Hackney

REPORT OF THE GROUP DIRECTOR, FINANCE & CORPORATE RESOURCES		
Pension Fund – Quarterly Update **Pensions Committee** **23rd July 2018**	**Classification** **PUBLIC** **Ward(s) affected** **ALL**	**Enclosures** **Three**

1. INTRODUCTION

1.1 This report is an update on key quarterly performance measures, including an update on the funding position, investment performance, engagement and corporate governance, budget monitoring, administration performance and reporting of breaches.

2. RECOMMENDATIONS

2.1 The Pensions Committee is recommended to note the report.

3. RELATED DECISIONS

- Pensions Committee 29th March 2017 – Approval of Pension Fund Budget 2017/18
- Pensions Committee 29th March 2017 – Approval of 2016 Actuarial Valuation and Funding Strategy Statement

4. COMMENTS OF THE GROUP DIRECTOR OF FINANCE & CORPORATE RESOURCES

4.1 The Pensions Committee acts as quasi-trustee of the London Borough of Hackney Pension Fund and as such, has responsibility for all aspects of the Pension Fund. Quarterly monitoring of the key financial variables which impact the Fund is crucial to ensuring good governance.

4.2 Monitoring the performance of the Fund and its investment managers is essential to ensure that managers are achieving performance against set benchmarks and targets. Performance of the Fund's assets will continue to have a significant influence on the valuation of the scheme's assets going forward. The investment performance of the Fund is a key factor in the actuarial valuation process and therefore directly impacts on the contributions that the Council is required to make into the Pension Scheme.

4.3 The Committee's responsibilities include setting a budget for the Pension Fund and monitoring financial performance against the budget. Quarterly monitoring of the budget helps to ensure that the Committee is kept informed of the progress of the Fund and can provide the Committee with early warning signals of cashflow issues and cost overruns.

4.4 Reporting on administration is included within the quarterly update for Committee as best practice governance. Monitoring of key administration targets and ensuring that the administration functions are carried out effectively will help to minimise costs and ensure that the Fund is achieving value for money.

4.5 Whilst there are no direct immediate impacts from the information contained in this report, quarterly monitoring of key aspects of the Pension Fund helps to provide assurance to the Committee of the overall financial performance of the Fund and enables the Committee to make informed decisions about the management of the Fund.

5. COMMENTS OF THE DIRECTOR OF LEGAL AND GOVERNANCE

5.1 The Pensions Committee, under the Council's Constitution, has delegated responsibility to manage all aspects of the Pension Fund.

5.2 The Local Government Pension Scheme Regulations 2013, Regulation 62, requires an Administering Authority to obtain an actuarial valuation of its fund every 3 years. The last valuation was carried out as at 31st March 2016, with the next due in 2019. There is no requirement for the Administering Authority to undertake interim valuations, although it has the ability to do so. Nevertheless, given the volatility of the financial markets it is a matter of good governance and best practice to monitor funding levels between formal valuations to ensure that all necessary steps can be taken in advance of any valuation.

5.3 The Council must monitor the performance of the pension fund in order to comply with its various obligations under the Local Government Pension Scheme Regulations. Those obligations include monitoring performance of investment managers and obtaining advice about investments. Ultimately the Council is required to include a report about the financial performance of the Fund in each year in the Annual Report. The monitoring of performance of the Fund is integral to the functions conferred on the Pensions Committee by the Constitution. The consideration of the present report is consistent with these obligations.

5.4 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. 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.

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

6. FUNDING POSITION BASED ON 2016 TRIENNIAL VALUATION

6.1 The Fund's actuary, Hymans Robertson, provides a quarterly update on the funding position of the Fund illustrating how the overall position has changed since the last actuarial valuation. The actuarial valuation as at 31st March 2016 set the contribution rates which have been applied from 1st April 2017. As at the end of March 2018, the funding level was 80.5% compared to 77% as at the end of March 2016.

6.2 The funding level of 80.5% at 31st March is based on the position of the Fund having assets of £1,497m and liabilities of £1,860m, i.e. for every £1 of liabilities the Fund has the equivalent of 80.5p of assets. It should be noted that the monetary deficit remains high and has increased slightly from £350m in March 2016 to £362m in March 2018.. The liabilities are a summation of all the pension payments which have been accrued up to the valuation date in respect of all scheme members, pensioners, deferred members and active members. These will be paid over the remaining lifetime of all members, which could stretch out beyond 60 years. The actuary then calculates the contributions which would be required in order for the Fund to meet its liabilities in respect of benefits accruing and to recover any deficit which has arisen.

6.3 The progress of the funding level on both an ongoing and yield curve basis is shown in the Actuary's Funding and Risk Report at Appendix 1 to this report. The report also highlights the asset risks to which the Fund is exposed, providing a basic breakdown of the Fund's asset allocation along with returns of major asset classes since 31st March 2016.

7. GOVERNANCE UPDATE

7.1 The introduction of asset pooling for LGPS funds has resulted in a need for constitutional change in administering authorities, to ensure that the new asset pools are properly recognised within the governance structure of funds. An important part of these changes is updating Pensions Committees' Terms of Reference, to ensure that the ongoing role of Committee members in asset allocation is recognised and to set out their new role in representing individual funds within the pools.

7.2 The proposed changes to the Terms of Reference for the Hackney Pensions Committee will need to be approved by Full Council; however, prior to this, Committee Members will be consulted to ensure that they have a full understanding of the changes and are satisfied that the Committee will continue to function effectively as the decision making body for the Pension Fund.

7.3 The proposed changes include a section updating the appointments procedure for co-opted scheme members and employer representatives on the Committee, to bring the process more into line with that used for the Pension Board representatives.

8. INVESTMENT UPDATE

8.1 Appendix 2 to this report provides a manager performance update from the Fund's Investment consultants, Hymans Robertson. The report includes an analysis of quarterly, 1 year and 3 year performance against benchmark, as well as Hymans Robertson's current ratings for each manager.

8.2 It should be noted that considerable changes have been made to the Fund's equity portfolio since the reporting date. The Lazard, Wellington and UBS mandates referred to in the report are no longer held by the Fund. Full details of the transition can be found in the paper 'Equity Restructure – Post-completion update'

9. BUDGET MONITORING

9.1 The Pension Fund budget for 2017/18 was approved by Pensions Committee at its 29th March 2017 meeting. The paper presented set out rolling forecast budgets to 2018-19, which predict an ongoing cash flow positive position for the Fund. The budget is shown in the table below.

9.2 The Fund has recently to a new company setup within the Council's accounting system which, when set up, will permit more detailed in year reporting. The 2018/19 budget will be available at the September 2018 meeting, and will be fully aligned to the new company setup. A full assessment of 2017/18 costs against budget will be included in the report

Description	2016/17 Outturn £'000	2017/18 Budget £'000	2018/19 Budget £'000	Comments
Member Income				
Employers' Contribution	67,162	59,387	57,849	Future forecasts based on 2016/17 forecast with an assumption that employer contributions will reduce in line with the Council's proposed reduced rates. Active membership numbers are assumed to reduce by 1% pa, with an assumed 1% pa pay rise. Budget to be revised and realigned with 2016/17 outturn.
Employees' Contribution	12,155	12,293	12,416	See Above
Transfers In	4,719	3,560	3,560	16-17 forecast figure used to forecast - the level of transfers in is outside the Fund's control
Member Income Total	84,036	75,239	73,824	
Member Expenditure				
Pensions	(41,807)	(42,904)	(44,637)	Future forecasts based on 2016/17 forecast. A Pensions Increase rate of 1% has been applied for 2017/18, with 2% applied for each of the following years. A year on year increase in the number of pensioners of 2% has been applied across the 3 year period
Lump Sum Commutations and Death Grants	(13,547)	(13,736)	(14,291)	Uses assumptions as above, but challenging to forecast as this is outside the Fund's control.
Refund of Contributions	(201)	(178)	(182)	Adjusted for CPI as per above with a 1% uplift for 2017/18, followed by 2% pa thereafter
Transfers Out	(5,632)	(6,633)	(6,633)	2016/17 forecast used for following 3 years. Transfers out are challenging to estimate as they are outside the Fund's control.

Member Expenditure Total	(61,187)	(63,451)	(65,743)	
Net Member Surplus	22,849	11,788	8,081	
Management Expenses				
Administration, Investment Management and Governance & Oversight	(5,869)	(4,922)	(5,008)	Forecast based on 2016/17 forecast, with a 1% uplift for 2017/18, followed by 2% pa thereafter. Budget to be revised and realigned with the final outturn.
Net Administration Expenditure	(5,869)	(4,922)	(5,008)	
Surplus from Operations	16,980	6,866	3,073	
Investment Income/Expenditure				
Investment Income	14,423	13,105	13,105	Investment income expected to remain constant across the period. Budget to be revised in line with 2017 outturn
Net Investment Income/Expenditure	14,423	13,105	13,105	
Cash Flow before Investment Performance	31,403	19,971	16,178	

10. RESPONSIBLE INVESTMENT UPDATE

10.1 The Pensions Committee has looked to increase the level of engagement with the underlying companies in which it invests. This includes taking a more proactive role in encouraging managers to take into consideration the voting recommendations of the Local Authority Pension Fund Forum (LAPFF). This section of the quarterly report therefore provides the Committee with an update on the work of the LAPFF and also voting recommendations and how managers have responded. In addition the update will include key topical issues concerning environmental and social governance issues in order to provide scope for discussion on these key issues.

10.2 During the quarter, LAPFF did not issue any voting alerts for companies directly held by the Fund, so no specific instructions were provided to Fund managers.

10.3 The LAPFF Quarterly Engagement report is attached at Appendix 3 to this report, setting out LAPFF's engagement activity over the Quarter in relation environmental, social and governance issues.

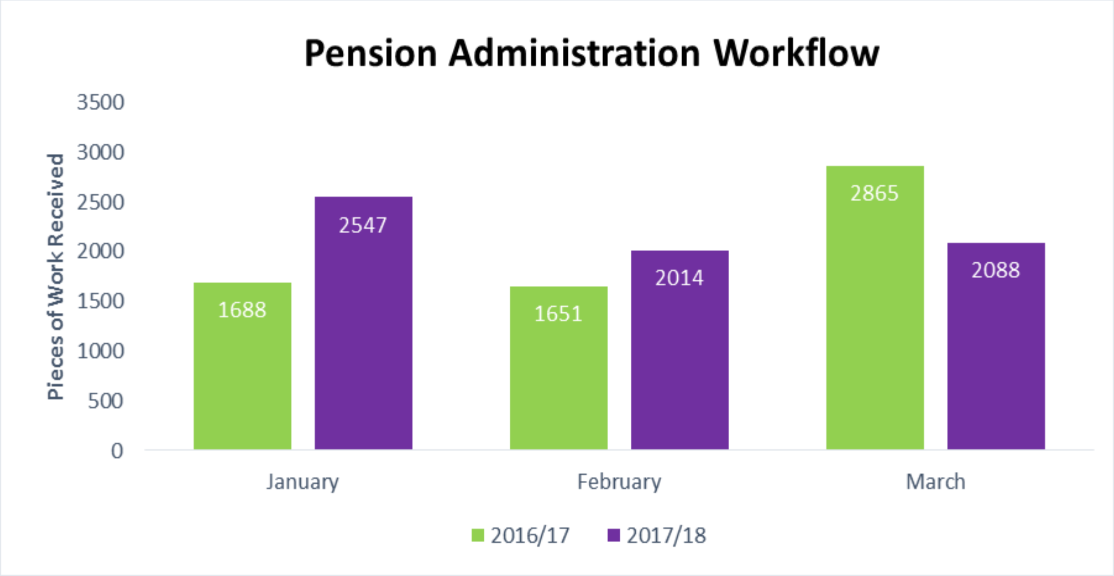
10.4 Following the restructuring of its equity portfolio, the Fund no longer retains any segregated mandates. It is therefore now key for the Fund to engage with its new pooled fund managers (BlackRock and the London CIV) and to develop a new approach to voting and engagement which is practical to implement in a pooled fund context. An indepth review of this area is planned for Autumn 2018 with a paper due to go to the December 2018 Pensions Committee meeting.

11. PENSION ADMINISTRATION

11.1 Pension Administration Management Performance

The case load for the administrators during Q4 2017/18 has decreased slightly in comparison to the same period in 2016/17. A total of 6,649 new cases were received during the current quarter, compared to 7,035 during Q4 in 2016/17

A comparison of the workflow for the administrators between Q4 2016/17 and the reporting quarter is set out below:-

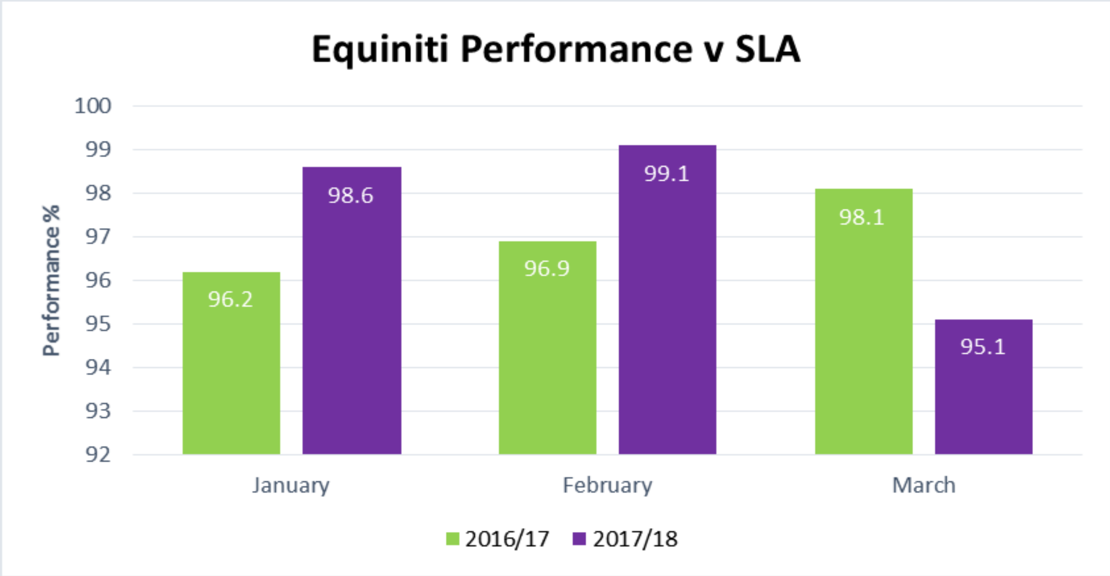


The average number of pieces of work received per month during Q4 2017/18 was 2,216 compared to an average of 2,345 received during the same period in 2016/17.

Much of this workload is attributed to the Council being the main employer in the Fund. Starter, opt-out outs, leavers and pay changes continue to be done manually as the new iTrent interface from the Council's payroll system is still under construction by Hackney's ITC.

The performance of the pension administrators is monitored by the Financial Services Section at Hackney on a monthly basis. Equiniti are working under a 'relaxed SLAs' regime due the number of data queries taking priority over the business as usual (BAU). Therefore performance against the service level agreement (SLA) is being monitored against priority work only (death grants, bank detail changes, pension into payment; i.e. all work relating to financials), and remains at an average of 97.6% for Q4 2017/18, compared to 99.9% for the same quarter last year.

The administrator's performance against the SLA for Q4 2016/17 and Q4 of the reporting period 2017/18 is set out below:



The volume of manual processing is still significantly above the norm. The majority of the additional work is due to the continued lack of an interface from the Council's payroll provider that is fit for purpose. The Council is the largest employer in the Fund and has the majority of the work.

It is hoped that the introduction of the Council's new payroll system will decrease the level of manual processing required. However, delays to the development of interfaces, monthly contribution reports and problems with some of the data transferred to the new payroll system, have meant that the administrators are unable to verify the accuracy of member data. Nor can they confirm the correct contributions are being paid by the Council and its LGPS members, as monthly reports are still not being provided by payroll to Equiniti. This is contrary to tPR compliance.

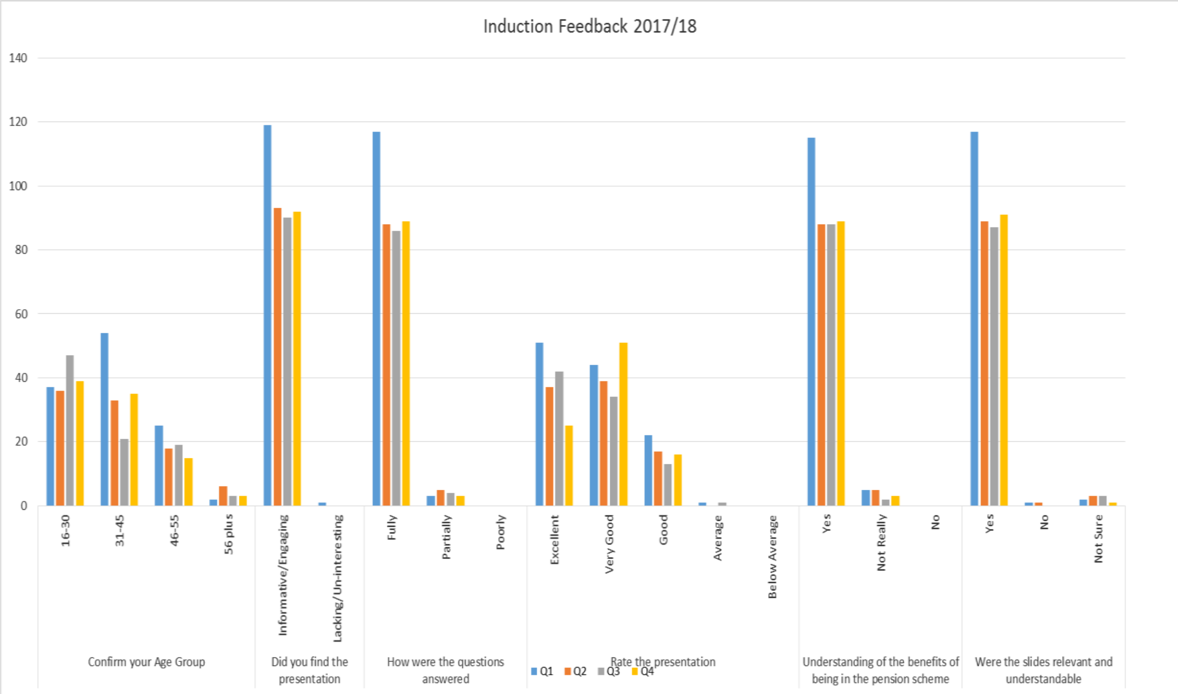
11.2 **New Starters and Opt-Outs**

	Total Active Membership at End of Quarter	Total Opt Outs For Quarter
Q4 2016/17	7,685	100
Q4 2017/18	7,522	112

The opt-outs in Q4 2017/18 remain in-line with previous months and average around 100 per month. The membership remains stable at 7,500.

11.3 **Scheme Administration**

The Financial Services in-house pension team facilitated at weekly induction sessions for 92 new employees during the reporting period. These sessions continue to receive very positive feedback with respondents rating the presentations as 'Very Good' or 'Excellent', and those who attended the sessions, have said they now have a greater understanding of the benefits of being in the scheme



11.4 **Ill Health Pension Benefits.**

The release of ill health benefits fall into 2 main categories, being those for deferred and active members. The Financial Services in-house pension team process all requests for the release of deferred member's benefits on the grounds of ill health, as well as assisting the Council's Human Resources team with the process for the release of active member's benefits on the grounds of ill health.

Deferred member's ill health benefits are released for life and are based on the benefits accrued to the date of leaving employment, with the addition of pension increase, but they are not enhanced by the previous employer.

Active members' ill health pensions are released on one of three tiers:

- Tier 1 - the pension benefits are fully enhanced to the member's normal retirement date and is typically only paid to those with very serious health conditions or life limiting health problems – paid for life, no review

- Tier 2 – the pension benefits are enhanced by 25% of the years left to the member's normal retirement date - paid for life, no review

- Tier 3 - the pension benefits accrued to date of leaving employment - paid for a maximum of 3 years and a review is undertaken once the pension has been in payment for 18months.

For tier 3, a scheme member's prognosis is that whilst they are unable to fulfil their current role on medical grounds to retirement, they may be capable of undertaking some form of employment in the relatively near future. However should the members' health deteriorate further, there is provision under the regulations for their benefits to be uplifted from tier 3 to tier 2, if the former employer agrees that their health condition meets the qualifying criteria for the increase.

The chart below sets out the number of ill-health cases that have been processed during Q4 of 2017/18, compared to the same period in the previous year.

DEFERRED MEMBER'S ILL HEALTH RETIREMENT CASES					
	CASES RECEIVED	SUCCESSFUL	UNSUCCESSFUL	ONGOING	WITHDRAWN
Q4 2106/17	3	0	1	2	0
Q4 2107/18	2	0	0	2	0

ACTIVE MEMBER'S ILL HEALTH RETIREMENT CASES					
	CASES RECEIVED	BENEFITS RELEASED ON TIER 1	BENEFITS RELEASED ON TIER 2	BENEFITS RELEASED ON TIER 3	UNSUCCESSFUL
Q4 2016/17	1	1	0	0	0
Q4 2017/18	3	2	0	1	0

11.5 Internal Disputes Resolution Procedure (IDRP)

This is the procedure used by the Fund for dealing with appeals from members both active and deferred. The majority of the appeals are in regard to either disputes around scheme membership or the non-release of ill health benefits. The process is in 2 stages:-

- Stage 1 IDRP's are reviewed and determinations made by a senior technical specialist at the Fund's pension administrators, Equiniti.

- Stage 2 IDRP's are determined by the Group Director, Finance & Corporate Resources taking external specialist technical advice from the Fund's benefits consultants.

The following case was concluded in the 4th quarter 2017/18:

<u>Stage 1</u>

Member not awarded ill health retirement benefits by the employer. Member appealed employer's decision.
Stage 1 review advised employer that due process had been correctly followed and full consideration was applied when reviewing the evidence.
The appeal was not upheld.

11.6 Other work undertaken in Q4 2017/18

<u>Third Party Administration</u>

Following the procurement exercise for Third Party Pension Administrators using the National LGPS Framework, the Pensions Committee met on 25 April 2017 and approved the award of the contract to Equiniti, the previous holders of the contract.

As reported to Committee in December 2017, the delivery of the new service specifications has been delayed, monthly interfaces have not been available to test and the administration system at Equiniti has yet to be reconfigured to accept the full monthly data reports. Therefore, it was agreed by both parties to delay the contract commencement date of 1 January 2018 to 1 April 2018.

Despite good progress being made in many areas of the new specification during the *'go-live'* extension period, there were still a number of essential points of delivery that had yet to be completed such as monthly interface, monthly MI reporting in relation to SLAs and KPIs, website & secure portal with guides and factsheets. Due to these continued delays, the Council has agreed to once again extend the commencement date from 1 April to 1 July 2018. If the full service specification is not delivered on 'go-live' day, it could result in retention of fees payable to Equiniti, until the specification is delivered to a reasonable standard.

Redundancy Exercises for Departmental Budget Purposes

In Q4 of 2017/18, the in-house pensions' team have received a total of 101 redundancy estimate requests, compared to 91 for the previous quarter, some of these are for members over the age of 55 who will have pension released. Of the 101 requests, only 10 employees received final paperwork and left the organisation by the end of March 2018.

Pre-retirement workshops

During the Q4 2017/18, the Pensions Team have set up a series of 'Pre-retirement workshops', aimed at members who are thinking of retiring within the next 2 to 5 years. These workshops will begin in May 2018 and run bi-monthly until January 2019, and will be in conjunction with a company called Affinity Connect. Affinity specialise in providing seminars/workshops on various aspects of pension and employment issues, such as retirement (as mentioned), mid-career financial planning and redundancy. Affinity provide the facilitator, learning material and bookings for the seminars/workshops free of charge to the Fund. If this first series of workshops is successful, we aim to roll these workshops out on an annual basis.

Annual Employers Forum

The annual Employer Forum was held on 9 March 2018, and was attended by 14 of the Fund employers, including 7 schools. The Forums agenda was varied and covered subjects from employer roles and responsibilities, year-end timetable & processes, and the commencement of GDPR from 25 May 2018. Equiniti presented on the importance of correct & timely data; AON provided a presentation on *'pension hot topics'*; the Pensions Regulator (tPR) on the importance of compliance with COP14, and finally the Prudential on AVCs.

Pensions Administration Strategy (PAS)

During Q4 of the reporting period, an updated PAS was finalised and brought to Pensions Committee in March 2018 prior to its distribution to schools and employers in the Fund. The updated PAS includes greater emphasis on the role of the Regulator (tPR) and its powers of enforcement, and also the responsibility of the Fund to report material failures of employers, and breaches of the law, to the tPR.

Newsletters

The Pensions Team produced their quarterly Newsletter at the end of March 2018, which was issued to both Employers and Schools/Academies within the London Borough of Hackney Pension Fund. The newsletter covered the 2017/18 Year End process and data needed from employers & payrolls to produce the 2018 Annual Benefit Statements, a round-up of the Employer Forum held on 9 March, how to identify fraudulent requests for personal pension information and the new LGPS contribution bands from 1 April 2018.

12. REPORTING BREACHES

12.1 As previously reported, the Fund continues to engage with the Pensions Regulator in regard to the 1,600 outstanding Annual Benefit Statements from 2016/17 year-end. Data investigations have continued and good progress has been made with approx 1,200 records being resolved by the in-house pension team. The remaining 400 data queries, which relate to LB Hackney employees, are unconfirmed leavers and/or opt-outs and once the correct information has been received from payroll, the record will be corrected and a deferred benefit statement issued.

12.2 This is the 3rd year the Fund has been required to submit a report to the Regulator concerning this issue. This issues has been raised at the highest level of the Council; accurate membership data is of increasing importance since the introduction of the CARE scheme, and it is critical that the problems with the Council's membership data submissions are resolved. Officers of the Fund continue to work with the Council's new payroll system, iTrent, and Equiniti to produce a working interface.

Ian Williams
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Appendices:
Appendix 1 –Funding & Risk Report (Hymans Robertson – Actuary)
Appendix 2 – Manager Performance Report (Hymans Robertson – Investment Consultant)
Appendix 3 – LAPFF Engagement Report Jan-March 2018

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