

## **Pension Board**

<b>Date:</b>	<b>23 August 2016</b>
<b>Classification:</b>	<b>General Release</b>
<b>Title:</b>	<b>Pension Fund Costs and Fees Benchmarking</b>
<b>Report of:</b>	<b>Steven Mair</b> <i>City Treasurer</i>
<b>Wards Involved:</b>	<b>All</b>
<b>Policy Context:</b>	<b>Effective Control over Council Activities</b>
<b>Financial Summary:</b>	<b>There are no financial implications arising from this report</b>

### **1. Executive Summary**

- 1.1 At the 10<sup>th</sup> May 2016 meeting, the Pension Board requested a report to determine the structure in comparing management fees and costs with other pension funds
- 1.2 This report summarises the costs for each type of expenditure which the Pension Fund incurred during the 2015/16 financial year compared to the previous two years and presents the benchmarking data which is available for comparing costs against other pension funds.

### **2. Key Matters for the Board**

- 2.1 The Board note the contents of this paper
- 2.2 The Board agree that benchmarked cost analysis be presented annually.

### **3. Background**

- 3.1 At the May meeting of the Westminster Local Pension Board, members were provided with an analysis of the Fund's management costs over the previous five years to 2014/15.

- 3.2 The report highlighted the complexities in benchmarking costs against other Fund's due to factors such as changes to the reporting requirements over time, the relationship between fund size and costs, whether assets are actively or passively managed and the inconsistency (in particular for pooled fund costs) and lack of transparency across Funds in reporting their cost information.
- 3.3 The Board requested a report on agreeing the structure of future pension management fees and costs reports.

#### **4. Westminster Pension Fund Management Expenses 2015-16**

- 4.1 The breakdown of the Pension Fund management expenses for 2015-16 is included as Appendix 1 (exempt) and the comparative figures for the prior two years are also included.
- 4.2 Fund manager fees are based on the market value of the fund, which has increased 10% over the three year period from £964 million to £1,058 million. The increase in manager fees is largely attributable to the performance management fees paid to one fund manager to reward out-performance. This is detailed in Appendix 1 (exempt).
- 4.3 Advisory and Professional fees are mainly determined by the volume of work undertaken by these advisors at the request of the Pensions Committee. The reduction in these costs over the three year period reflects the level of work undertaken plus the lower fees which have been secured during the re-tender of the Actuary and Pensions Administration contracts. Actuarial and investment strategy reviews are not annual events.
- 4.4 Central costs are the internal staffing and associated costs incurred for managing the Pension Fund. The costs which are paid by the Council in respect of those officers within City Treasurers and Peoples Services who undertake work on behalf of the Pension Fund are recharged each year. These costs have remained relatively constant over the three years.
- 4.5 All expense invoices are checked by officers against budget based purchase orders. The Pension committee review annual analysis of scheme costs in a similar format to the papers enclosed. The monitoring of investment returns is based on net of fees calculations.

#### **5. Benchmarking Costs Provided by the DCLG**

- 5.1 The analysis below considers Westminster's costs compared to the annual analysis prepared by the DCLG for 2014-15. Data for 2015-16 is expected towards the end of the year.

**Table A: Local Government Pension Scheme administration and fund management costs in England and Wales 2014-15, per scheme member (psm)**

	Administration costs (£ psm)	Fund management costs (£ psm)	Total costs (£ psm)
English shires	£22.41	£130.05	£152.46
Metropolitan authorities	£15.91	£148.77	£164.68
Inner London	£42.50	£205.66	£248.17
Outer London	£48.94	£174.74	£223.68
Other English authorities	£48.14	£152.07	£200.21
<b>All English authorities</b>	<b>£24.98</b>	<b>£142.28</b>	<b>£167.26</b>
<b>Welsh authorities</b>	<b>£28.28</b>	<b>£180.17</b>	<b>£208.45</b>
<b>All authorities</b>	<b>£25.19</b>	<b>£144.65</b>	<b>£169.84</b>

- 5.2 The above is a measure of administration costs per member. The appropriate comparison for Westminster is inner London £42.50, as this takes into account scheme size and local costs.
- 5.3 Westminster had 16,060 scheme members at 31st March 2015.
- 5.4 Westminster's costs in 2014-15 of £7,047,000 comprise investment £5,261,000, administration and governance £626,000 and transaction fees £1,160,000.
- 5.5 Westminster's administration costs and Governance costs represent £38.98 per member, below the inner London average of £42.50.
- 5.6 Westminster's fund management costs represent £328 per member, significantly in excess of the inner London average of £206. More than half (58%) of Westminster's costs are represented by one fund manager, Majedie, mostly the performance related element. While performance fees look expensive when the investment manager exceeds their target, they do provide an alignment of interest.
- 5.7 The DCLG also provide data to allow comparison of fund manager costs as a percentage of asset value. For inner London the average cost in 14/15 was 0.34% of the year end market value. For Westminster the value was 0.48%.

## Conclusion

- 5.8 Westminster's administration costs are lower than the inner London average. Investment costs are higher with the performance fee element for Majedie being the main explanation.

## **6. Benchmarking Costs Provided by CEM Benchmarking**

- 6.1 CEM provide a global benchmarking service. The latest available survey based on 2014 data comprised of a database of 407 funds representing £5.8 trillion in assets, 194 of these were public funds.
- 6.2 The median membership was 43,618 members (versus Westminster's 16,060 members). The median assets per member was £104,941 (versus Westminster's £68,406).
- 6.3 It is important to note that costs included in the report for the LGPS are reported for the financial year ending March 2015 but for the wider universe of funds, costs are for the year ending December 2014.
- 6.4 In 2014/15, Westminster's total investment cost was 50.8 bps (£5,329k). This was above the global median of 49.2 bps (£5,161k). Total investment costs excluded transaction costs.
- 6.5 CEM calculates a benchmark cost for each fund to take account of differences in total costs due to fund size and asset mix. For Westminster, the benchmark cost was 49.9 bps (£5,234k). Comparing against this benchmark, Westminster incurred an excess cost of just 0.9 bps (£94k).
- 6.6 CEM list generic reasons why a Fund's costs might be higher compared to their benchmark are:
- Using a higher cost implementation style such as appointing external fund managers and employing active fund management. This is not taken account of in the benchmark equation. The Westminster Pension Fund was 73% externally actively managed, which was above the global average of 67%. Active managers have the capacity to outperform the benchmark index and therefore can provide additional returns in excess of the fees paid.
  - Paying more than similar sized funds for same-style, same-asset-class investment management. Peer-based reporting is available (but not yet purchased) from CEM benchmarking at an additional cost, which provides further analysis on this.
  - Paying more than similar sized funds for oversight, custodial and other costs. Westminster incurred costs of 3.3 bps which matched the LGPS median and was below the Global median of 4.0 bps.

## **Conclusion**

- 6.7 Being high or low cost is neither good nor bad. The important question is whether the Fund is receiving sufficient value for any cost. The investment performance of the Fund Managers is monitored quarterly by the Pension Fund Committee and the payment of outperformance fees over recent years would tend to support this.

## **7. Future Reporting and Monitoring of Pension Fund Costs and Fees**

- 7.1 Due to the complexity involved in the benchmarking of costs and the resources required to carry out such comparisons, it is only feasible to use existing sources of such analysis.
- 7.2 Cost benchmarking information from DCLG and CEM is available annually at no cost to the Fund and it is proposed that this be reported to the Pension Board when it becomes available.
- 7.3 CEM benchmarking can provide a peer-based benchmarking report on costs and/or performance at an additional cost. This is being investigated by officers to determine whether it is a suitable option for Westminster and the findings will be reported to the Board at the next meeting.

**If you have any queries about this Report or wish to inspect any of the Background Papers please contact:**

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## **BACKGROUND PAPERS:**

- CEM Benchmarking 2014/15 Investment Benchmarking Analysis for City of Westminster

## **APPENDICES:**

### **Appendix 1: EXEMPT**

Westminster Pension Fund Management Costs