shape of the proposed strategies would become apparent after the end of year valuation and contributions had been agreed with employers, and the plan was to bring this to the Committee for approval later in 2019.
26. A discussion was had about the formulation of percentages outlined in the illustrative portfolio proposals. The representative from Mercer told the Committee that changes had been made in an attempt to keep the return the same as the previous strategy and that it would take about four years to achieve the target allocation. The Strategic Finance Manager added that it was an ongoing piece of work both internally and with BCPP on management cashflow.
27. The Chairman questioned whether BCPP would be able to offer a wider scope within the discussed asset classes than the Fund would be able to on its own and was told by the Strategic Finance Manager that this was the case and that there were further benefits in the illiquid asset class and in risk management.
28. The Strategic Finance Manager is to organise a training session on illiquid assets before the next Committee meeting on 13 September 2019.
29. The Committee resolved the following:

- Noted the initial work carried out by officers and the Investment Consultant, Mercer, on reviewing the investment strategy
- Gave approval for officers, Mercer, the Independent Advisor and the Chairman of the Committee (and other members of the Committee, if deemed appropriate) to continue work on this review. Formal recommendations will then be put forward to the Committee at its meeting on 13 September 2019.

Valuation assumptions

30. The representative from Hymans Robertson introduced the report and explained to the Committee that there was no clear evidence to justify a change in the discount rate. He went on to recommend that the rate was maintained at 4.2% for the 2019 valuation.
31. Discussing longevity assumptions, the representative from Hymans Robertson informed the Committee that these were the same as at the last valuation. The rate of improvement in life expectancy had slowed down since then but was improving amongst pension contributors.
32. A Member of the Committee questioned how often longevity was reviewed to work out figures and was told by the representative from Hymans Robertson that this was done at the time of the valuation for the purposes of the Fund but that data was provided from private sector schemes on a yearly basis. The Chairman added that the Continuous Mortality Investigation (CMI) was constantly carrying out analysis to see what changes were occurring.
33. Responding to a question about what impact an increase in certainty would have on expected return, the representative from Hymans Robertson explained that more certainty would be achieved by a lower investment return, but that this would result in higher contributions from members of the Fund scheme. The Independent Advisor then spoke about the fact that the scheme is c93% funded and that the aim was to make sure that they did not need to go back to employers in the future for higher contributions.
34. The Committee resolved to approve the recommended actuarial assumptions to be used by the actuary in the 2019 valuation.

National Pooling Update

35. Details regarding this item are included in a separate paper.

Governance Review

36. Details regarding this item are included in a separate paper.

Pension Fund Accounts 2018/19

37. The Strategic Finance Manager said that the Committee had always seen the accounts but this was the first time it had seen them before the external audit had taken place. The Director of Corporate Finance also explained that she felt it was right for Members to see the difference between the draft and final versions as the role of the Committee was to be custodians of the Fund.

38. The Senior Accountant informed the Committee that the main changes had been summarised in the covering report under the 'Summary of Findings' heading. The officer went on to explain that the Fund had transitioned its first asset to Border to Coast and made improvements in terms of timing and efficiency in producing the accounts.
39. Responding to a question about the deadline for approving the accounts, the Senior Accountant informed the Committee that this would take place at the end of July 2019.
40. It was agreed that the recommendation should be amended to explicitly mention that the accounts had been presented to the Committee in draft form.
41. The Committee resolved to approve the draft 2018/19 Pension Fund Accounts, subject to an unqualified opinion issued by audit.

Administration Monitoring Report

42. The Strategic Finance Manager explained to the Committee that he had undertaken constructive meetings with the Pensions Lead Manager and that the Pension Fund and Pension Administration teams were now meeting on a monthly basis.
43. The Committee also heard about the introduction of new metrics for KPIs and that progress against project milestones and business as usual performance would be reported to the Board on a quarterly basis.
44. The Committee noted the content of the report and approved the monitoring approach of the Fund.

Pension Fund Business Plan 2018/19 Outturn Report

45. The Strategic Finance Manager introduced the report and highlighted the key areas of interest. The Committee heard that Items 7, 8 and 11 were partial achievements but that the Strategic Finance Manager had received assurance that Items 7 and 8 were in the project plan and that the Pensions Fund department were working with the Pensions Lead Manager. With regards to Item 11, he informed the Committee that the statutory deadline was not met due to employers failing to engage sufficiently with the Fund but that they were on course to make the deadline for all benefit statements that year.
46. The Committee heard from the Pensions Lead Manager, who explained that Pensions Administration were focusing on improving engagement with employers, timeliness of returns and the accuracy of the provided information. He went on to say that at the time of the publication the Pensions Administration update report noted that 216 out of 276 returns had been received from scheme employers but that there were now just six outstanding.
47. The Chairman of the Board raised the issue of missing addresses for deferred members and explained that close attention needed to be paid to the problem.
48. The Committee noted the achievements and progress made with regards to the Business Plan objectives shown in respect to the 2018/19 financial year and approved the outturn report.

MHCLG Statutory Guidance on Asset Pooling

49. The Strategic Finance Manager expressed to the Committee the importance of the proposed changes to the current statutory investment pooling guidance outlined in the report and explained that both a response by the Border to Coast Joint Committee and an individual response on behalf of Surrey County Council from the Executive Director of Finance had been issued to MHCLG after consultation with the Chairman of the Committee.
50. The Committee heard about concerns that the government seemed to use passive funds as a default for the way adjusted returns are measured. A well-researched response to a previous government consultation had been issued by LGPS funds on this question.
51. The Strategic Finance Manager informed the Committee that he had recently found out that a follow-up consultation was going to take place.

Cashflow analysis

52. The Committee noted the cashflow position for quarters three and four and determined that no change was required to the investment or funding strategy as a result of the current cashflow position.

Report contact: Neil Mason, Strategic Finance Manager (Pensions)

Contact details: T: 020 8213 2739 E: neil.mason@surreycc.gov.uk

Annexes:

Annex 1 – Pension Fund Committee forward plan

Annex 2 – Local Pension Board committee report

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