



meeting

PENSIONS INVESTMENT SUB COMMITTEE

date

15 DECEMBER 2006

agenda item number

REPORT OF THE STRATEGIC DIRECTOR OF RESOURCES
PENSION INVESTMENT CONFERENCES, INSPECTION AND
AWARDS PRESENTATION

Purpose of the Report

1. To report back on the key areas covered at two recent conferences attended by Members and to inform the Sub Committee of the details of a Property Inspection and the outcome of two Awards presentations.

Information and Advice

2. In October, the Local Government Employers held their Annual Local Government Pension Scheme Trustees' Conference in Leeds and it was attended by two members of the Sub Committee. Additionally, in November, three members attended the Local Government Chronicle's seminar on options for a new Local Government Pensions Scheme. The Professional Pensions Awards Presentation also took place in October and was attended by the Chairman and an Officer. In late November, the Chairman and an Officer attended a partners meeting of the Standard Life European Property Growth Fund, inspecting a number of properties and attending an Awards presentation. This report summarises the main issues raised at the two conferences and provides details of the partners' meeting/inspection and outlines the outcome of the Awards Presentations.

Trustees Conference, Leeds

3. The Conference examined the many issues facing the Local Government Pension Scheme and chose a number of themes to illustrate these namely pension provision, risks associated with running the pension scheme, regulations, governance, actuarial valuations and communication. On pension provision, the new look Local Government Pension Scheme and the various options involved were outlined. Changes to the Pensions Regulations are anticipated by March 2007 to take effect from April 2008.

4. The current problems facing Pension Funds, most noticeably forecasted fund deficits, have been caused by a number of factors including poor equity returns over 2000 to 2002, increased demand for bonds, the removal of ACT on equities, improved longevity, lack of asset diversification and FRS17 requirements for a greater accountancy transparency. The risks to Pension Funds were many and varied but speakers identified ways to lessen these including the use of alternative investment strategies. These could be liability driven, involving leveraged loans, infrastructure and property investment. Different models existed to help Funds manage risks and a specific framework relating to longevity or mortality risk was illustrated during one of the sessions.
5. On regulation, the key changes that have been introduced recently were identified as follows:-
 - a) Civil Partnership Act – partner entitled to comparable spouse benefits
 - b) New Statement Requirements – two new statements on Funds' Communication and Governance Policies
 - c) Finance Act 2004 – removal of the maximum number of years that can be used in the calculation of benefits, the first phase in introducing flexible retirement and new introduction of the Pensions Regulator
 - d) Age Discrimination – employment equality relating to age to be effective from 1 December 2006
6. The Government intends to introduce amending regulations requiring each Fund to review its governance arrangements against a best practice model and to state in its Governance Policy Statement the extent of compliance. The proposals are anticipated to be issued for consultation by the end of December 2006 and implemented by April 2007. Overall, the Department for Communities and Local Government (DCLG) view is that most local government pension funds operate good practice and that the proposed amended regulations are intended to prompt change in a minority of existing funds.
7. The core options suggested as part of the new look Pension Scheme proposals were examined from an actuarial standpoint. Factors such as longer life expectancy, commutation and investment risk were considered as part of a preview of the impact of the various options. The speakers also reviewed administrative costs of Funds.
8. Communication in a time of increasing pensions complexity was seen as essential and the requirement to have a Communications Strategy was illustrated. Other initiatives available to Funds were identified as pension websites, telephone helplines, newsletters, leaflets, roadshows and AGMs.

Local Government Chronicle Seminar – Options for a new LGPS

9. The seminar presented four different themes to delegates namely the future direction of the Pension Scheme, funding issues, investing overseas and the governance of Funds. The first speaker, Terry Crossley from the DCLG reassured the audience that the Government is committed to securing good, viable derived benefit pensions for workers who are and should be covered by the Local Government Pension Scheme (LGPS). The four main options for the LGPS were outlined and responses to the options were summarised. These responses are currently being assessed and the timetable for legislation by March 2007 and implementation by April 2008 was re-affirmed. In addition, 2007 is likely to see other LGPS reforms covering administrative regulations, governance provisions and an admitted body status review. Whether the new look LGPS would be a change for the better was examined by the Chief Executive of the London Pension Fund Authority. The options were reviewed and potential future developments including tiered employee contribution rates, increased flexibility for early retirement and scope for further employer discretion were discussed. The outcome, in terms of which options the Government would choose was left undecided.

Looking ahead, more regulation is anticipated in a number of areas including added years, admission body changes, scheme governance and the new look LGPS. Currently, the Unison judicial review on the 85 year rule is ongoing and the London Pension Fund has joined a lawsuit against BP. Overall another busy year is anticipated.

10. Three speakers covered funding issues beginning with an actuarial assessment of the prospects for the 2007 valuation. With post 2004 valuation changes including the removal of the 85 year rule, increased transitional protections and commutation the cost of pension schemes are not too dissimilar to 2004. Despite good equity returns the overall valuation position may not change markedly. Different actuaries will deal with valuations differently. Some may decide that a higher discount rate is appropriate and some assumptions could alter e.g. on pay increases. Overall, the actuary's message was cautious concerning any significant improvement in valuations.
11. The merits of adopting a liability driven investment strategy and diversifying asset holdings were explored. The key objective was to ensure that market volatility does not threaten future pension payments by matching future cash flows from liabilities but there are potential problems including the complexity and suspicion of a liability driven concept. Diversification can also reduce volatility and enhance returns and various approaches have evolved including asset classes and tactical asset allocation.
12. Overseas investments are one means of diversifying Funds' assets and increased investment in overseas equities is occurring while overseas bonds are decreasing. Equities are viewed more favourably with key areas identified as Japan, Europe and the Asia Pacific region.

Information is also more readily available than previously to help investors make decisions. Improving accounting standards and financial reporting, including forecast data, provide the opportunity for more informed decisions.

13. Governance of pension funds remains a key issue and being able to demonstrate good governance via integrity, openness and fairness was essential. Communication was important and the two main statements – the Funding Strategy Statement and the Statement of Investment Principles – were core documents in explaining approaches to fund management.

Professional Pensions Awards

14. The Professional Pensions Awards were held in October in London and the Authority's Fund was shortlisted in 5 categories namely the Best Use of Specialist Investment Managers (public), DB Communications Award, Large Scheme of the Year, Corporate Governance and the Trustee Development Award. The Fund was successful in the Best Use of Specialist Manager category and the Chairman received the Award which was duly presented to the Chairman of the Authority at the County Council meeting in October. The Award represents excellent recognition of the Fund's strategy to diversify its asset holdings and to ensure its assets are managed by leading investment specialists.

Partners Meeting, Property Inspection and Awards Presentation 30 November 2006 and 1 December 2006

15. The Pension Fund has invested £20m in the Standard Life European Property Growth Fund. In total, the Property Growth Fund's size is approximately £600m and it has 27 contributing partners, of which the County's Pension Fund is one. Standard Life hold twice annual advisory committee and partners meetings to inform partners of the Fund's progress and to receive feedback on its decisions.
16. The most recent meeting was held in Paris on 30 November 2006 and was attended by the Chairman and one Officer. Standard Life reported a return of 25% on its investments for the 12 months to the end of September 2006. Overall, since its inception in 2001 (the County Fund joined in 2002) the return has been 10.7% per annum, with a 3 year return of 15.8%. Property investments are spread throughout Europe and are actively managed with the bulk of properties in France, Spain and Belgium though about 14% of the Fund is invested in non Euro zone Countries. A number of partners were present at the meeting and were all pleased with the Fund's performance. An opportunity to increase the County's investment in the Fund, albeit by a relatively modest amount, is soon to be available as one of the Fund's partners will be relinquishing its 20m euro investment for asset allocation reasons. Existing partners will be invited to take up this relinquished investment, and the County Fund will seek to increase its share.

17. The Standard Life representatives outlined further prospective purchases informing the partners that the Fund still had approximately £200m to draw down, though potential investments worth approximately £400m were in discussion.
18. A property inspection for the partners was held on 1 December 2006, where 4 prime investments in Paris were inspected, valued at over £100m. In addition, partners attended the IPE Awards presentation on the evening of 30 November 2006. In all, the partners meetings, the property inspection and Awards presentation provided a very effective means of assessing both the Fund's investment return and also obtaining the views of other partners on the Fund's progress.

Statutory and Policy Implications

19. This report has been compiled after consideration of implications in respect of finance, equal opportunities, personnel, crime and disorder and those using the service. Where such implications are material, they have been described in the text of the report.

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Legal Comments

Background Papers Available for Inspection