

**Open Report on behalf of Andrew Crookham,
Executive Director - Resources**

Report to:	Pensions Committee
Date:	18 March 2021
Subject:	Pension Fund Update Report

Summary:

This report updates the Committee on Fund matters for the quarter ending 30 September 2020 and any other current issues.

The report covers:

1. Funding and Performance Update
2. TPR Checklist Dashboard
3. Breaches Register Update
4. Risk Register Update
5. Asset Pooling Update
6. Good Governance Review
7. Independent Advisor – Review Against Objectives
8. Investment Consultancy Services Contract
9. Conference and Training Attendance

Recommendation(s):

That the Committee:

- 1) consider and note the report;
- 2) consider the performance of the Independent Advisor and consider any changes/improvement required; and
- 3) approve the creation of a working group of officers and volunteers from the Pensions Committee to consider the Actuarial appointment and, following due process, recommend an appointment to the October meeting of the Pensions Committee.

Background

1. Funding and Performance Update

1.1 Over the period covered by this report, the value of the Fund increased in value by £192.5m (+7.8%) to £2,660.2 on 31 December 2020.

Asset Allocation

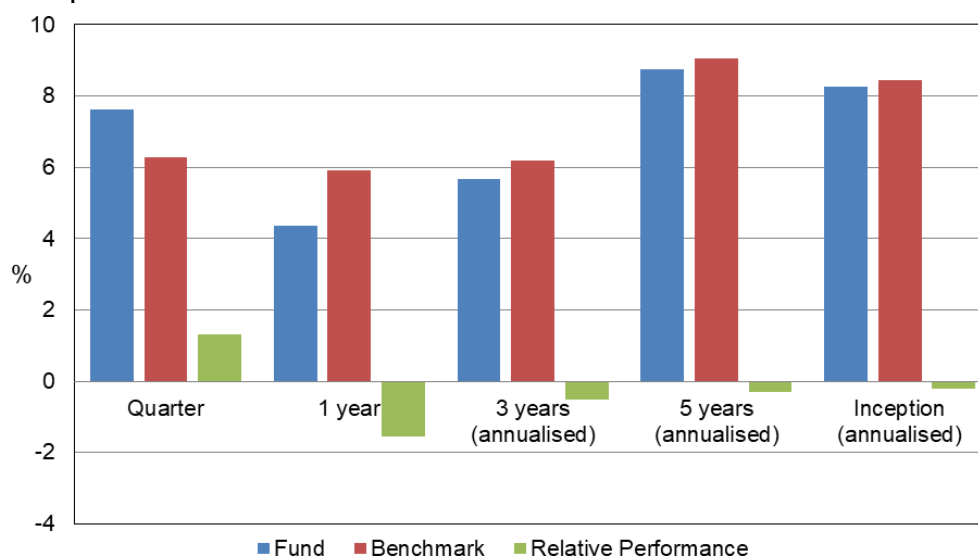
1.2 Appendix A shows the Fund's distribution as at 31 December. At an asset class level, property is below its lower tolerance. A proposal for an additional property investment to assist in rebalancing this asset class is brought at paper 14.

1.3 The Fund's overall position relative to its benchmark is set out in the table below.

Asset Class	Q4 2020 £m	Q3 2020 £m	Asset Allocation %	Strategic Asset Allocation %	Difference %
UK Equities	422.6	375.6	15.9	15.0	0.9
Global Equities	1,143.0	1,041.7	42.9	40.0	2.9
Alternatives	506.1	482.9	19.0	21.0	(2.0)
Property	201.2	196.1	7.6	10.0	(2.4)
Fixed Interest	366.4	355.4	13.8	13.5	0.3
Cash	20.9	15.9	0.8	0.5	0.3
Total	2,660.2	2,467.6	100.0	100.0	

Fund Performance

1.4 The graph and table below shows the Fund's performance against the benchmark over the quarter, one year, three years, five years and since inception. The Fund has a target to outperform the strategic benchmark by 0.75% per annum.



	Fund %	Benchmark %	Relative Performance %
Quarter	7.61	6.29	1.32
1 year	4.35	5.90	(1.55)
3 years*	5.66	6.19	(0.53)
5 years*	8.75	9.04	(0.29)
Inception**	8.25	8.45	(0.20)

*Annualised from 3yrs. **Since Inception figures are from March 1987

- 1.5 Over the quarter, the Fund produced a positive return of 7.61% (as measured by Northern Trust), outperforming the benchmark by 1.32%. The Fund was behind the benchmark over the one, three and five year periods, following a poor one year performance, and has underperformed by 0.2% on the since inception figures.
- 1.6 Appendix B shows the market returns over the three and twelve months to 31 December 2021.

Funding Level

- 1.7 The funding update is provided to illustrate the estimated development of the funding position of the Lincolnshire Pension Fund from the latest formal valuation, 31 March 2019, to the current quarter end, 31 December 2020. The accuracy of this type of funding update is expected to decline over time, as the period since the last valuation increases. This is because the funding update does not allow for changes in individual members' data since the last valuation. It is, however, a useful tool to assist the Committee to identify whether the time is right to reduce the overall risk in the asset allocation of the Fund, as it approaches a 100% funding level.
- 1.8 At the last formal valuation, conducted by Hymans Robertson, the Fund assets were £2,353m and the liabilities were £2,536m. This represented a deficit of £183m and equated to a funding level of 93%. Since the valuation the funding level has fallen by 2% to 91%. The graph below shows the changes to the funding level since 31 March 2019.



1.9 Over the period 31 March 2019 to 31 December 2020 the deficit, in real money, has increased from £183m to £256m. Investment returns of 12.6% over the period since the valuation have been higher than expected. The outlook for future investment returns over the next 20 years on the Fund's portfolio of assets has also fallen (from 4.0% to 3.2%), increasing the value placed on liabilities. Since the valuation, contributions have broadly matched the accrual of new benefits.

1.10 The table below shows the main impactors on the deficit.

Surplus/(deficit)	£m
Surplus/(deficit) as at 31/03/2019	(183)
Contributions (less benefits accruing)	4
Interest on surplus/(deficit)	(18)
Excess return on assets	139
Change in inflation & expected future investment return	(198)
Surplus/(deficit) as at 31/12/2020	(256)

1.11 As the Committee are aware, Barnett Waddingham has replaced Hymans Robertson as the Fund's Actuary with effect from 1 January 2021. The funding position calculated by Barnett Waddingham, using their methodology as at 31 December 2020, is shown below:

- The current projection of the smoothed funding level as at 31 December 2020 was 93.5%.
- This compares with the rebased (smoothed) funding level of 98.9% at the 31 March 2019 funding valuation.
- The discount rate underlying the smoothed funding level as at 31 December 2020 was 4.2% p.a. The investment return required to restore the funding level to 100% by 31 March 2040, without the employers paying deficit contributions, would be 4.5% p.a.

2 TPR Checklist Dashboard

2.1 To assist in the governance of the Lincolnshire Fund, it assesses itself against the requirements of the Pension Regulator's (TPR's) code of practice 14 for public service pension schemes, as set out in a check list attached at appendix C. This is presented to the Committee and Board at each quarterly meeting, and any non-compliant or incomplete areas are addressed. This is seen as best practice in open and transparent governance.

2.2 No areas have changed since the last quarter's report.

2.3 The Areas that are not fully completed and/or compliant are listed below.

F1 – Maintaining Accurate Member Data - Do member records record the information required as defined in the Record Keeping Regulations and is it accurate?

Amber - Scheme member records are maintained by WYPF. Therefore much of the information here and in later questions relates to the records they hold on LCC's behalf. However, as the scheme manager, LCC is required to be satisfied the regulations are being adhered to. Data accuracy is checked as part of the valuation process and the annual benefits statement process. Monthly data submissions and employer training are improving data accuracy, however there are a number of historical data issues that are in the process of being identified and rectified.

F5 - Maintaining Accurate Member Data - Are records kept of decisions made by the Pension Board, outside of meetings as required by the Record Keeping Regulations?

Grey – not relevant as we do not expect there to be decisions outside of the PB. This will be monitored.

H7 - Maintaining Contributions - Is basic scheme information provided to all new and prospective members within the required timescales?

*Amber - New starter information is issued by WYPF, **when they have been notified by employers**. This is done by issuing a notification of joining with a nomination form, transfer form and a link to the website. However, because the SLA relates to when notified, it does not necessarily mean the legal timescale has been met which is within 2 months of joining the scheme. The monthly data returns and employer training are improving this process.*

K7 – Scheme Advisory Board Guidance - Members of a Local Pension Board should undertake a personal training needs analysis and put in place a personalised training plan.

Remaining Amber - Annual Training Plan of Committee shared with PB and all PB members invited to attend.

3 Breaches Reporting - update

3.1 The Fund, and those charged with its governance, has a requirement to log and, where necessary, report breaches to the Pensions Regular. The Breaches Register attached at appendix D shows those breaches logged since recording began. Since the last quarter end, one breach has been added, detailed below:

- **Late payment of contributions** – a separate paper is presented to the Committee at paper 9, updating the Committee on all monthly employer contribution breaches over quarter.

4 Risk Register Update

- 4.1 The risk register is a live document and updated as required. Any changes are reported quarterly, and the register is taken annually to Committee to be approved.
- 4.2 There has been one amendment to the risk register since the last Committee meeting. This is under Investment risk and is the removal of risk I8 – Economic uncertainty due to the UK leaving the EU, following the successful exit agreement between the EU and Great Britain.
- 4.3 There are currently no red risks.

5 Asset Pooling Update

Sub Funds

- 5.1 The additional investment of 7.5% (£195.5m) into the Global Equity Alpha sub-fund was made in March 2021, as part of the transition out of the Invesco mandate. This involved an exchange of units with another Border to Coast Partner Fund of who were looking to reduce their Global equity exposure, and a purchase of units with the balance.
- 5.2 The investment with Border to Coast into the Multi Asset Credit (MAC) Fund is expected to be completed in the second half of 2021. Ahead of this, the Fund invested 3.5% of the Fund with the MAC Fund's core manager, Pimco, in two tranches in July 2020. This will transfer to the Border to Coast Fund once that is launched, with an additional 1.5% of the Fund being invested in the new sub-fund.
- 5.3 Border to Coast has held a number of workshops with officers and advisors on the property offering, alternative investments and responsible investment.
- 5.4 Officers and advisors across the Partner Funds have continued to work closely with Border to Coast, through attendance at virtual meetings and workshops, on the development of the sub-fund products.

Joint Committee Meetings

- 5.5 The minutes of the Joint Committee meeting held on 24 November, and the agenda items for the latest meeting of 9 March, were shared with Board members on 1 March. Below are the agenda items for the meeting and the minutes will be circulated with the next JC agenda:
 - Schedule of Future Meetings
 - Annual Election 2021
 - Joint Committee Budget
 - Governance Charter Update
 - 2020 Partner Fund Satisfaction Survey

- Border to Coast Market Review
- Real Estate Update
- Listed Alternatives Fund – Fund Design and Prospectus Submission
- Performance Report
 - UK Listed Equity
 - Overseas Developed Equity
 - Emerging Markets Equity
 - UK Listed Equity Alpha
 - Global Equity Alpha
- Update on Emerging Matters

5.6 The next JC meeting will be held on 15 June 2021 and papers will be circulated to Board members. Any questions or comments on the papers should be directed to Cllr Strenziel, Chairman of the Pensions Committee, who can raise them at the meeting.

Shareholder Matters

5.7 As the Committee are aware, there are two distinct roles that Lincolnshire County Council has with Border to Coast: the shareholder and the investor (or client). The Committee's role is that of investor, and is represented at the Joint Committee by the Chairman of the Pensions Committee. The shareholder role is undertaken by the Executive Director of Resources, and fulfils the role as set out in the Shareholder Agreement, which was approved by Full Council in February 2017.

5.8 Ahead of any shareholder approvals, officers, including S151 officers, work closely with Border to Coast to ensure full understanding of the resolution, the impact of it not being approved and discuss this with the JC ahead of any resolution being sent for approval. An informal shareholder meeting is also held on the date of each Joint Committee meeting.

5.9 There has been one shareholder resolution since the last report, to approve the strategic plan for 2021-2024 and the supporting budgets for 2021-2022.

6. Good Governance Review

6.1 As the Committee are aware, Hymans Robertson were commissioned by the Scheme Advisory Board (SAB) in 2019 to undertake a governance review of the LGPS, and the second phase report was approved in February 2020 and brought to the Committee for information. The third and final phase was unfortunately delayed due to the pandemic, but has now been completed and was approved by SAB in February this year.

6.2 The final phase report (attached at appendix E) looked at more detail on the proposals put forward in the second phase, in order to progress with implementation and focussed on the proposals which needed further analysis or consideration ahead of implementation.

6.3 The key areas that have had further clarity added are:

- The LGPS senior officer – core requirements, principles and characteristics, personal competencies and organisational structure.
- Conflicts of interest – setting expectations on the areas covered.
- Representation – how engagement is done with wider employers and scheme membership.
- Skills and training – requirements for Pension Committees and S151 officers.
- Service delivery – how administering authorities can be empowered to penalise inefficient employers in a more effective way, minimum standards of performance and administration strategy statements.

6.4 SAB have written to MHCLG with the proposals and setting out an action plan (attached at appendix F), which consists of formal requests from SAB to MHCLG and other bodies to implement the recommendations from the project together with actions for the SAB which are either dependant on or regardless of the outcome of those requests.

6.5 At this time there is no timescale known for MHCLG to respond to SAB, however there will be a consultation on any statutory guidance before it is introduced. Further information will be brought to the Committee once it is available.

7. Independent Advisor – review against objectives

7.1 In 2019, the Competition and Markets Authority (CMA) issued an order requiring Pension Fund to set objectives for their investment consultants. The Fund agreed a set of objectives with both its Investment Consultant and Independent Investment Advisor ahead of the deadline in December 2019. Under the Order, and also under the new Stewardship Code 2020, the consultant (and advisor) should be reviewed against these objectives at regular intervals.

7.2 The objectives and role agreed for the Investment Advisor are attached at appendix G. The Investment Advisor was asked to complete a self-assessment of his performance against the objectives, and his comments are shown below:

- provide a quarterly report and briefing covering current and future economic and market conditions to the Committee;

Comment: These reports have always been submitted on time and have covered economic and market conditions relating to both equities and bonds as I have seen them. The Chairman has invited me to supplement

my report by a verbal update and amplification at the quarterly committee meetings. I believe that my reports have generally (but not always) identified such trends correctly.

- challenge the views of the Committee, the officers and the professional Investment Consultant (currently Hymans Robertson) to bring a different perspective to investment discussions;

Comment: Since the change in the Hymans Advisor from Paul Potter to David Morton in mid-2020, I have not found the need to give an alternative view - being in general agreement, so far. This is in marked contrast to my experience as Independent Advisor at another County Council scheme – where I recently had a major disagreement with Hyman’s investment advice to sell equities and buy bonds. Some years ago, I had a major disagreement with Hymans over the conservative assumptions in their actuarial valuation basis for the Lincolnshire Fund, which led to a modest relaxation in them.

- assist the Committee to challenge and question the Fund's investment managers on their performance and strategy;

Comment: This was a key role for me in the years before pooling of investments and since Border to Coast became the dominant fund manager. The opportunity to comment on alternative investments (e.g. property, private equity) is somewhat limited.

- assist the Committee in understanding the appropriateness of the investment strategy / strategic asset allocation to meet the Fund’s liabilities;

Comment: Investment strategy is principally the preserve of Hymans Robertson as they produce the asset liability modelling strategy after each three yearly actuarial valuation. This is a subject that I have always regarded as one of my principal strengths. If I had a different view, I would have certainly put it forward. I continue to believe that the heavy weighting of the strategy towards equities and alternatives is the right one for a long term fund such as the Lincolnshire Scheme. Hymans, in my view, have a tendency to “over diversify” the fund’s investment classes i.e. resulting in it having too many small holdings which are unable to make a material impact on its overall total return or risk profile.

- offer opinion and challenge to other ad-hoc investment related matters:

Comment: I do so when required. The most recent example was in participating in the working party to review the scheme’s actuarial advisory firm. This led to the appointment of Barnett Waddingham, late last year.

- 7.3 The Committee are asked to review the responses from the Investment Advisor, and consider any changes/improvement required.

8 Investment Consultancy Services Tender

- 8.1 At the July 2020 meeting of this Committee, it was agreed that the Investment Consultancy Services contract could have a twelve month extension to 31 December 2021, to allow for a full governance review of the Lincolnshire Fund against the new Good Governance requirements to be undertaken ahead of appointing a consultant.
- 8.2 Unfortunately, as a result of the pandemic, the progress of the Good Governance project stalled, and statutory guidance from MHCLG has not been produced. However, the final Good Governance report from Hymans Robertson was presented to the Scheme Advisory Board at its February 2021 meeting. This has meant though that the governance review that the Fund had planned has not been undertaken, although it is hoped that this can happen in the 20/21 financial year.
- 8.3 Given that there has already been a twelve month extension to the Investment Consultancy contract, it is recommended that the contract is retendered ahead of the end of the extension date. It is a statutory requirement for the Fund to take professional investment advice, therefore an investment consultant will always be required.
- 8.4 The intention is to use the National Frameworks Investment Consultancy Services framework agreement to call off from.
- 8.5 To enable a robust call-off process within the timeframe available, officers request that a working group is created from officers and volunteers from the Committee to:
- agree the specification and information to tender (ITT) documentation for call-off from the framework;
 - to evaluate responses; and
 - to recommend an appointment to the October meeting of this Committee
- 8.6 It is expected that this work would begin in July 2021.
- 8.7 The Committee are therefore asked to approve the recommendation to create this working group. Following the May elections and County Council AGM, Officers will request volunteers from the Pensions Committee to participate in the group.

9 Conference and Training Attendance

- 9.1 It is stated in the Committee's Training Policy, approved each July, that following attendance (virtual or otherwise) at any conferences, seminars, webinars or external training events, members of the Committee and officers will share their thoughts on the event, including whether they recommended it for others to attend.

9.2 The Committee and officers are therefore requested to share information on relevant events they have participated in since the last Committee meeting.

Conclusion

- 10 The Fund has continued its recovery from the falls earlier in the year, and is 91% funded as at the end of December (under the methodology of Hymans Robertson).
- 11 The Committee are requested to review the performance against objectives of the Investment Advisor at section 7, and consider any changes/improvement required.

Consultation

a) Risks and Impact Analysis

The Pension Fund has a risk register which can be obtained by contacting the author of this report.

Appendices

These are listed below and attached at the back of the report	
Appendix A	Distribution of Investments
Appendix B	Market Returns (31 December 2020)
Appendix C	TPR Checklist Dashboard
Appendix D	Breaches Register
Appendix E	Good Governance Review – Final Report
Appendix F	Good Governance – SAB Action Plan
Appendix G	Investment Advisor Objectives

Background Papers

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

This report was written by Jo Ray, Head of Pensions, who can be contacted on 01522 553656 or jo.ray@lincolnshire.gov.uk.

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