



**REPORT OF SERVICE DIRECTOR – FINANCE, PROCUREMENT & IMPROVEMENT**

**PENSIONS AND LIFETIME SAVINGS ASSOCIATION (PLSA) LOCAL AUTHORITY CONFERENCE 2016**

**Purpose of the Report**

1. To report on the PLSA Local Authority Conference 2016 held in the Cotswolds.

**Information and Advice**

2. The PLSA Conference 2016 was held on 16<sup>th</sup> to 18<sup>th</sup> May 2016 at the Cotswold Water Park Four Pillars Hotel in Gloucestershire. In accordance with prior approval and as part of the Fund's commitment to ensuring those charged with decision-making and financial management have effective knowledge and skills; the conference was attended by Councillor Reg Adair, Chris King (Unison) and Mr Nigel Stevenson (Service Director – Finance, Procurement & Improvement). The theme of this year's conference was 'Efficient, transparent, collaborative: Shaping in the modern LGPS'.
3. ***Pre-Conference Meetings***  
The conference commenced with a number of sessions covering topics such as capital preservation vs outperforming the market (arguing that LGPS funds should concentrate on absolute and long-term total returns rather than market benchmark performance and short performance evaluation) and a session about using smart beta to improve performance over passive managed index-linked equity investments. These included presentations from Newton Investment Management and State Street Global Advisors
4. ***Joanne Segars, Chief Executive, PLSA***  
The main conference began with Joanne Segars welcoming everyone to the Conference and setting the tone for the event. She began by highlighting a number of challenges facing the LGPS including:
  - The EU referendum
  - Striving for efficiencies through right investment opportunities, are they affordable and are the investment regulations appropriate
  - Getting our capital allocations correct and are we investing for the long term
  - Are there too many risks in the LGPS and are the benefits affordable
  - How do we ensure the right approach to pooling of investments in the LGPS is made
  - Are the timescales for pooling submissions too tight and how we ensure the correct governance arrangements are in place, and
  - What is the role of the Pension Board?
5. ***A Political Imperative***

Marcus Jones MP, Local Government Minister gave his personal views on what he is looking for from the submission of the pooling proposals and what he sees as the greatest benefits, and risks, of pooling assets in the LGPS.

Overall he was satisfied with the momentum for pooling but reiterated concerns over correct governance structures and the need for greater ambition for investment in infrastructure (although no targets would be set). He also indicated that the Government Actuary's Department (GAD) would review the 2016 LGPS valuation – to be published in 2018. In addition, the unprecedented number of responses to the consultation on changes to the investment regulations (23,000) would cause a delay in publishing these regulations. The intention would be to move away from prescription to more prudential approach and he spent time trying to allay fears over the concerns raised on the proposed intervention powers for the Secretary of State.

He concluded his speech with a reiteration of the statement on the review that GAD will do and the question to be answered on affordability – and potential implications to benefits.

In responses to questions the Minister explained about his ambition for infrastructure investment, although he wasn't able to answer Councillor Adair's question on providing a definition of infrastructure. He recognised the national issue on shorter recovery periods for academies due to their weaker covenant but did not propose that the Government would provide the same covenant to academies as provided to local government. Unfortunately, he also expressed his disappointment that the lack of progress on Fair Deal, Aggregation and Investment Regulations was down to civil servants. In addition, he indicated that there were no plans to change the position of local authority Members being able to join the LGPS.

## **6. *Controlling All Costs***

The 2016 valuation will be critical to the sustainable future of the LGPS. How will the new cost control mechanism shape this valuation and how can we ensure fair measurement of deficits across the LGPS? This session was led by Martin Clarke, Government Actuary, Government Actuary's Department, Councillor Roger Phillips, Chair of the Scheme Advisory Board and Fiona Farmer, National Officer, Unite the Union.

Martin began his presentation by explaining that GAD were concluding their review of the 2013 valuations of the LGPS based on the 4 themes of compliance with regulations, consistency between valuations, overall solvency and long-term cost efficiency. This had no statutory force and was based on a sample of valuations but set identified well known issues of comparability (including variances in discount rates), differing recovery periods and overall affordability concluding with RAG ratings on the 4 themes. This exercise would help them prepare for the major review of the 2016 LGPS valuations.

Fiona's presentation centred on the issue of affordability of the LGPS and the two masters that will assess this, GAD and the Scheme Advisory Board (SAB). Roger's presentation also looked at the scheme affordability question and the issues of comparability between funds. He also explained how the HMT has hard rules on affordability of the scheme ('the cost cap') which will change the scheme benefits (through negotiation or imposition) whereas the SAB can only recommend changes. Both start from differing ceilings as to affordability.

We are too early in the valuation cycle to yet know if the cost cap, under either model, will be breached or not.

## 7. **Concurrent Sessions**

A number of concurrent sessions were delivered:

### a) Good Governance – Being a Local Pension Board

This session looked at the governance arrangements for local pension boards and the areas they should be focusing on and included presentations from Neil Mason, Senior Advisor, Surrey Pension Fund and John Raisin, Chair, Merseyside Local Pension Board (and also adviser to the Nottinghamshire Pension Board).

### b) Broadening your horizons

As the monumental changes in the LGPS sector play out there are several important questions that arise about the approach the new pools will take to investment management. One of these questions is around the length of investments. There is growing evidence that unconstrained active management is most effective over a full market cycle (7 years), but at the same time we see an increased tendency for governance structures to create a focus on one and three year numbers. The LGPS may need to consider their time horizon in this new environment and the possible implications that follow. This session included presentations from Ben Kotter, Institutional Portfolio Manager, MFS and Mathew Dawson, Treasury and Pension Fund Manager, Warwickshire Pension Fund.

The discussion that followed included the setting up of the Pools and how Funds submit their criteria to get their say in the final choice of Managers to ensure transparency on appointments.

### c) Exploiting behavioural finance to enable trustees decision making

The impact on human behavioural biases on decision making is a well-known and well-documented phenomenon. But can we harness the power of these biases to help Trustees make better long term strategic decisions as well as invest assets on a day to day basis to profit from the behaviours in the market? This session reviewed how an awareness of these biases can be harnessed to ensure optimal investment decision making and practical ways of implementing investment strategies and included presentations from Daniel Melley, Global Head of Consultant Relations, Winton and Mark Wynn, Head of Finance, Cheshire West and Chester Council.

## 8. **Good governance and the LGPS**

Chaired by Joanne Segars, this session explored one of the Government's key criteria for pools; that they improve the governance of the LGPS. This session was led by Dawn Turner, Head of Pension Fund Management, Environment Agency, Mike Ellsmore, Chair of Local Pension Boards at Croydon, Southwark and Sutton and Karen McWilliam, Head of Public Sector Benefits Consultancy at Aon Hewitt.

Karen's presentation concentrated on the differing roles staff and members play as trustees of their local funds and the need to ensure whilst wearing the different hats everyone stays focused on their active role.

Mike's presentation reiterated the point that we shouldn't forget the good performance of the LGPS over the last 20 years (returning over 8%, being 5% above inflation) so we must be doing something right. The attributes of good governance are stability, consistency of approach, openness and taking the long-term view. As a consequence, we need to remember, when setting up the pools, that the financial obligation rests with the employers and not with the pool. It is important then that there is good communication to avoid employers feeling distant from the pools.

Dawn's presentation began with reminding everyone of fiduciary duty - 'an individual in whom another has placed the utmost trust and confidence to manage and protect property or money. The relationship wherein one person has an obligation to act to another's benefit'. As a consequence it is important as we move towards pools that there are proper transparent business plans and strategies in place, with excellent performance management and reporting and with the relevant risk management strategies, all focused on outcomes.

## 9. *Concurrent Sessions*

A number of concurrent sessions were delivered.

### a) The valuation – can you keep it simple please?

Leanne Johnston, Principal, Mercer and Euan Miller, Assistant Executive Director, Greater Manchester Pension Fund, discussed how deficits keep increasing despite assets have done well. The temptations that exist to pull complex levers to control them are inevitable. Whilst Leanne explained that the valuation process is simple, both argued that getting to the right answer in the valuation is rather complex. Especially as you have multiple employers, all with differing funding levels and deficit recovery periods, with differing covenants, differing member profiles and differing asset strategies. Consequently, standardised funding level comparisons are inevitably difficult.

### b) Investment regulations – investing in a world without restriction

Ralph McClelland, Associate Director, Sackers and Alex Younger, Investment & Actuarial Services Manager, Norfolk Pension Fund discussed what the new investment regulations ultimately mean, how funds should be approaching their investment strategy statements and what prudence means in the LGPS. Both presenters argued that the new regime would mean better transparency over decisions and that since pools were here the regulations would need to change. Both were also concerned by the extension of the Secretary of State's powers to intervene and although Marcus Jones MP had indicated earlier in the day how he would see these powers being used the drafting was far wider than anticipated.

### c) Managing Information

Kevin McDonald, Director, Essex Pension Fund, Jen Mullis, Assistant Director, Department for Business, Innovation and Skills and Matt White, Assistant Director, Department for Education discussed the role of education bodies in the LGPS scheme and the wider challenges and considerations bearing in mind the change in status of employers as well as new employers joining the scheme.

### d) What are the issues that face local pension boards

Open to members of Local Pension Boards (LPB) this session intended to set out the main issues facing LPB including legal status, their work programme and their role in the pooling.

## 10. **Combining forces**

Regardless of the many challenges associated with the day job, pooling is clearly at the top of everyone's agenda. In this session we had an opportunity to hear from Fiona Miller, Border to Coast and Matthew Trebilcock, Project Brunel on the progress these two pools are making. Sharing what are the real opportunities and challenges and how we ensure that all these pools will fit together.

Fiona and Matthew began with the summary of pooling and why we are here. The Border to Coast Pension Partnership (BCPP) will bring together 13 funds, with an asset value of £35.9bn, representing 905,995 members and 2,166 employers. The Brunel Pension Partnership (BPP) will bring together 10 funds, with an asset value of £23.2bn, representing 641,790 members and 1,537 employers. There appears to be some consistency across all proposals surrounding the governance, namely:

- a) On fund, one vote
- b) Equitable sharing of costs
- c) Asset allocation remaining with the funds
- d) Clear segregation between the Fund and the Pool
- e) Democratic accountability retained
- f) Three tiers of control
  - Supervisory entity
  - Executive body
  - Investment management
- g) Regulated structures where appropriate

Both also saw savings derived from external management fees, rationalisation of mandates and managers, moving from external to internal management and opportunities for investments. The speed of moving to internal and more passive management would depend on existing internal management capacity.

As a consequence of pooling the lead officers from each of the pools had had the opportunity to meet to 'check and challenge' progress and collaborate on proposals. Both presenters thought the biggest issues currently were the time to complete this work, balancing this with existing commitments, communication and the need for consistent support, guidance and advice.

In response to questions both Fiona and Matthew saw pooling as bringing more benefits and opportunities, as well as the ability to provide more resilience but it would be at an initial cost.

## 11. **Weathering new challenges**

The global economic climate remains somewhat cloudy, and the forecast calls for only the slightest chance of interest rate rises on this side of the Atlantic. Carl Tannenbaum, Chief Economist, Northern Trust gave a fascinating presentation on the economic prospects during the balance of 2016 and what can policy makers do to help clear the horizon. His conclusions were:

- The global outlook is cloudy, but he expects China to avoid a hard landing
- Performance will continue to be somewhat uneven, some regions and sectors are further along

- Risks to the outlook are varied, with the potential for complicated politics

In response to questions, particularly on increases in bond rates and inflation (William Bourne) Carl indicated that oil prices being so low was having an impact. As these rise so CPI will increase. One day interest rates will go up hence the argument for austerity now so as to avoid costs due to government debt being too high. However, in his view what was needed now was global infrastructure investment to boost global economic growth rather than debt reduction.

## 12. ***Investing for success***

One of the critical issues facing the new pools will be how to balance the investment needs of the participating funds with the requirement to reduce the overall number of mandates. This session was led by Julian Pendock, Investment Oversight Director, London CIV and Mark Wynn, LGPS Central Pool.

Mark began his presentation with an explanation of the Central Pool proposal including governance, very similar to Fiona Miller (Border to Coast) and Matthew Trebilcock, (Project Brunel) presentations. As the Fund would now concentrate on identifying the liability profile, the investment strategy and manage the relationships with the Pool (supplier and shareholder) there would be a number of roles he would be giving up, namely;

- Local implementation
- Manager oversight and monitoring
- Manager monitoring and due diligence
- Manager hiring and firing
- Resources

Julian gave a presentation on the progress of the London CIV which covered the aspect of not underestimating the time and cost to set it up as well as the very complex challenges and discussions that needed to be worked through. Julian's experience indicated that merging a large number of investment mandates into a few would take time and would need to build trust and confidence in all parties for it to be successful,

## 13. ***Transaction costs – clear as mud?***

We are now over a year into the new guidance for disclosing transaction costs. How have funds found the process of uncovering these costs, what more is to come and what is still missing? This session was led by Peter Dorward, Royal London Independent Governance Committee, David Kane, Head of Finance, West Midlands Pension Fund and Chris Hitchen, Chief Executive, RPMI.

This was a very dry subject and it was a difficult task for the presenters to make this an exciting session. Most of the session surrounded the changes made by Cipfa into the task of identifying transactional costs with all management fees but, as this is not compulsory, no one yet has been brave enough to do so. Although this may add to the transparency agenda they could be open to misinterpretation and it was doubtful they would add to the comparative data debate. This proved to be an area where further work was required.

## 14. ***Best practice for employers participating in the LGPS***

It's no secret that the number of employers is expanding rapidly and that the challenging economic climate is making life difficult for admitted bodies. The 2016 valuation is likely to bring new challenges and difficult discussions. So how do employers looking to participate in

the scheme get on the front foot? This session was led by Helen Forrest Hall, Policy Lead: DB, Pensions and Lifetime Savings Association, John Prior, Principal, Punter Southall and Nick Stones, Partner, Pinsent Masons.

Again this proved to be a disappointing debate with most of it concentrating on issues that new employers, especially small contractors, may face in joining the LGPS.

#### 15. **Political Reality**

The conference concluded with Michael Crick, Political Journalist & Broadcaster giving his views on the interesting political times in which we now live, from local, Scottish and Mayoral Elections in early May, to an EU referendum in June and the US General Election in November. He went on to hypothecate on what the future may look if the EU referendum meant exit, Boris Johnson could be Prime Minister and Donald Trump could be on his way to the Whitehouse.

### **Statutory and Policy Implications**

16. This report has been compiled after consideration of implications in respect of finance, the public sector equality duty, human resources, crime and disorder, human rights, the safeguarding of children, sustainability and the environment and those using the service and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

### **RECOMMENDATIONS**

- 1) That it be noted that attendance at key conferences is part of the Fund's commitment to ensuring those charged with decision-making and financial management have effective knowledge and skills.
- 2) That the report be noted

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#### **Constitutional Comments**

17. Because this report is for noting only, no Constitutional Comments are required.

#### **Financial Comments (SRC 29/05/16)**

18. There are no direct financial implications arising from this report.

#### **Background Papers**

None