Hackney

REPORT OF THE GROUP DIRECTOR, FINANCE & CORPORATE RESOURCES		
Quarterly Update Report **Pensions Committee** **15th March 2021**	**Classification** **Public** **Ward(s) affected** **ALL**	**Enclosures** **Three** **AGENDA ITEM NO.** **7**

1. INTRODUCTION

1.1 This report is an update on key quarterly performance measures, including an update on the funding position, fund governance, investment performance, responsible investment, administration performance and reporting of breaches. It provides the Committee with information on the position of the Fund between October and December 2020.

2. RECOMMENDATIONS

2.1 The Pensions Committee is recommended to note the report.

3. RELATED DECISIONS

- Pensions Committee (Urgency Delegation March 2020) – 2019 Final Valuation Report and Funding Strategy Statement
- Pensions Committee 29th March 2017 –Investment Strategy Statement
- Pensions Committee 26th March 2019 –Pension Administration Strategy (PAS)

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

4.1 The Pensions Committee has delegated responsibility for management of the Pension Fund. Quarterly monitoring of key aspects of the management of the Pension Fund is good practice and assists the Committee in making informed decisions. .

4.2 Monitoring the performance of the Fund's 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 Reporting on administration is included within the quarterly update for Committee as best practice. 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.

4.4 Whilst there are no direct 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's Terms of References sets out its responsibility for management of the Pension Fund. The Committee has delegated responsibility:

- To make arrangements for the triennial actuarial valuation, monitor liabilities and to undertake any asset/liability and other relevant studies as required.
- To monitor the performance and effectiveness of the investment managers and their compliance with the Statement of Investment Principles (Investment Strategy Statement).
- To set an annual budget for the operation of the Pension Fund and to monitor income and expenditure against budget.
- To act as Scheme Manager for the Pension Fund

5.2 Given these responsibilities, it is appropriate for the Committee to consider a regular quarterly update covering funding and investment matters, budget monitoring and scheme administration and governance.

6. FUNDING UPDATE

6.1 The Fund's actuary, Hymans Robertson, provides a quarterly funding and risk report illustrating how the overall position has changed since the last actuarial valuation. This is shown at Appendix 1 to this report. The results are presented on the basis of the 2019 valuation, using rolled forward assumptions updated for changes in the Fund's expected future investment return, which changes according to economic conditions.

6.2 As at the end of December 2020, the funding level based on the 2019 valuation was 92% compared to 91% as at the end of March 2019, an improvement from 87.7% previously reported as at end September 2020.

6.3 The funding level of 92% at December 2020 is based on the position of the Fund having assets of £1,757m and liabilities of £1,907m, i.e. for every £1 of liabilities the Fund has the equivalent of 92p of assets. The monetary deficit remains high, increasing from £131m in March 2019 to £150m in December 2020 but this represents a significant improvement on September when it stood at £228m. 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.

6.4 As can be seen from the above, the markets remain volatile with asset values being affected by developments in the Covid-19 pandemic and other economic factors and sentiments. The valuation of liabilities are affected by the expected future return on investments, an estimate of the Fund's annualised return over 20 years. This changes as economic conditions fluctuate, with a reduction in the expected return resulting in a higher present value placed on liabilities.

7. GOVERNANCE UPDATE

7.1 As set out in the previous Quarterly Update Report, officers of the Fund provided responses to a governance survey issued by Hymans Robertson. The survey was commissioned by the LGPS Scheme Advisory Board and asked respondents to consider the governance of the LGPS and potential conflicts of interest between the pensions function of administering authorities and their host local authority. The survey focused on financial decision-making and the role of the s151; officers considered that a number of the suggestions represented good practice (e.g. approval of pension fund budgets by pensions committees) but recommended against radical change to existing structures.

7.2 The responses to the survey and Hymans Robertson's initial report have now been considered by the Scheme Advisory Board (SAB). A Phase II report has now been published on the SAB website and sets out a number of recommendations across 2 workstreams; Standards & Outcomes and Compliance & Improvement.

7.3 To allow local government officers to concentrate on priority matters during the Covid emergency, the SAB agreed that the Phase III Implementation Working Group should be stood down until further notice. However, in February 2021, Hymans issued its Good Governance Phase III report to the Scheme Advisory Board. It states that it was considered that some proposals from Phase 2 didn't need further detail in order to progress with implementation and focussed on the proposals which needed further analysis or consideration ahead of implementation. The report provides additional details on these proposals for the consideration of the SAB. A more detailed update on the proposals will be presented to the Pensions Committee at its next meeting. The Hymans Report to SAB can be found at the following web address: https://www.lgpsboard.org/images/Other/Good_Governance_Final_Report_February_2021.pdf

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. The report shows that the Fund performed strongly over the quarter as risk assets rallied following strong return in equities (particularly in emerging markets), and a reduction in yields and credit spreads. Over the quarter the Fund has outperformed the benchmark by 1.1% and the high level asset allocation is broadly in line with target.

9. RESPONSIBLE INVESTMENT UPDATE

9.1 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.

9.2 The LAPFF Quarterly Engagement report is attached at Appendix 3 to this report, setting out LAPFF's engagement activity over the Quarter in relation to environmental, social and governance issues. Following the restructuring of its equity portfolio, the Fund no longer retains any segregated mandates and therefore has no direct holdings in the companies referenced. It does, however, retain exposure via its pooled passive funds to a large number of the companies LAPFF engages with.

9.3 As can be seen from the LAPFF Quarterly Update Report, much of the engagement with companies has continued to focus on climate change issues and have supported the "Say on Climate" initiative. They have also continued to focus on social issues including meetings with the chairs of AngloAmerican and Glencore regarding engagement with those communities affected by their activities. In addition to this LAPFF have started engaging with companies in relation to the investments in Israeli-Palestinian territories. They have determined a preliminary list of seventeen companies with which to engage and engagements with three of these have occurred over the quarter.

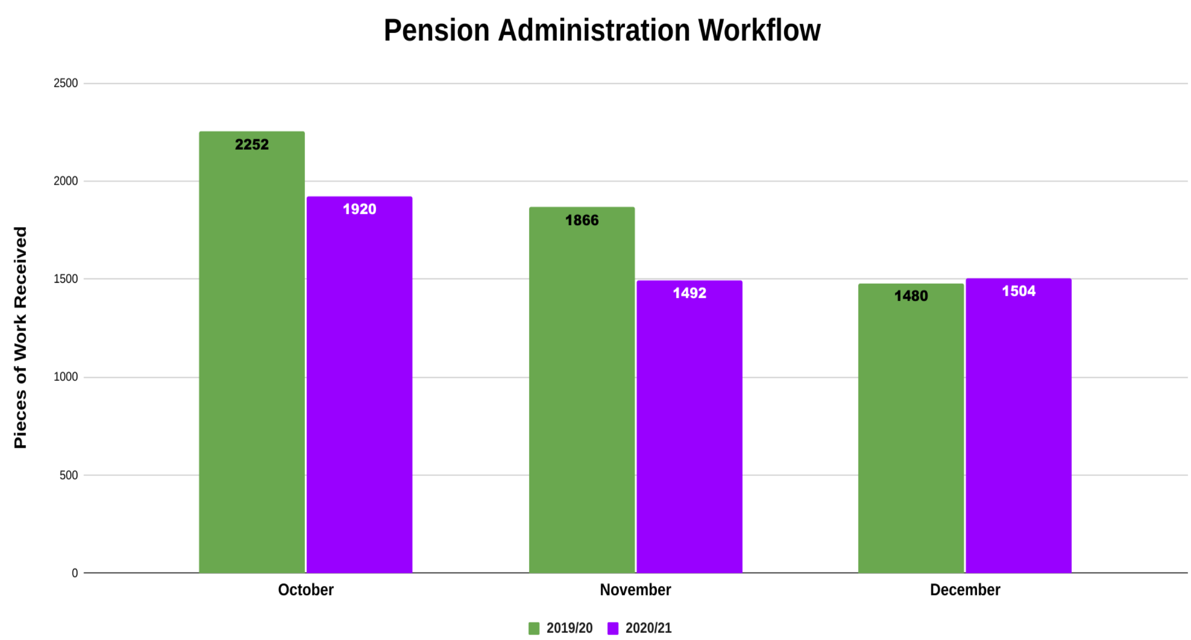
10. RISK MONITORING

10.1 As requested at the last meeting of the Pensions Committee, there is a separate report in respect of the Pension Fund Risk Register on the agenda for the March Committee meeting, along with a short related training session.

11. PENSION ADMINISTRATION

11.1 Pension Administration Management Performance

During Q3 2020/21, the administrators received a total of 4,916 new cases compared to 5,598 during Q3 in 2019/20. A comparison of the monthly workflow between Q3 2019/20 and the reporting quarter is set out below:-



As previously reported, due to the COVID-19 pandemic, guidance was issued by the Pension Regulator, and in accordance with this, the administering authority and Equiniti shifted priorities to ensure the critical services continued to be delivered during this period:-

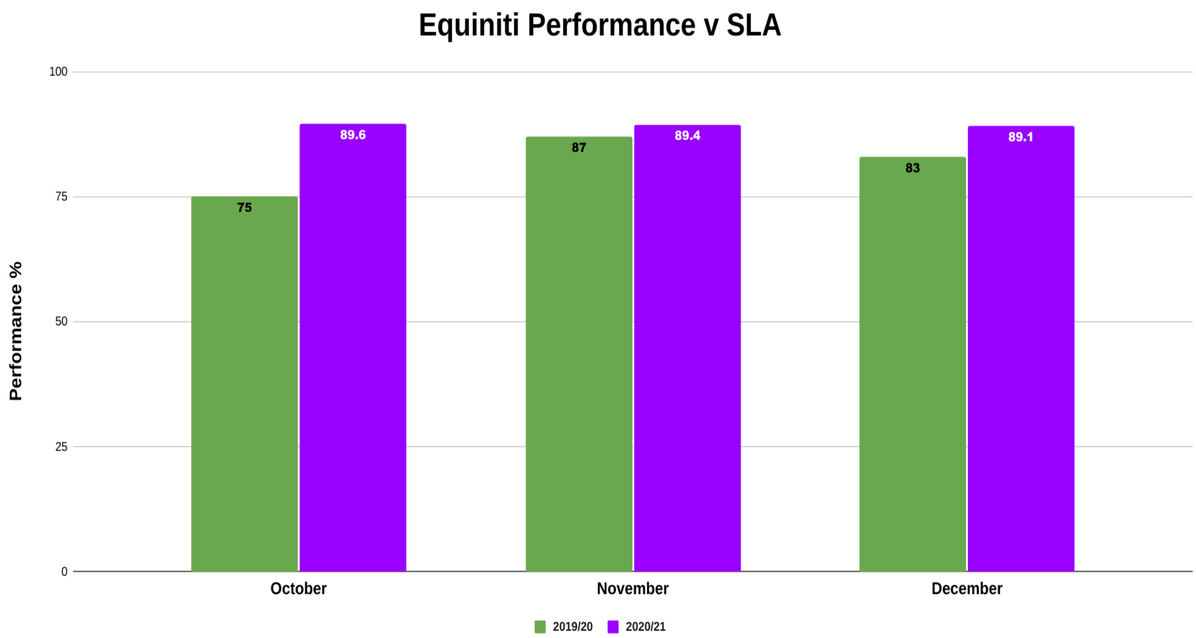
- Paying member's benefits – ensure the monthly pension pay is continued
- Retirement processing – those retiring to receive priority in the workflow and payments made
- Bereavement services – to ensure the process of informing the Fund and the payment of death grants is as smooth as possible

The administering authority applied a number of other measures and process changes that would allow the services to continue, albeit with varying degrees of change to the normal practices. Therefore we would accept:-

- Electronic or typed signatures on starter, leaver and opt out forms
- Photographs of member ID – passport, birth certificate, driving licence
- A medical certificate issued at the time of death if relatives are unable to obtain death certificates
- Expression of Wishes forms for the payment of death grants – if it cannot be witnessed the member is to reference COVID on the form

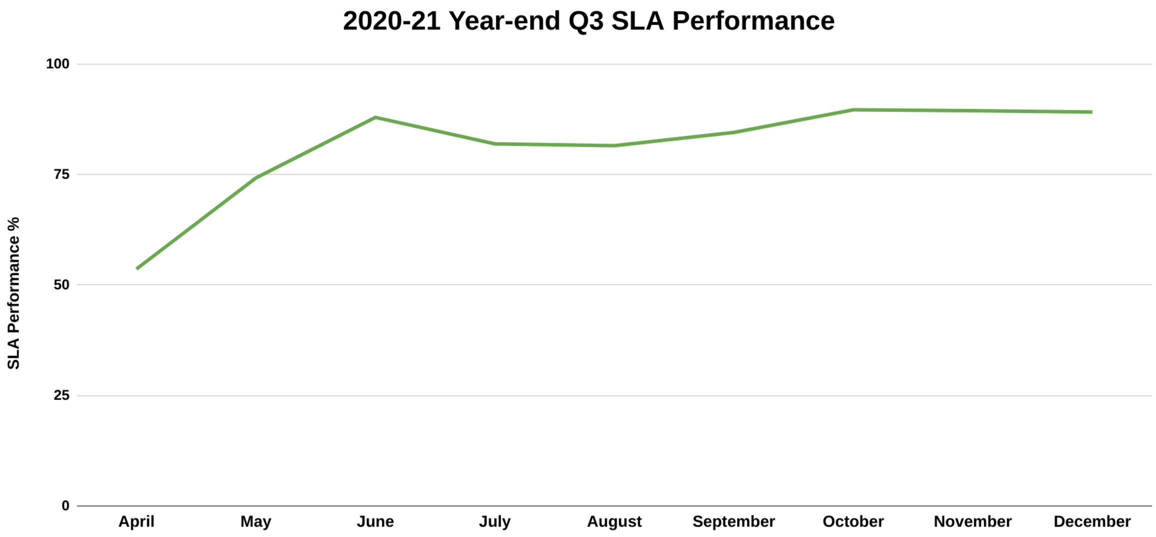
These measures have been in place throughout the reporting period but will be revisited by Equiniti and the administering authority once the pandemic eases.

Performance against all of the service level agreement (SLA) is being monitored and an averaged SLA of 89.4% was achieved for Q3 2020/21, compared to 81.7% for the same quarter last year. The administrator's monthly performance against the SLA during Q3 2020/21 and Q3 of 2019/20 is set out below:



SLAs being reported are still in relation to the SLAs in the old contract. For the new reporting year the administration report will move to the new contract SLAs, together with additional monitoring of the magnitude of work tasks being received, completed and outstanding.

It is clear that the administration performance has been affected by the “lockdown” measures, particularly during the first lockdown in 2020. The SLA performance from April 2020 to the end of December is shown in the graph below, clearly showing that this position has been improved significantly.



The performance of the external pension administrators is monitored by the administering authority’s pension team at Hackney on a monthly basis. Whilst the SLA performance has been disappointing, the administering authority are continuing to work with Equniti to continue the month on month improvements.

In the reporting period data validation work was also taking place in preparation of the main scheme employer going live with the interface between payroll and Equiniti. This impacted on the resources available in the BAU team. The authority is also conscious of the effect the annual renewal and benefit statement process has on the SLAs. The Inhouse Hackney team is currently working with Equiniti on how the 2021 annual benefit statement process can be improved to ensure this does not affect the BAU delivery again.

11.2 New Starters and Opt-Outs

	Total Active Membership at end of Quarter	Total Opt Outs for Quarter
Q3 2020/21	6,953	91
Q3 2019/20	6,880	203

The number of opt outs in Q3 2020/21 is significantly lower compared to Q3 2019/20 but this is likely to be due to the triannual auto enrolment exercise for the Council in July 2019 which sees a spike in Opt Outs.

11.3 Ill Health Pension Benefits

The release of ill health benefits fall into 2 main categories, being those for deferred and active members. The administering authority team at Hackney process all requests for the release of deferred members' benefits. Deferred members' ill health benefits are released for life, are based on the benefits accrued to the date of leaving employment, (with the addition of pension increases whilst deferred), but they are not enhanced by the previous employer.

The team also assist the Council's HR team with the process for requests to release an active members' benefits on the grounds of ill health retirement.

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 – paid for life, no review
- Tier 2 – the pension benefits are enhanced by 25% - 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 undertaken when pension has been in payment for 18months.

The applications received have been similar in volume compared to the same period in the previous year:

DEFERRED MEMBER'S ILL HEALTH RETIREMENT					
	CASES RECEIVED	SUCCESSFUL	UNSUCCESSFUL	ONGOING	WITHDRAWN
Q3 2020/21	0	0	0	0	0
Q3 2019/20	1	1	0	0	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
Q3 2020/21	2	0	2	0	0
Q3 2019/20	1	0	1	0	0

11.4 **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 two stages:-

- Stage 1 IDRP's are reviewed and determinations made either by the Pensions Manager or 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.

Stage 1 – Two applications were submitted during this quarter against the former employer, one in relation to an ill health retirement dispute and the other in relation to an historical part time working/gratuity matter. Both appeals were not upheld.

Stage 2 – No applications were submitted in this quarter.

11.5 **Other work undertaken in Q3 2020/21**

Third Party Administration Implementation update

The major outstanding point of delivery under the new contract specification is in relation to employer interfaces and member online services. These were delayed due to the onset of the COVID-19 outbreak in the UK in late March 2020 which unfortunately halted the planned rollout and training programme. However, the first phase of the employer online portal work is now being progressed. The inhouse Hackney pension team has worked closely with the project delivery manager from Equiniti and have now agreed a detailed specification proposal. It is anticipated that the employer portal can be rolled out for employers to use in Q1 or Q2 of 2021/22.

Voluntary Redundancy (VR) Exercises for the Council

As previously reported the administering authority's pension team took the lead in the 2019 council wide VR programme.

Whilst the majority of employees leaving under VR had a last day of service of 29 February 2020, due to service requirements some were given extended leave dates, which were agreed by the corporate panels. During Q3 a further 3 employees left the organisation under the VR terms and conditions.

McCloud Programme Update

Programme background

Regulatory changes are required to rectify the age discrimination identified in the transitional protections put in place across the public sector in moving from final salary to career average revalued earnings (CARE) benefits schemes in 2014 and 2015. The key features of the proposed remedy include levelling up benefits for the younger members who suffered discrimination using a form of final salary underpin. Final regulations are expected to be effective from 1 April 2022 and will be retrospective back to 1 April 2014.

In order to prepare the Hackney Pension Fund for the expected regulatory changes the administering authority has set up a Programme to implement the changes in the regulations.

Update
Work has been progressing in the Data; Communications and Finance workstreams, with the workstreams including key officers from Hackney pensions, team members from Equiniti and consultants from Aon (providing Programme management, and technical assurance) and Hymans Robertson, as set out in the Programme Charter.

The Programme has been focussing on priority areas as follows:

- Initial work has been undertaken to identify the membership currently in scope of the extended final salary underpin (c4,100 records or 9% of the membership) based on the proposals consulted upon.
- Requests have been sent to active and former participating employers to obtain data (e.g. part time hours history) required to calculate the underpin.
- The process for checking and validating the new data, prior to uploading the new data to the administration system has been agreed in principle and is under way for those employers who have provided data by the initial end February 2021 deadline. Output from the validation checks will be analysed by Equiniti and reviewed by Hackney pensions team before a decision is made to upload the new data to the administration system.
- Communications with employers and members continues. Members are being directed to the Fund website for updates, and employers have been provided with training on the impact of McCloud at the recent employer forum.
- An impact analysis has been undertaken to get an updated view of the proposed regulatory changes on employer and overall Fund liabilities ahead of the next valuation. This was last considered as part of the 2019 valuation when there was very little detail regarding the proposed remedy. The outcome of this is that it is now estimated that at whole fund level, liabilities increase by £3m, although the overall funding level remains at 92%. The allowance made in the 2019 valuation exercise was adequate to cover this. At employer level, 14 will not be affected as they had no employees meeting the rectification criteria and for the remaining 29 employers, liabilities increase by between 0.1% and 1.2%. The Fund is actively communication with employers to explain impact on their balance sheet and potential contribution rates at next valuation.

Additional workstreams will be mobilised shortly focussing on changes that may be required for future ongoing administration; implementing benefit rectification for any members impacted by the underpin who have left active membership, and to consider complex cases and issues such as tax; transfer values and divorce cases.

Work is largely progressing as planned at this stage, with the only significant issue relating to timescales for receipt of historic council data in the preferred format following the 2017 system migration. However, the necessary data is believed to be accessible from an alternative source if it cannot be obtained from the payroll records, and it is just a question of how to most efficiently collate this.

Risks continue to be monitored within the Programme governance structure, including oversight from the Programme Management Group. These risks are actively managed and the overall Programme risk is now included in the Fund risk register.

We will provide a further update on progress at the next meeting.

Exit Payment Cap update

At the last meeting, the Committee was updated on the impact of the public sector exit cap. However, since then the exit cap has now been disapplied.

On 12 February 2021, HM Treasury [HMT] published directions to disapply the exit cap regulations with immediate effect. This means the exit cap does not apply to exits that take place on or after 12 February 2021.

HMT confirmed that the Government concluded that the Cap may have had unintended consequences and on 25th February The Restriction of Public Sector Exit Payments (Revocation) Regulations 2021 were made and laid before parliament and will come into force on 19th March 2021. These regulations confirm the effect of the disapplication Directions made on the 12th February 2021, but are not retrospective.

Exits from 12 February 2021

The exit cap does not apply to exits that happen on or after 12 February 2021.

When an LGPS member exits due to redundancy or business efficiency at age 55 or over:

- the member is entitled to and must take an unreduced pension under regulation 30(7) of the LGPS Regulations 2013
- the Scheme employer must pay the strain cost of paying that pension early requested by the administering authority, and
- the Scheme employer must not make a cash alternative payment to or on behalf of the member.

Therefore any ongoing redundancies must be offered unreduced pension benefits. The administering authority have communicated the revocation of the Cap to scheme Employers but will keep monitoring the ongoing exists to ensure the full benefits are offered.

Exits between 4 November 2020 and 11 February 2021

The 2020 Regulations have not been revoked retrospectively. The regulations contain an obligation for employers to make payments to employees who left during the period between the original regulations coming into force (4th November 2020) and the date of these regulations coming into force.

Such payments being the difference between what was paid and the exit payments that the employee would have been entitled to had regulation 3 of the 2020 Regulations not been in force.

The Hackney Pension Fund are not aware of any redundancies in this time that breached the £95k cap but will continue to monitor exits.

Looking ahead

The Government confirmed in the guidance that HMT will bring forward proposals at pace to tackle unjustified exit payments. We understand that MHCLG plans to introduce further changes to exit payments but will consult again on further reforms to exit payments before any changes are made.

The Government has not confirmed when the exit cap or further reforms will be introduced, although we think it is unlikely to happen in the next few months due to the time it will take to consult and make changes to legislation.

We will provide updates in future reports once more is known about timescales. In the meantime, the Hackney Pension Fund are including warnings about possible future reforms to exit payments when any relevant early leaver estimates are being provided.

GMP Project Update

As explained in the last report, a project has been ongoing to reconcile the Fund's GMP data with that held by HMRC, following the change to contracted-out pension rules in April 2016. This has led to the identification of a number of scheme members who have had benefits either overpaid or underpaid, in some cases for a number of years. Equiniti are now finalising the calculations in relation to these overpayments and underpayments. It should be noted that the information we have is still estimated and the final numbers of members affected, and the impact on these members, will only be known as each case goes through final verification checks. There are approximately 2,000 pensioners and dependents where their GMP on the Fund's records will change. Of those, there are an estimated 771 where their pension will either increase or decrease.

It had been hoped that those pensioners who have been underpaid would have their benefits corrected (and the arrears paid) in the March pensioner payroll (with the overpayment cases being dealt with later this year) but unfortunately the final checks on member data are taking longer than anticipated and it won't be possible to meet the March payroll deadlines. April and May payrolls are affected by the annual Pensions Increase exercise and because of this it is not recommended to make other changes to member records during these payrolls. This means that no members will see their pension corrected as a result of the GMP reconciliation exercise until at least the July payroll (after allowing for recalculations due to the updated Pensions Increase and allowing for all members to receive adequate notice of the amendments to their benefits).

Around 380 members are being reviewed as a separate exercise, and any amendments needed to their benefits will be actioned on an individual basis. These are members who became entitled to their GMP before reaching their State Pension Age (SPA). This makes their calculation more complicated, so additional checks are being undertaken with this group to ensure accuracy and to ensure that checks on this group do not hold up the overall exercise. It is not known at this stage how many of this group will actually see a change to the benefits they are currently receiving.

It is disappointing that the GMP reconciliation exercise will not be finalised as quickly as we had hoped but it is more important to ensure that the calculations are correct and the delay also gives us more time to ensure the communications are appropriate, particularly for those members who are more elderly or who are facing a significant reduction to their benefits. As requested at the last meeting, the communications will be agreed with the Chair before they are finalised.

12. REPORTING BREACHES

12.1 There have been no reportable breached in the last quarter. We continue to experience lack of access to the Fund's breaches register due to the ongoing issues caused by the cyber attack in October.2020.

Ian Williams
Group Director of Finance & Corporate Resources

Appendices:
Appendix1 – Funding Update (Hymans Robertson – Actuary)
Appendix 2 – Investment Performance and Report (Hymans Robertson – Investment Consultant)
Appendix 3 – LAPFF Quarterly Engagement Report

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