Hackney

REPORT OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES		
Pension Fund Budget 2017-18 **Pensions Committee** **29th March 2017**	**Classification** **PUBLIC** **Ward(s) affected** **ALL**	Appendices 1 **AGENDA ITEM NO.**

1. INTRODUCTION

1.1 This report presents the budget for the Pension Fund for 2017-18 and indicative for the following 2 years, along with an update of the 2016/17 outturn vs budget. It considers income and expenditure from various sources and the impact on these for the Pension Fund in the next financial year.

2. RECOMMENDATIONS

2.1 The Committee is recommended to:

- **Approve the budget for 2017-18 attached at Appendix 1.**

3. RELATED DECISIONS

3.1 Pensions Committee 23rd March 2016 – Pension Fund Budget Report 2016-17.

4. COMMENTS OF THE GROUP DIRECTOR, CORPORATE FINANCE AND RESOURCES

4.1 As part of the constitutional responsibilities for the Pensions Committee it is required to set an annual budget and then to monitor that budget. This report sets out the budget forecast for the financial year 2017/18. In addition, the prior year budget is compared against projected income and expenditure.

4.2 Sound financial management of the Pension Fund, including budget-setting, helps ensure that the Pension Fund is run in an efficient and cost-effective manner. Poor management of the Pension Fund finances would result in increased costs, which would need to be met through higher employer contributions to the Pension Fund.

5. COMMENTS OF THE DIRECTOR, LEGAL

5.1 The Committee's terms of reference provide the responsibility for setting an annual budget for the operation of the Pension Fund and for monitoring income and expenditure against the budget.

5.2 In considering the draft budget the Committee must be clear that the financial assumptions on which the budget is based are sound and realistic. It must also satisfy itself that the budget is robust enough to accommodate the potential pressures outlined in the report whilst ensuring that the fund is managed as efficiently as possible to maximise the benefits to members of the Scheme.

5.3 There are no immediate legal implications arising from this report.

6. SUMMARY

6.1 Under the London Borough of Hackney Constitution Terms of Reference for the Pensions Committee, the Committee has responsibility to set an annual budget for the operation of the Pension Fund and to monitor income and expenditure against budget. This report is being put before the Committee to enable it to fulfil this responsibility.

6.2 Due to the volatility that exists within most areas of the Pension Fund Account, preparing a budget for the Pension Fund is complex. Both investment income and management fees are subject to the vagaries of investment market performance, and are thus largely outside the control of the Pension Fund. This element of the budget, therefore, cannot be predicted with any great degree of certainty. As such, no forecast is being made at this stage for the change in the market value of investments, or for any profit or loss suffered on their disposal. It is, however, fully recognised that any movement in the value of Fund assets will have significant impact on the overall funding level, and on the actuarial valuation and contributions set by the Fund Actuary.

6.3 Member income and expenditure can be significantly impacted by transfers of staff either through natural changes or with staff subject to TUPE transfer and by the number of deaths and retirements that can occur during the year.

6.4 The appendix to this report sets out the budget for 2017/18 and includes the expected outturn against budget for 2016/17. The budget will be monitored on a quarterly basis in the Pension Fund Quarterly Update.

7. 2016-17 BUDGET UPDATE

7.1 The contribution figures presented in this budget update for the current financial year reflect slightly higher levels of member income than budgeted. Employer and employee contributions are both significantly over budget, at £62.8m and £12.2m respectively, whilst the difference is reduced by lower than expected levels of transfers in. A major driver behind the variance is that active membership numbers have continued to rise, whilst the budget predicted a 5% year on year reduction. Additionally, the cessation of Hackney Homes as an employer and TUPE of its staff to the Council has resulted in the higher Council rate being paid for these members. Staff received a 1.0% payrise from 1st April 2016, just below the budgeted figure of 1.1%. With the exception of the Hackney Homes cessation and TUPE, contribution rates paid are largely unchanged since 2014/15 and have therefore had only a small impact on member income relative to last year.

7.2 At £41.6m, the forecast for pensions paid is slightly above the budgeted level of £40.2m. No Pensions Increase was payable for 2016/17, so increasing pensioner numbers have been the main driver of increases to pensions in payment.

7.3 Lump sum commutations and death grants are above the budgeted amount, at £13.3m compared to £11.0m; however, these are outside of the Fund's control and cannot be accurately forecasted. At £6.6m, transfers out are forecasted to be somewhat higher than the £4.7m budgeted. The budget was doubled for 2015/16 as a result of the Government's Freedom and Choice agenda; however, the expected increase in transfers out did not materialise. Given the low level of enquiries received during 2016/17, the increase does not appear to have resulted from Freedom and Choice

7.4 Forecast Administration costs are slightly below budget for 2016/17, at £764k compared to a budget of £789k. , Expenditure on Oversight and Governance is under budget at £366k compared to a budget of £425k. This reflects reduced consultancy costs relative to 2015/16, largely as a result of significant one-off costs, such as the audit of Equiniti's implementation of LGPS2014, charged during 2015/16.

7.5 Forecast Investment expenses are notably higher than budgeted at £3.7m compared a budgeted value of £2.5m. The bulk of this increase has resulted from an adjustment to the budget to ensure that fee estimates are included within the budget for managers who do not invoice directly. Whilst these are recorded in the accounts they have not previously been incorporated into budgeted figures. Investment income is lower than forecast at £13.1m compared to £14.3m; however, investment income for the final quarter is challenging to forecast.

8.0 2017/18 PENSION FUND BUDGET

8.1 Contributions for the next financial year are forecast at £60.0m (employer) and £12.3m (employee), representing a reduction for employer contributions and slight increase for employee contributions. The forecasts assume a 1.1% salary increase for 2017/18, as per the previous budget, which is assumed to apply to each of the next 3 years. Although officers are not aware at this stage of large scale restructures that will significantly affect active membership, ongoing austerity measures make it prudent to assume some downward pressure on staff numbers.

8.3 Employer contributions are assumed to reduce in line with the planned reduction in the Council's contribution rate over 3 years, from 36.9% at present to 33% by 2019/20. Employee contribution rates are forecast to remain at current levels; given that amendment is possible only at a national level, any change will not be immediate. However, it should be noted that this valuation cycle will see the first full scheme level valuation, with the potential for use of the Treasury or Scheme Advisory Board cost management processes. This could result in changes to employee contributions or member benefits, leading to potentially significant changes in the Fund's cashflow and funding level.

8.4 For pensions paid, an inflationary increase of 1% has been applied for 2017/18, following the release of the September-September CPI results. An increase of 2% has been forecast for 2018-19 and 2019-20. The number of pensioners is also forecast to increase by 2% year on year. Transfers out depend very much on individual member decisions and are difficult to forecast with any certainty; as such, the current year forecast has been used. After very little impact in the first two years, no allowance has been made for additional transfers out as a result of the Freedom and Choice agenda. Overall, the current net member surplus is expected to reduce over the next 3 years, as a result of reducing contributions and increased member expenditure.

8.5 Costs of running the Pension Fund are expected to increase over the next 3 years, with a 1% rise forecast for 2017/18 and 2% per annum thereafter. After considerable changes to scheme administration and governance during 2014/15 and 2015/16 it is hoped that the cost of administering the scheme will stabilise; however, it should be noted that any further significant changes to the scheme would be likely to result in additional cost.

8.6 It is hoped that savings can be made from closer collaborative work and fee savings as the Fund sees the benefits from the London CIV. No allowance has been made for this in the budget owing to uncertainty over the potential timescales to transition assets. It is expected that, if it maintains its current asset allocation, the Fund will see a reduction in investment management fees paid as assets are moved over to the CIV. However, given the Government's push to enable greater infrastructure investment, it is possible that some of these savings might be offset through a move towards more complex asset classes. It should also be noted that fees are, to a large extent, dependent on the value of assets under management; fees payable in future will therefore be heavily dependent on investment performance.

8.7 Cashflow for the Pension Fund is expected to be positive in 2017/18, with a £19.8m inflow forecasted. This represents a slight drop compared to 2016/17s forecasted £25.0m; more significant reductions are forecast over the next 3 years, driven mostly by changes in the balance between member income and expenditure. However, as previously discussed, many of the forecast changes are of an uncertain nature, making it difficult to forecast future cashflows with accuracy. As the most significant drivers of the Fund's cashflow are those associated with member income and expenditure, any future changes to membership numbers, salaries and contribution rates are likely to have significant impact.

8.8 As in previous years, no forecast is being made of the change in market value or growth in the investment portfolio due to the unpredictable and volatile nature of financial markets.

8.9 The full breakdown of the budget for 2017/18 is included as an Appendix to this report along with projections for the following 2 years. The report also shows the actual projection of the 2016/17 Pension Fund revenue account based on actuals up to December 2016.

Appendices

Appendix 1 – 2017-18 Budget

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Background Papers

None