Public Document Pack

City of Westminster

Committee Agenda

Title:	**Pension Fund Committee**
Meeting Date:	**Tuesday 22nd March, 2016**
Time:	**7.00 pm**
Venue:	**Rooms 1A, 1B and 1C, 17th Floor, City Hall, 64 Victoria Street, London SW1E 6QP**
Members:	**Councillors:** Ian Rowley (Chairman) Antonia Cox Patricia McAllister

Members of the public are welcome to attend the meeting and listen to the discussion Part 1 of the Agenda

Admission to the public gallery is by ticket, issued from the ground floor reception at City Hall from 6.00pm. If you have a disability and require any special assistance please contact the Committee Officer (details listed below) in advance of the meeting.

An Induction loop operates to enhance sound for anyone wearing a hearing aid or using a transmitter. If you require any further information, please contact the Committee Officer, Toby Howes, Senior Committee and Governance Officer.

Tel: 020 7641 8470; Email: thowes@westminster.gov.uk
Corporate Website: www.westminster.gov.uk

Note for Members: Members are reminded that Officer contacts are shown at the end of each report and Members are welcome to raise questions in advance of the meeting. With regard to item 2, guidance on declarations of interests is included in the Code of Governance; if Members and Officers have any particular questions they should contact the Head of Legal & Democratic Services in advance of the meeting please.

AGENDA

PART 1 (IN PUBLIC)

1. MEMBERSHIP

To report any changes to the Membership of the Committee.

2. DECLARATIONS OF INTEREST

To receive declarations of interest by Members and Offices of any personal or prejudicial interest.

3. MINUTES **(Pages 1 - 10)**

To approve the Minutes of the meeting of the Pension Fund Committee held on 16 November 2016.

4. MINUTES OF PENSION BOARD

To note the minutes of the Pension Board meeting held on 18 January 2016.

To follow.

5. ASSET POOLING AND THE LONDON COLLECTIVE INVESTMENT VEHICLE - UPDATE **(Pages 11 - 84)**

Report of the City Treasurer.

6. UNDERLYING RISKS IN ACCEPTING ADMITTED BODIES TO THE PENSION SCHEME **(Pages 85 - 88)**

Report of the City Treasurer.

7. FUND FINANCIAL MANAGEMENT **(Pages 89 - 114)**

Report of the City Treasurer.

8.	**EXTERNAL AUDIT PLAN FOR CITY OF WESTMINSTER PENSION FUND 2015-16** Report of the City Treasurer.	**(Pages 115 - 134)**
9.	**PERFORMANCE OF THE COUNCIL'S PENSION FUND** Report of the City Treasurer.	**(Pages 135 - 174)**
10.	**PENSION FUND BENCHMARKING COSTS** Report of the City Treasurer.	**(Pages 175 - 186)**
11.	**ANALYSIS OF THE 2014/15 PENSION ADMINISTRATION COSTS** Report of the Director of Human Resources.	**(Pages 187 - 190)**
12.	**ANY OTHER BUSINESS THE CHAIRMAN CONSIDERS URGENT**	
	PART TWO (IN PRIVATE)	
13.	**MINUTES** To approve the confidential Minutes of the Pension Fund Committee held on 16 November 2016.	
14.	**MINUTES OF PENSION BOARD** To note the confidential Minutes of the Pension Board meeting held on 18 January 2016. To follow.	

Charlie Parker
Chief Executive
16 March 2016

This page is intentionally left blank

CITY OF WESTMINSTER

MINUTES

Pension Fund Committee (Formerly Superannuation Committee)

MINUTES OF PROCEEDINGS

Minutes of a meeting of the **Pension Fund Committee (Formerly Superannuation Committee)** held on **Monday 16th November, 2015**, Rooms 3 and 4, 17th Floor, City Hall, 64 Victoria Street, London, SW1E 6QP.

Members Present: Councillors Suhail Rahuja (Chairman), Antonia Cox, Patricia McAllister and Ian Rowley.

Officers Present: Officers: Carolyn Beech (Director of Human Resources), Steven Mair (City Treasurer), Nikki Parsons (Pension Fund Officer), Neil Sellstrom (Tri-Borough Pensions Team) and Toby Howes (Senior Committee and Governance Officer).

Also Present: Hugh Grover (Chief Executive, London Collective Investment Vehicle, London Councils), Julian Pendock (Investment Oversight Director, London CIV, London Councils), Alistair Sutherland (Deloitte), Susan Manning (Pension Board Representative), Dr Norman Perry (Pension Board Representative) and Christopher Smith (Pension Board Representative).

1 MEMBERSHIP

1.1 There were no changes to the Membership.

2 DECLARATIONS OF INTEREST

2.1 The Chairman declared that he was employed by fund managers who have amongst their clients Hermes. However, he was not involved in any element of the work which relates to the Westminster Pension Fund and accordingly he did not regard this as a prejudicial interest.

3 MINUTES

3.1 **RESOLVED:**

That the Minutes of the meeting held on 8 September 2015 be signed by the Chairman as a correct record of proceedings.

4 MINUTES OF PENSION BOARD

4.1 Members acknowledged that the Committee would receive the minutes of the last Pension Board meeting for noting on future agendas. The Committee noted the minutes of the last Pension Board meeting held on 19 October 2015.

5 UPDATE ON LONDON COLLECTIVE INVESTMENT VEHICLE

5.1 Hugh Grover (Chief Executive, London Collective Investment Vehicle, London Councils) gave the first half of a presentation on progress on the London Collective Investment Vehicle (CIV). He advised that the London CIV included 30 London boroughs and the City of London Corporation. The CIV had been formally authorised in October 2015, and it had received its first wave of funds amounting to £6 million that had been authorised by the Financial Conduct Authority (FCA) on 13 November. Hugh Grover advised that the first sub-fund had been set up operating on active global equities and eight other sub-funds would be set up early in 2016, including three passive equity funds. The CIV had discussed the possibility of appointment with 20 fund managers and four fund managers currently were appointed to work with the CIV, with most of the remaining 16 fund managers expressing their wish to work with the CIV. Hugh Grover added that it was hoped that the two remaining London boroughs would join the CIV.

5.2 Julian Pendock (Investment Oversight Director, London CIV, London Councils) then addressed the Committee. He began by explaining the governance structures in place, including segregated mandates and pooled mandates. Members also heard about factors to consider in respect of fixed income. Julian Pendock then turned to infrastructure and emphasised the significant value adds that could be gained through larger economies of scale. The CIV also needed to take into account issues such as the changing nature of the infrastructure market.

5.3 During Members' discussion, details were sought about the steps that would be taken to minimise transactional costs. It was commented that aggregating fund managers was the right strategy for the CIV to take which would mean reducing costs, whilst local authorities participating in the CIV would not need to change fund managers. A Member commented that it would be advantageous if the CIV invested in UK commercial property on a larger scale and he enquired whether there were any plans to do so. In noting the aggregating of fund managers, he commented that they were still accountable to the decisions they made and he asked whose role it would be to monitor fund managers, adding that the Council should also undertake its own monitoring.

5.4 In reply, Hugh Grover advised that the CIV had been working hard with fund managers to reduce transactional costs, however there was probably not much more scope to reduce these costs further. One fund was also affected by stamp duties in Dublin and discussions were taking place as to how to address this. Hugh Grover advised that there were future plans to invest in commercial property, however the immediate priority was to firmly establish the CIV. He commented that there were diverse property and infrastructure portfolios across the London boroughs. Investment in equities had been chosen for the launch of the CIV as it was felt that a simpler area of investment was beneficial at this stage. Julian Pendock confirmed that it was his role to monitor fund managers' performance on behalf of the CIV. The Chairman added that the Council would continue to monitor fund managers' performance and this would be reported the Committee as well as the CIV's monitoring. He commented that fund managers were incentivised to work with the CIV because of the increasing role it would play in making investments on behalf of councils.

5.5 Members enquired whether the CIV would be looking to invest in large infrastructure projects and if so at what stage would it start to benefit from such investments. A point was raised as to whether higher charges would need to be imposed as the CIV grew and became more complex. A Member commented that there was an element of risk in investing in areas that were not fully understood and expressed concern about investing in new, large infrastructure projects, particularly in respect of the danger of underestimating costs. He also enquired whether the CIV would be considering investments in private markets.

5.6 In reply, Hugh Grover advised that it was the decision of the participating London boroughs as to whether to invest in large infrastructure projects. He commented that if a group of London boroughs wanted to invest in particular infrastructure projects, then the CIV could do this on their behalf. In respect of costs, he explained that there were both service charges and fees applied across the Fund as a whole. A comprehensive analysis would need to be undertaken to predict costs and the CIV would be liable to Corporation Tax, however every effort would be made to minimise the costs of the CIV fund. Hugh Grover stated that it was hard to predict how the CIV would grow and this would be at the discretion of the London boroughs.

5.7 Julian Pendock advised that in terms of fixed income, there was considerable fragmentation amongst the London boroughs and so these sub-funds would remain smaller compared to others. The CIV also needed to focus on areas such as interest rates and it would consult extensively with the London boroughs in order to minimise risks. Julian Pendock emphasised the benefits of London boroughs co-investing and sharing costs. He also stated that the CIV would be looking at possible investments in private markets in the future.

5.8 The Chairman sought further details on the cost savings that the CIV would make, including examples of these. He commented that fund managers fees were large in comparison to other fees and asked whether there would be a future report outlining the cost savings the CIV would make. The Chairman asked how fund managers were reacting to the steps being taken by CIVs and whether non-London councils could join the CIV. Another Member enquired what would happen in situations where the CIV had made a collective decision and some London boroughs had subsequently dissented.

5.9 In reply, Hugh Grover commented that there should not be an excessive focus on fees savings as the CIV would also bring benefits through larger economy of scale. He suggested savings of around 50% on sub-funds and around 65% on index funds as estimated by Deloitte could be achieved, whilst other savings would also be made through joint procurements. Hugh Grover commented that although other CIVs had quoted some significant savings, in his view these were hard to justify and a benchmarking exercise amongst CIVs needed to be undertaken. The Committee noted that of the 20 fund managers the CIV had been in discussion with, many of the 16 who had not been appointed were now re-engaging with the CIV and some were offering fee savings of around 50%. Hugh Grover advised that where a London borough subsequently dissents from a decision by the CIV, this would be considered by a Joint Committee and every effort would be made to find common ground.

5.10 Members welcomed any attempts to encourage non-London councils to join the CIV which would increase economies of scale and drive costs down and expressed their approval of the work undertaken by the CIV to date.

6 PENSIONS ADMINISTRATION UPDATE

6.1 Carolyn Beech (Director of Human Resources) presented the first report updating Members on progress of the Communications and Engagement Strategy 2015-2016 that had been agreed by the Committee at the last meeting on 8 September. She advised that the Pensions Annual General Meeting on 21 September had been successful, with attendance from current, prospective and retired members. The Admitted Body Forum had met on 4 November and the agenda included teachers' pensions, Local Government Pension Scheme legal update and a review of processes between other providers and BT. Carolyn Beech advised that a Pension Surgeries session held on 6 November had been so popular that additional dates were to be planned.

6.2 Members enquired if any issues had arisen from the Admitted Body Forum meeting. A Member stated that a KPMG paper had suggested that pension schemes should have more separation between local authorities and admitted bodies and she enquired whether this was possible. She also sought clarification in respect of statement of pension rights for a survivor's rights when a scheme member died.

6.3 In reply, Carolyn Beech advised that the Admitted Body Forum had expressed concern about payroll providers of schools not using BT who had submitted their payroll files late. The external payroll providers had expressed some confusion since the Council's move to BT and all were working closely to resolve the issue. Carolyn Beech advised that a statement of pension rights for survivors existed on the Annual Benefits Statement. She advised that there was already a degree of separation between the Council and admitted bodies in the pension scheme, however scheduled bodies were more closely tied with the Council as they were schools. Neil Sellstrom (Tri-Borough Pensions Team) advised that the KPMG report had emphasised the need to ensure that the Pension Fund money was appropriately separated from the Council's money.

6.4 Carolyn Beech then presented the second report that sought the withdrawal of the abatement policy. In response to Members request for further clarification on the matter, Carolyn Beech advised that the abatement policy was applied when an employee who had left the Council was now earning more through their pension and their salary with another local authority than the salary they were earning at the Council. The report recommended the withdrawal of the abatement policy as its application was inconsistent because it did not apply to those ex-employees now working in the private sector, nor those working for local authorities in a consultancy capacity.

6.5 **RESOLVED:**

1. That the progress made against the Westminster City Council Local Government Pension Scheme Communications and Engagement Strategy 2015/2016 be noted; and

2. That it be agreed that the Westminster City Council abatement policy be withdrawn.

7 ADMISSION AGREEMENT FOR JPL CATERING

7.1 Carolyn Beech presented the report that outlined the admission agreement on the Pension Fund scheme for JPL Catering. She advised that the Committee did not have powers to refuse the admission, however the risks to the Council was minimal as the Ark Academy Trust were liable for costs should JPL Catering fold.

7.2 Members commented on the detail of the admission agreement and sought further details on its costs and how it was produced. In reply, Carolyn Beech advised that a template was used to draw up admission agreements and the costs were not significant.

7.3 Members requested a future report on the underlying risks in accepting admitted bodies to the pension scheme.

7.4 **RESOLVED:**

That the closed Admission Agreement for JPL Catering Limited be ratified.

8 KEY PERFORMANCE INDICATORS

8.1 Steven Mair (City Treasurer) presented the report and advised that the Secretariat to the Local Government Pension Scheme (LGPS) Scheme Advisory Board (SAB) had agreed the five key themes that individual LGPS fund performances should be assessed for the 2015 national benchmarking exercise. The SAB had also identified four core key performance indicators (KPIs) to identify under-performing funds and 14 supplementary ‘health’ KPIs that can be used to identify where potential management problems may lie and improvements that could be made. Steve Mair added that the Council was awaiting for more data before making a further response to the SAB.

8.2 Members commented that some LGPS funds would be heavily underfunded compared to others. It was suggested that the Council could offer examples of best practice in respect of training, although there was still room for improvement in this area. Members also felt that the benchmarking exercise would pressurise councils into focusing on obtaining discount rates.

8.3 In reply to Members' comments, Steve Mair advised that the benchmarking exercise would afford the opportunity for the Council to be informed of its position relative to other local authorities on a standard basis. Neil Sellstrom added that standard assumptions were compiled by actuaries in respect of level of funding and a report was to be produced on this.

8.4 **RESOLVED:**

1. That the Council's response to the key performance indicator exercise be noted; and

2. That it be noted that the national results of the key performance indicator exercise will be available early in 2016.

9 BUSINESS PLAN

9.1 Steven Mair introduced the report on the 2015/2016 Business Plan and welcomed comments from Members. The Chairman welcomed the Business Plan which would bring the benefit of standardising a number of factors for the tri-boroughs. A Member suggested that some of the deadlines in the Business Plan were demanding and she asked whether there was any possibility of slippage. In noting that the Standard Life mandate for Hammersmith and Fulham Council was the same as the Council's, Members requested that consideration be given to including this in the London CIV.

9.2 In reply to Members' comments, Steven Mair advised that most targets on the Business Plan had been met to date, and although every effort was being made to meet the remaining targets, it was possible that there could be some slippage in the medium term. Steven Mair agreed to make enquiries about the possibility of the Standard Life being included in the London CIV.

9.3 **RESOLVED:**

That the 2015/2016 Business Plan and the 2016 Forward Work Plan be noted.

10 FUND FINANCIAL MANAGEMENT

10.1 Steven Mair presented the report and drew the Committee's attention to the recommendations. He advised that it had been expected that the consultation would have already taken place, however this would now be undertaken from the last week of November. Members noted that under the Markets in Financial Instruments Directive II rules due to come into force in January 2017, councils were to be defaulted to client retail status. The Local Government Association was also in discussions with the Financial Conduct

Authority to consider if any changes can be made to smooth the processes involved for local authorities in relation to their pension functions.

10.2 Members commented that it would be desirable that the ending of the Investment Adviser Contract tied in with the ending of the one at Hammersmith and Fulham Council. A Member sought further explanation about a high risk identified in relation to operational administration regarding failure of payments to scheme members and supplier payments and was it related to the move to BT. Steve Mair responded that the move to BT was partly attributable to the problems experienced and that the Council was working with Surrey County Council to resolve the problem. In the meantime, a 'workaround' solution was in place to ensure the payments were made.

10.3 **RESOLVED:**

1. That the updated risk register for the Pension Fund be approved.

2. That the Fund's position against the Investment Regulations be noted.

3. That the Class Actions update be noted.

4. That the information regarding the pooling of investments in the LGPS be noted.

5. That the information regarding the Markets in Financial Instruments Directive II be noted; and

6. That the extension of the current Investment Adviser contract with Deloitte to 31 October 2016 be approved.

11 CASH FLOW MONITORING AND STRATEGY

11.1 Steven Mair introduced the report and advised that more funds needed to be generated to meet the Fund's requirements. Members noted that in order to address immediate cash flow requirements, a £20 million disinvestment from Legal and General was proposed. A more structured approach to disinvestment was also proposed with a monthly programme of cash transfers from the fund managers to the Fund's back account.

11.2 Members recognised that the pension scheme was maturing and that the pay outs to scheme members should be undertaken in a systematic manner. It was queried why the total of £24 million per annum proposed in the monthly programme of cash transfers could not be paid in as one lump payment.

11.3 In reply, Neil Sellstrom advised that £2 million monthly payments were proposed as this replicated the monthly cash deficit and so it made investment sense, as well as ensuring lower transactional costs. Members noted that 50% of the payments would be derived from income and the other 50% from disinvestments from Legal and General.

11.4 **RESOLVED:**

1. That the cashflow position of the Fund be noted.

2. That the strategy for managing the cash flow position using investment income and structured disinvestment be approved; and

3. That the disinvestment of £20 million from Legal & General in December 2015 be approved.

12 QUARTERLY PERFORMANCE REPORT

12.1 Alistair Sutherland (Deloitte) presented the report updating Members on the Fund's quarterly performance. He advised that overall the Fund had underperformed its composite benchmark by 58bps in the third quarter of 2015, largely as a result of the weak performance from one of the active equity managers, Majedie, and because of the overall poor performance of equities in the quarter. Alistair Sutherland then advised Members of the performance of each of the Fund's managers.

12.2 Alistair Sutherland advised that Deloitte was working with Legal and General with regard to looking at options on how it could be moved to the London CIV platform as a single mandate. Similarly, Majedie had expressed its interest in being involved with the CIV.

12.3 Members enquired whether Longview had indicated any interest in being involved with the CIV. Alistair Sutherland advised that Longview did not seem as enthusiastic as other fund managers in being part of the CIV, although discussions with them continued.

12.4 **RESOLVED:**

That the covering report, the performance report from Deloitte and the current actuarial assumptions and valuation be noted.

13 MINUTES

13.1 **RESOLVED:**

That the confidential Minutes of the meeting held on 8 September 2015 be signed by the Chairman as a correct record of proceedings.

14 INVESTMENT STRATEGY - BONDS

14.1 The Committee considered a confidential report on investment strategy.

The Meeting ended at 8.50 pm

CHAIRMAN: ________________________ **DATE** _____________________

This page is intentionally left blank

City of Westminster

Committee Report

Decision Maker:	**PENSION FUND COMMITTEE**
Date:	**22 March 2016**
Classification:	**General Release**
Title:	**Asset Pooling and the London Collective Investment Vehicle - Update**
Wards Affected:	**All**
Policy Context:	**Effective control over Council Activities**
Financial Summary:	**There are no immediate financial implications arising from this report.**
Report of:	**Steven Mair** ***City Treasurer*** **smair@westminster.gov.uk** **020 7641 2904**

1. Executive Summary

1.1 The Government consultation on the pooling of Local Government Pension Scheme (LGPS) assets states an intention for there to be six pools of assets of around £25bn nationally with a proposal to change the investment regulations to enforce the pooling. Westminster as shareholders of the London Collective Investment Vehicle (CIV), are signatories to the initial response to the Government from the London CIV.

1.2 The London CIV has achieved regulatory status and has already taken on some assets from London Pension Funds. It is proposed to transfer the assets managed by Bailie Gifford in late May / early June 2016. The transfer of the LGIM assets is currently expected to take place in June 2016.

2. Recommendation

2.1 That the Committee delegate to the City Treasurer, in consultation with the Chair of the Pension Fund Committee, the decision to agree to the transition of Pension Fund assets to the London CIV where the Fund has a pre-existing relationship with the investment manager and where the transfer of such assets is financially advantageous to the Pension Fund.

3. Reasons for decision

3.1 The agreement of this delegation will allow officers, in consultation with the Chair, to proceed with the transfer of assets to the London CIV between meetings and secure fee savings at the earliest opportunity.

4. Introduction and background

4.1 On 7th April 2014 Cabinet agreed that Westminster City Council be a shareholder in the Authorised Contractual Scheme (ACS) Operator set up to run the London LGPS Collective Investment Vehicle (London CIV). It was also agreed that the Chair of the Pension Fund Committee be appointed to the Pensions Joint Committee of elected members responsible for overseeing the London CIV.

4.2 An update on progress with the London CIV was reported to the Pension Fund Committee on 8th September 2015. At that meeting it was agreed that the Fund would invest £150,000 in the CIV to meet regulatory capital requirements and this investment was made in October 2015. It was also agreed that a further £25,000 contribution be made to the set up costs, taking the total contribution to £75,000. This was paid in October 2015.

4.3 On 25th November 2015 the Government published two consultation documents in which it confirmed its intention to require LGPS funds in England and Wales to form pools of assets of approximately £25bn with the purpose of saving investment management costs, improving performance and facilitating a greater investment in infrastructure. A response was required by 19th February 2016 on initial plans for pooling either individually or collectively, with a more detailed plan to follow by 15th July 2016.

4.4 Alongside the consultation on pooling, the Government published draft revised investment regulations for consultation. The aim of the proposed regulations is to ensure the regulatory framework allows pooling to take place. The proposals give wide intervention powers to the Government to enforce the pooling of assets and also seek to update the previous regulations much of which date from 1999.

5. Proposal and issues

Government consultation

5.1 Following the Chancellor's Autumn Statement on 25th November 2015, the Government published its proposals and timetable for requiring LGPS schemes to pool their assets. The consultation documents were emailed to the Pension Fund Committee members on 26th November 2015 and are attached at Appendices 1 and 2 for reference.

5.2 The consultation proposes that LGPS investments should be managed via six pools, each with a minimum of £25bn, which could be used to invest in infrastructure and local growth. Responses to this consultation were expected to set out a proposal based around four key criteria:

- Benefits of scale i.e. at least £25bn
- Strong governance and decision making
- Reduced costs but based upon more transparent reporting of costs
- Capacity to invest in infrastructure

5.3 Initial proposals were to be submitted to the Government by 19th February 2016 and it was clarified that a collective response from each pool would be appropriate. As shareholders of the London CIV, Westminster City Council is one of the signatories of the response from the London CIV attached at Appendix 3. Each Fund will be expected to respond by 15th July 2016 with a commitment to a particular asset pool, and a profile of current costs and anticipated savings. This will include expected transition costs and any assets likely to held outside the pool and the rationale for doing so e.g. private equity closed funds.

5.4 The Government are also consulting on revisions to the LGPS (Management and Investment of Funds) Regulations 2009 which aim to complement the above consultation. This is seeking to implement a 'prudential' approach to replace the currently prescribed investment limits set out in Schedule 1 of the 2009 Regulations,. This will place the responsibility for setting a suitable diversified investment strategy on individual funds. However, in relaxing the Regulations it is proposed to introduce safeguards in the form of reserve powers for the Secretary of State to intervene at individual fund level to enforce pooling and if investment strategies do not adhere to regulation and guidance.

LONDON CIV UPDATE

5.5 The London CIV has now achieved regulated status and has commenced the process of taking on the management of assets from London pension funds. Assets in the Allianz diversified growth fund involving three London funds were transferred in December 2015 and a further seven funds are transferring assets invested in Baillie Gifford's global equity and diversified growth funds in late May/early June 2016.

5.7 The current expected date for Legal & General Investment Management (LGIM) transfer is June 2016. The Pension Fund Committee is asked to agree the proposed delegation set out in section 2 to allow officers to progress the transfer of the Baillie Gifford and LGIM assets as soon as it is possible.

6. Options

6.1 As the City of Westminster Pension Fund is already a shareholder in the London CIV and has contributed to the set up costs and invested regulatory capital, it is appropriate for the Fund to pool assets in the London CIV. Although there are seven other pools being suggested nationally at this stage, no other pool is as advanced in terms of being able to take on assets and achieve fee savings.

6.2 As a founding shareholder of the London CIV, Westminster has the opportunity to influence the future direction through the Joint Committee which the Chair of the Pension Fund Committee sits on. It is not clear that this influence would be possible outside the London CIV. Although developments will be monitored as the other pools develop, it is believed the London CIV is the best option for Westminster.

If you have any questions about this report, or wish to inspect one of the background papers, please contact the report author:

Nikki Parsons nparsons@westminster.gov.uk or 020 7641 6925

BACKGROUND PAPERS: None

APPENDICES:

Appendix 1 – Department of Communities and Local Government – LGPS: Revoking and replacing the LGPS (Management and Investment of Funds) Regulations 2009 consultation

Appendix 2 – Department of Communities and Local Government – LGPS: Investment Reform Criteria and Guidance

Appendix 3 – London CIV and participating boroughs response to the Government consultation

Department for
Communities and
Local Government

Local Government Pension Scheme: Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009

Consultation

November 2015
Department for Communities and Local Government

This document/publication is also available on our website at www.gov.uk/dclg

If you have any enquiries regarding this document/publication, complete the form at http://forms.communities.gov.uk/ or write to us at:

Department for Communities and Local Government
Fry Building
2 Marsham Street
London
SW1P 4DF
Telephone: 030 3444 0000

For all our latest news and updates follow us on Twitter: https://twitter.com/CommunitiesUK

November 2015

ISBN: 978-1-4098-4731-1

Contents

About this consultation

This consultation document and consultation process have been planned to adhere to the Consultation Principles issued by the Cabinet Office.

Representative groups are asked to give a summary of the people and organisations they represent, and where relevant who else they have consulted in reaching their conclusions when they respond.

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

The Department for Communities and Local Government will process your personal data in accordance with DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

Individual responses will not be acknowledged unless specifically requested.

Your opinions are valuable to us. Thank you for taking the time to read this document and respond.

Are you satisfied that this consultation has followed the Consultation Principles? If not or you have any other observations about how we can improve the process please contact DCLG Consultation Co-ordinator.

Department for Communities and Local Government

2 Marsham Street

London

SW1P 4DF

or by e-mail to: consultationcoordinator@communities.gsi.gov.uk

The consultation process and how to respond

Scope of the consultation

Topic of this consultation:	This consultation proposes to revoke and replace the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 with the draft regulations described in this paper. There are two main areas of reform: 1. A package of reforms that propose to remove some of the existing prescribed means of securing a diversified investment strategy and instead place the onus on authorities to determine the balance of their investments and take account of risk. 2. The introduction of safeguards to ensure that the more flexible legislation proposed is used appropriately and that the guidance on pooling assets is adhered to. This includes a suggested power to allow the Secretary of State to intervene in the investment function of an administering authority when necessary.
Scope of this consultation:	Views are sought on: 1. Whether the proposed revisions to the investment regulations will give authorities the flexibility to determine a suitable investment strategy that appropriately takes account of risk. 2. Whether the proposals to introduce the power of intervention as a safeguard will enable the Secretary of State to intervene, when appropriate, to ensure that authorities take advantage of the benefits of scale offered by pooling and deliver investment strategies that adhere to regulation and guidance.
Geographical scope:	This consultation applies to England and Wales.
Impact Assessment:	The proposed interventions affect the investment of assets by local government pension scheme administering authorities. These authorities are all public sector organisations, so no impact assessment is required.

Basic Information

To:	The consultation is aimed at all parties with an interest in the Local Government Pension Scheme (the Scheme) and in particular those listed on the Government's website: https://www.gov.uk/government/publications/local-government-pension-scheme-regulations-information-on-who-should-be-consulted
Body/bodies responsible for the consultation:	Secretary of State, Department for Communities and Local Government. The consultation will be administered by the Workforce, Pay and Pensions Division.
Duration:	25 November 2015 to 19 February 2016
Enquiries:	Enquires should be sent to Victoria Edwards. Please email LGPSReform@communities.gsi.gov.uk or call 0303 444 4057.
How to respond:	Responses to this consultation should be submitted to LGPSReform@communities.gsi.gov.uk by **19 February 2016**. Electronic responses are preferred. However, you can also write to: LGPS Reform Department for Communities and Local Government 2/SE Quarter, Fry Building 2 Marsham Street London SW1P 4DF
Additional ways to become involved:	If you would like to discuss the proposals, please email LGPSReform@communities.gsi.gov.uk
After the consultation:	All consultation responses will be reviewed and analysed. A Government response will then be published within three months, and subject to the outcome of this consultation, the resulting regulations laid in Parliament.
Compatibility with the Consultation Principles:	This consultation has been drafted in accordance with the Consultation Principles.

Background

Getting to this stage:	The proposals in this consultation are the culmination of work looking into Local Government Pension Scheme investments that began in early 2013. It has been developed in response to the May 2014 consultation, *Opportunities for collaboration, cost savings and efficiencies,* which considered whether savings might be delivered through collective investment and greater use of passive fund management. A copy of the consultation and the Government's response is available on the Government's website: https://www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies. The consultation responses called for a voluntary approach to reform, opposing the introduction of a single, national model of pooling. The Government has therefore invited authorities to develop their own proposals for pooling, subject to common criteria and guidance. The criteria for reform have been developed using the consultation responses and following a series of workshops and conversations with authorities and the fund management industry since the July Budget 2015. Some respondents to the May 2014 consultation also suggested that amendments were required to the investment regulations in order to facilitate greater investment in pooled vehicles. In addition, prior to that consultation, authorities and the fund management industry had called for wider reform. A small working group, whose participants are listed in Annex A, was established to look at whether the approach to risk management and diversification in the existing regulations was still appropriate. They recommended moving towards the "prudential person" approach that governs trust based pension schemes. The group also sought clarity as to whether certain types of investment were possible, such as the use of derivatives in risk management. The work of that group has informed the development of this consultation. In relaxing the regulatory framework for scheme investments, it is important to introduce safeguards to ensure that the less prescriptive approach is used appropriately. The July Budget 2015 announcement also indicated that measures should be introduced to ensure that those authorities who do not bring forward ambitious proposals for pooling, in keeping with the criteria, should be required to pool. This consultation therefore sets out how the Secretary of State might intervene to ensure that authorities take advantage of the benefits of scale offered by pooling and deliver investment strategies that adhere to regulation and guidance.

Previous engagement:	The proposed changes in this consultation are the result of a programme of engagement that began in summer 2013: • Round table event, 16 May 2013. Representatives of administering authorities, employers, trade unions, the actuarial profession and academia discussed the potential for increased cooperation within the Scheme. • A call for evidence, run with the Local Government Association, June to September 2013. This gave anyone with an interest in the Scheme the opportunity to inform the Government's thinking on potential structural reform. The results were shared with the Shadow Scheme Advisory Board, which provided the Minister for Local Government with their analysis of the responses. • Consultation, *Opportunities for collaboration, cost savings and efficiencies,* May to June 2014. The consultation set out how savings of £470-660m a year could be achieved by collective investment and greater use of passive fund management. It also sought views as to how these reforms might best be implemented. The Government's response is available online: https://www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies. • Informal engagement, July to November, 2015. Since the July Budget 2015 announcement, officials have attended over 25 workshops and bi-lateral meetings with administering authorities and the fund management industry. These discussions have been used to develop the criteria for reform and inform how the proposed power of the Secretary of State to intervene might work. In addition, the Investment Regulation Review Group was formed in 2012 to consider potential amendments to the investment regulations. The group included representatives from administering authorities, actuarial firms, pension lawyers and the fund management industry. An initial proposal for reform was prepared that has also informed the development of the draft regulations that are the subject of this consultation.

Introduction and Background

Introduction

1.1 In May 2014 the Government published a consultation which set out how savings of up to £660m a year might be achieved through greater use of passive management and pooled investment. Investing collectively can help authorities to drive down costs and access the benefits of scale, and also enables them to develop the capacity and capability to invest more cost effectively in illiquid asset classes such as infrastructure. The Government has therefore invited authorities to develop ambitious proposals for pooling assets that meet published criteria. More information about the criteria and process of reform is available on the Government's website: https://www.gov.uk/government/publications/local-government-pension-scheme-investment-reform-criteria-and-guidance.

1.2 This consultation complements that invitation, recognising that the existing regulations place restrictions on certain investments that may constrain authorities considering how best to pool their assets. It therefore proposes to move to a prudential approach to securing a diversified investment strategy that appropriately takes account of risk. In so doing, and to ensure that authorities take advantage of the benefits of scale, the Government proposes to introduce a power to allow the Secretary of State to intervene to ensure that authorities take advantage of the benefits of scale offered by pooling and deliver investment strategies that adhere to regulation and guidance.

1.3 This paper sets out the purpose and rationale of the suggested amendments to the investment regulations, and seeks views as to whether the proposed approach would best deliver those stated aims.

Background

1.4 With assets of £178bn at its last valuation on 31 March 2013, the Local Government Pension Scheme is one of the largest funded pension schemes in Europe. Several thousand employers participate in the Scheme, which has a total of 4.68 million active, deferred and pensioner members.[1] The Department for Communities and Local Government is responsible for the regulatory framework governing the Scheme in England and Wales.

1.5 The Scheme is managed through 90 administering authorities which broadly correspond to the county councils following the 1974 local government reorganisation as well as each of the 33 London boroughs. In most cases, the administering authorities are upper tier local authorities such as county or unitary councils, but there are also some authorities established specifically to manage their pension liabilities, for example the London Pension Fund Authority and the Environment Agency Pension Fund. The

[1] Scheme asset value and membership figures taken from Department for Communities and Local Government statistical data set - Local government pension scheme funds summary data: 2012 to 2013 https://www.gov.uk/government/statistical-data-sets/local-government-pension-scheme-funds-summary-data-2012-to-2013

administering authorities have individual governance and working arrangements. Each has its own funding level, cash-flow and balance of active, deferred and pensioner members. Authorities take these circumstances into account when preparing their investment strategies, which are normally agreed by the councillors on each authority's pension committee. The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 set the legal framework for the development of these investment strategies and the investments carried out by administering authorities. This consultation proposes that the Government revokes and replaces those regulations.

1.6 Under the Public Service Pensions Act 2013, there is a requirement for a national scheme advisory board, as well as a local board for each of the 90 funds. In 2013, Scheme employers and the trade unions established a shadow board, which has been considering a number of issues connected with the Scheme, including its efficient management and administration. Appointments have now been made to the national scheme advisory board and the Chair is expected to be appointed shortly.

Getting to this stage

2.1 The consultation is formed of two main proposals:

1. A package of reforms that propose to remove some the existing prescribed means of securing a diversified investment strategy and instead place the onus on authorities to determine the balance of their investments and take account of risk. The changes proposed would move towards the "prudent person" approach to investment that applies to trust based pension schemes.
2. The introduction of safeguards to ensure that the more flexible legislation proposed is used appropriately, and that the guidance on pooling assets is adhered to, including a power to allow the Secretary of State to intervene in the investment function of an administering authority when necessary.

Pooling assets to deliver the benefits of scale

2.2 The proposals set out in this consultation are the culmination of work carried out over the last two and a half years to explore how to reform the way the Scheme makes its investments in order to achieve the benefits of scale and drive efficiencies.

2.3 In summer 2013, the coalition government launched a call for evidence to explore how the Scheme might be made more sustainable and affordable in the long term. 133 responses were received, many of which took the opportunity to discuss whether collective investment and greater collaboration might deliver savings for the Scheme.

2.4 Following the call for evidence, the Minister for the Cabinet Office and Minister for Local Government commissioned a cost-benefits analysis from Hymans Robertson on a range of proposals. Hymans Robertson's report explored three areas:

- **The cost of investment:** Many of the costs associated with investment are not transparent and so difficult to capture. The costs of managing and administering the Scheme were reported as being £536 million in 2012-13.[2] However, Hymans Robertson found that the actual cost was likely to be rather higher; with investment costs alone estimated as in excess of £790 million a year.[3]
- **Approaches to collaboration:** Hymans Robertson was asked to examine the costs and benefits of three options for reform: merging the authorities into 5-10 funds, creating 5-10 collective investment vehicles, or establishing just 1-2 collective investment vehicles. They found that the net present value of savings over ten years was highest with a small number of vehicles, while merging funds offered the lowest benefit.[4]

---

[2] Local government pension scheme funds summary data: 2012 to 2013
[3] Department for Communities and Local Government: Local Government Pension Scheme structure analysis, Hymans Robertson pp. 10-11. https://www.gov.uk/government/consultations/local-government-pension-scheme-opportunities-for-collaboration-cost-savings-and-efficiencies
[4] Hymans Robertson, p.6

- **The aggregate performance of the scheme:** The report found that the Scheme as a whole had been achieving the market rate of return in each of the main equity markets over the ten years to March 2013. If the Scheme's investments in bonds and equities had been managed passively instead of actively, authorities could have saved at least £230m a year in management fees without affecting overall investment returns.[5]

2.5 Drawing on the Hymans Robertson report and the call for evidence, the coalition government published a consultation in May 2014 entitled *Opportunities for collaboration, cost savings and efficiencies*. This set out how the Scheme could save up to £660m a year by using collective investment vehicles and making greater use of passive management for listed assets like bonds and equities. The consultation sought views on these proposals, and how they might be most effectively implemented. Respondents were broadly in favour of pooling assets, but felt that any reform should be voluntary and led by administering authorities. While many recognised a role for passive management in an investment strategy, most also felt that some active management should be retained.

2.6 At the July Budget 2015, Ministers having reflected on the consultation responses, the Chancellor announced the Government's intention to invite administering authorities to bring forward proposals for pooling local government pension scheme investments. Authorities' proposals would be assessed against published criteria, designed to encourage ambition in the pursuit of efficiencies and the benefits of scale. These criteria have now been published and are available online at https://www.gov.uk/government/publications/local-government-pension-scheme-investment-reform-criteria-and-guidance.

Updating the investment regulations

2.7 When considering the implications of creating asset pools amongst authorities, some respondents to the May 2014 consultation took the opportunity to call for a review of the existing investment regulations. At their introduction in 2009, the regulations sought to ensure that authorities established a balanced and diversified portfolio by placing restrictions on the proportion of their assets that could be invested in different vehicles. For example, deposits with a single bank, institution or person, (other than the National Savings Bank), were restricted to 10% of an authority's assets. These restrictions have been kept under regular review and have been subject to change following representations from the investment sector and pension fund authorities.

2.8 Some respondents to the consultation suggested that the current limits on investments would prevent authorities from making meaningful allocations to a collective investment vehicle, one of the leading options for asset pooling, as the allocation to particular types of vehicle is capped at 35%. Participants in the London Boroughs' collective investment vehicle and the collaboration between the London Pension Fund Authority and Lancashire County Council also wrote to the Department encouraging reform in this area.

[5] Hymans Robertson, p.12

2.9 While the proposals for collective investment in the May 2014 consultation prompted encouragement to review the investment regulations, the idea of reform was not new. In 2012, following representations from the investment sector, the Government formed a small working group to revisit and examine the investment regulations with input from actuaries, fund managers and administering authorities. This group, whose membership is set out in Annex A, recommended that a more permissive approach should be taken to the legislative framework, similar to the "prudent person" model that applies to trust based pension schemes. This approach places the onus on the pension fund to determine a suitable balance of investments to meet its liabilities, which are clearly articulated in an investment strategy. The group also felt that the existing regulations introduced uncertainty for some authorities as to what constituted a permitted investment, as some asset classes were explicitly referenced but others were not. In particular, concern has been expressed as to whether or not pension fund authorities are permitted to invest in vehicles such as derivatives, hedge funds and forward currency contracts.

2.10 The proposals in this consultation paper therefore seek to address these issues, placing the onus on authorities to determine a diversified investment strategy that appropriately takes risk into account.

2.11 However, in relaxing the regulatory framework for scheme investments, it is also important to introduce safeguards to ensure that the less prescriptive approach proposed is used appropriately. Similarly, the July Budget 2015 announcement stated that draft regulations would be introduced to require an authority to pool its investments if it did not bring forward ambitious proposals that met the Government's criteria. This consultation therefore sets out how the Secretary of State might intervene to ensure that authorities take advantage of the benefits of scale offered by pooling and deliver investment strategies that adhere to regulation and guidance.

Response to the Law Commission's Review of Fiduciary Duty

2.12 The Kay Review on Fiduciary Duty published its final report in July 2012. In addition to making a number of recommendations to address the excessive focus on short-term performance in equity investment markets, it recommended that the Government ask the Law Commission to review the fiduciary duties of investment intermediaries amid concerns that these common law duties were being interpreted by some pension schemes as a requirement to focus solely on short-term financial returns.

2.13 In their report, published in July 2014, the Law Commission called on the Department to review:

- Whether the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 should transpose article 18(1) of the Institutions for Occupational Retirement Provision (IORP) Directive, and
- Those aspects of Regulation 9 of the 2009 Regulations which require investment managers to be appointed on a short-term basis and reviewed every three months.

2.14 These recommendations were supported by the Government's progress report on the implementation of the Kay Review published in October 2014 by the Department for Business Innovation and Skills.

2.15 Article 18(1) of the IORP Directive requires assets to be invested in the best interests of members and beneficiaries and, in the event of a conflict of interest, in the sole interests of members and beneficiaries.

2.16 Regulation 4 of The Occupational Pension Schemes (Investment) Regulations 2005 (SI 2005 No 3378) transposed Article 18(1):

"4. (1) The trustees of a trust scheme must exercise their powers of investment, and any fund manager to whom any discretion has been delegated under section 34 of the 1995 Act (power of investment and delegation) must exercise the discretion, in accordance with the following provisions of this regulation

(2) The assets must be invested:

(a) In the best interests of members and beneficiaries; and

(b) In the case of a potential conflict of interest, in the sole interest of members and beneficiaries."

2.17 The Local Government Pension Scheme is a statutory scheme made under section 1 of the Public Service Pensions Act 2013 and previously under The Superannuation Act 1972. It is not subject to trust law and those responsible for making investment decisions in the Scheme are not therefore required to comply with Regulation 4 of the 2005 Regulations.

2.18 However, this does nothing to change the general legal principles governing the administration of Scheme investments and how those responsible for such decisions should exercise their duties and powers under the Scheme's investment regulations.

2.19 In a circular issued by the then Department of the Environment in 1983 (No 24), the Secretary of State took the view that administering authorities should pay due regard to the principle contained in the case of Roberts v Hopwood [1925] A.C. 578 p. 595:

"A body charged with the administration for definite purposes of funds contributed in whole or in part by persons other than members of that body owes, in my view, a duty to those latter persons to conduct that administration in a fairly business-like manner with reasonable care, skill and caution, and with a due and alert regard to the interest of those contributors who are not members of the body. Towards these latter persons, the body stands somewhat in the position of trustees or managers of the property of others."

2.20 Those in local government responsible for making investment decisions must also act in accordance with ordinary public law principles, in particular, the ordinary public law principles of reasonableness. They risk challenge if a decision they make is so unreasonable that no reasonable person acting reasonably could have made it.

2.21 Having considered fully the recommendation made by the Kay Review and supported by both the Law Commission and the Government, Ministers are satisfied that the Scheme is consistent with the national legislative framework governing the duties placed on those responsible for making investment decisions. The position at common law is also indistinguishable from that produced by the 2005 Regulations applicable in respect of trust-based schemes.

2.22 We do, however, propose to remove the requirement for the performance of investment managers to be reviewed once every three months from the regulations.

Proposal 1: Adopting a local approach to investment

Deregulating and adopting a local approach to investment

3.1 In developing these draft regulations, the Government has sought, where appropriate, to deregulate and simplify the regulations that have governed the management and investment of funds since 2009. Some of the existing provisions have not been carried forward into the draft 2016 Regulations in the expectation that they would be effectively maintained by general law provisions and so specific regulation is no longer needed. For example, those making investment decisions are still required to act prudently, and there remains a statutory requirement to take and act on proper advice. Some of the provisions in the 2009 Regulations which have not been carried forward on this basis include:

- Stock lending arrangements under Regulation 3(8) and (9) of the 2009 regulations. The view is taken that the definition of "investment" in draft Regulation 3 is sufficient given that a stock lending arrangement can only be used if it falls within the ordinary meaning of an "investment".
- Regulation 8(5) of the 2009 regulations ensures that funds are managed by an adequate number of investment managers and that, where there is more than one investment manager, the value of the fund money managed by them is not disproportionate. Here, the view is taken that administering authorities should be responsible for managing their own affairs and making decisions of this kind based on prudent and proper advice.
- There are many provisions in the 2009 Regulations which impose conditions on the choice and terms of appointments of investment managers. Since the activities of investment managers are governed by the contracts under which they are appointed, the view is taken that making similar provision in the 2016 Regulations would be unnecessary duplication. Examples include the requirement for investment managers to comply with an administering authority's instructions and the power to terminate the appointment by not more than one month's notice.
- Regulation 12(3) of the 2009 Regulations requires administering authorities to state the extent to which they comply with guidance given by the Secretary of State on the Myners principles for investment decision making. As part of the wider deregulation, the draft regulations make no provision to report against these principles, although authorities should still have regard to the guidance.

3.2 These examples of deregulation are for illustrative purposes only. It is not an exhaustive list of provisions which the Government proposes to remove. Consultees are asked to look carefully at the full extent of deregulation and comment on any particular case that raises concerns about the impact such an omission might have on the effective management and investment of funds.

Investment strategy statement

3.3 As part of this deregulation, the draft regulations also propose to remove the existing schedule of limitations on investments. Instead authorities will be expected to take a prudential approach, demonstrating that they have given consideration to the suitability of different types of investment, have ensured an appropriately diverse portfolio of assets and have ensured an appropriate approach to managing risk.

3.4 Key to this will be the investment strategy statement, which authorities will be required to prepare, having taken proper advice, and publish. The statement must cover:

- A requirement to use a wide variety of investments.
- The authority’s assessment of the suitability of particular investments and types of investments.
- The authority’s approach to risk, including how it will be measured and managed.
- The authority’s approach to collaborative investment, including the use of collective investment vehicles and shared services.
- The authority’s environmental, social and corporate governance policy.
- The authority’s policy on the exercise of rights, including voting rights, attached to its investments.

Transitional arrangements

3.5 Draft regulation seven proposes to require authorities to publish an investment strategy statement no later than six months after the regulations come into force (this is currently drafted as 1 October 2016, in case the draft regulations come into effect on 1 April 2016). However, the draft regulations would also revoke the existing 2009 Regulations when they come into effect. Transitional arrangements are therefore required to ensure that an authority’s investments and investment strategy are regulated between the draft regulations coming into effect and the publication of an authority’s new investment strategy statement. The transitional arrangements proposed in draft regulation 12 would mean that the following regulations in the 2009 Regulations would remain in place until the authority publishes an investment strategy or six months lapses from the date that the regulations come into effect:

- 11 (investment policy and investment of pension fund money)
- 14 (restrictions on investments)
- 15 (requirements for increased limits)
- Schedule 1 (table of limits on investments)

Statement of Investment Principles

3.6 We do not propose to carry forward the existing requirement under regulation 12 of the 2009 Regulations to maintain a Statement of Investment Principles. However, the main elements, such as risk, diversification, corporate governance and suitability, will instead be carried forward as part of the reporting requirements of the new investment strategy statement. Administering authorities will still be required to maintain their funding strategy statements under Regulation 58 of the 2013 regulations.

Non-financial factors

3.7 The Secretary of State has made clear that using pensions and procurement policies to pursue boycotts, divestments and sanctions against foreign nations and the UK defence industry are inappropriate, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government. The Secretary of State has said, “Divisive policies undermine good community relations, and harm the economic security of families by pushing up council tax. We need to challenge and prevent the politics of division.”

3.8 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 already require administering authorities to publish and follow a statement of investment principles, which must comply with guidance issued by the Secretary of State. The draft replacement Regulations include provision for administering authorities to publish their policies on the extent to which environmental, social and corporate governance matters are taken into account in the selection, retention and realisation of investments. Guidance on how these policies should reflect foreign policy and related issues will be published ahead of the new Regulations coming into force. This will make clear to authorities that in formulating these policies their predominant concern should be the pursuit of a financial return on their investments, including over the longer term, and that, reflecting the position set out in the paragraph above, they should not pursue policies which run contrary to UK foreign policy.

Investment

3.9 A few definitions and some aspects of regulation 3, which describes what constitutes an investment for the purpose of these regulations, have been updated to take account of changing terminology and technical changes since the regulations were last issued in 2009. For example, the reference to the London International Financial Futures Exchange (LIFFE) has been removed as it now operates as a clearing house and so is covered by the approved stock exchange definition.

3.10 Some additional information has been included to make clear that certain investments, such as derivatives, may be used where appropriate. The Government expects that having considered the appropriateness of an investment in their investment strategy statement, authorities would only use derivatives as a means of managing risk, and so has not explicitly stated that this should be the case.

Questions

1. Does the proposed deregulation achieve the intended policy aim of removing any unnecessary regulation while still ensuring that authorities’ investments are made prudently and having taken advice?

2. Are there any specific issues that should be reinstated? Please explain why.

3. Is six months the appropriate period for the transitional arrangements to remain in place?

4. Should the regulation be explicit that derivatives should only be used as a risk management tool? Are there any other circumstances in which the use of derivatives would be appropriate?

Proposal 2: Introducing a safeguard - Secretary of State power of intervention

Summary of the proposal

4.1 The first part of this consultation lifts some of the existing restrictions on administering authorities' investments in order to make it easier for them to pool their investments and access the benefits of scale. To ensure that this new flexibility is used appropriately, the consultation also proposes to introduce a power to intervene in the investment function of an administering authority if the Secretary of State believes that it has not had regard to guidance and regulations. The consultation sets out the evidence that the Secretary of State may draw on before deciding to intervene, and makes clear that any direction will need to be proportionate. The power proposed in this consultation is intended to allow the Secretary of State to act if best practice or regulation is being ignored, which will help to ensure that authorities continue to pursue more efficient means of investment.

4.2 The July Budget 2015 announcement set out the Government's intention to introduce "backstop" legislation to require those authorities who do not bring forward sufficiently ambitious plans to pool their investments. It also explained that authorities' proposals would need to meet common criteria, which have been published with draft guidance alongside this consultation. The draft power to intervene discussed in this paper could be used to address authorities that do not bring forward proposals for pooling their assets in line with the published criteria and guidance. The guidance will be kept under review, and will be revised as circumstances change and authorities' asset pools evolve.

4.3 The following sections set out the process for intervention described in draft regulation 8.

Determining to intervene

4.4 The draft regulations propose to give the Secretary of State the power to intervene in the investment function an administering authority, if the Secretary of State has determined that the administering authority has failed to have regard to the regulations governing their investments or guidance issued under draft regulation 7(1). In reaching that conclusion, the Secretary of State will consider the available evidence, which might include:

- Evidence that an administering authority is ignoring information on best practice, for example, by not responding to advice provided by the scheme advisory board to local pension boards.
- Evidence that an administering authority is not following the investment regulations or has not had regard to guidance published by the Secretary of State under draft Regulation 7 (1). For example, this might include failing to participate in one of the large asset pools described in the existing draft guidance, or proposing a pooling arrangement that does not adhere to the criteria and guidance.

- Evidence that an administering authority is carrying out another pension-related function poorly, such as an unsatisfactory report under section 13(4) of the Public Service Pensions Act 2013, or another periodic reporting mechanism. (Section 13(4) of the 2013 Act requires a person appointed by the Secretary of State to report on whether the actuarial valuation of a fund has been carried out in accordance with Scheme regulations, in a way that is consistent with other authorities' valuations, and so that employer contribution rates are set to ensure the solvency and long term cost efficiency of the fund.)

4.5 If the Secretary of State has some indication to suggest that intervention might be necessary, the draft regulations propose that he may order a further investigation to provide him with the analysis required to make a decision. If additional evidence is sought, draft regulation 8(5) would allow the Secretary of State to carry out such inquiries as he considers appropriate, including seeking advice from external experts if needed. In this circumstance, the administering authority would be obliged to provide any data that was deemed necessary to determine whether intervention is required. The authority would also be invited to participate in the review and would have the opportunity to present evidence in support of its existing or proposed investment strategy.

The process of intervention

4.6 If the Secretary of State is satisfied that an intervention is required, he would then need to determine the appropriate extent of intervention in the authority's investment function. The draft regulations propose to allow the Secretary of State to draw on external advice to determine what the specific intervention should be if necessary.

4.7 Draft regulation 8(2) describes the interventions that the Secretary of State may make. The power has been left intentionally broad to ensure that a tailored and measured course of action is applied, based on the circumstances of each case. For example, in some cases it may be appropriate to apply the intervention just to certain parts of an investment strategy, whereas in particularly concerning cases, more substantial action might be required. The proposed intervention might include, but is not limited to:

- Requiring an administering authority to develop a new investment strategy statement that follows guidance published under draft Regulation 7(1).
- Directing an administering authority to invest all or a portion of its assets in a particular way that more closely adheres to the criteria and guidance, for instance through a pooled vehicle.
- Requiring that the investment functions of the administering authority are exercised by the Secretary of State or his nominee.
- Directing the implementation of the investment strategy of the administering authority to be undertaken by another body.

4.8 The Secretary of State will write to the authority outlining the proposed intervention. As a minimum, this proposal will include:

- A detailed explanation of why the Secretary of State is intervening and the evidence used to arrive at their determination.

- A clear description of the proposed intervention and how it will be implemented and monitored.
- The timetable for the intervention, including the period of time until the intervention is formally reviewed.
- The circumstances under which the intervention might be lifted prior to review.

4.9 The authority will then be given time to consider the proposal and present its argument for any changes that it thinks should be made. If, at the end of that period an intervention is issued, any resulting costs, charges and expenses incurred in administering the fund would be met by the pension fund assets.

Review

4.10 As set out above, each intervention will be subject to a formal review period which will be set by the Secretary of State but may coincide with other cyclical events such as the preparation of an annual report or a triennial valuation. At the end of that period, progress will be assessed and the Secretary of State will decide whether to end, modify or maintain the current terms of the intervention, and will notify the authority of the outcome. The authority will also have the opportunity to make representations to the Secretary of State if it feels a different course of action should be followed. Throughout this period of intervention, the authority will be supported to improve its investment function, so that it is well placed to bring the intervention to an end at the first opportunity.

4.11 The Secretary of State’s direction will include details about what is required of the authority in order to end the intervention, and how progress will be measured. Progress could, for example, be measured by creating a set of performance indicators to be monitored on an ongoing basis by Government officials, the local pension board, the scheme advisory board, or an independent body. A regime of regular formal reports to the Secretary of State could also be required.

4.12 The draft regulations also allow the Secretary of State to determine that sufficient improvement has been made to end the intervention before the review date. The administering authority may also make representations to the Secretary of State before that date, if it has clear evidence that the prescribed action is no longer appropriate.

Questions

5. Are there any other sources of evidence that the Secretary of State might draw on to establish whether an intervention is required?

6. Does the intervention allow authorities sufficient scope and time to present evidence in favour of their existing arrangements when either determining an intervention in the first place, or reviewing whether one should remain in place?

7. Does the proposed approach allow the Secretary of State sufficient flexibility to ensure that he is able to introduce a proportionate intervention?

8. Do the proposals meet the objectives of the policy, which are to allow the Secretary of State to make a proportionate intervention in the investment function of an administering authority if it has not had regard to best practice, guidance or regulation?

Summary of the draft regulations

(1) Citation, commencement and extent

This details the citation and scope of the draft regulations, and gives the date at which they will come into force.

(2) Interpretation

These provisions define terms used in the draft regulations with reference to legislation, and cite the legislation that gives administering authorities the powers that may be impacted by the draft regulations.

(3) Investment

This draft regulation defines what is considered an investment for the purposes of the regulations. This definition includes futures, options, derivatives, limited partnerships and some types of insurance contracts. It also defines who a person with whom a contract of insurance can be entered into is.

(4) Management of a pension fund

This draft regulation lists the monies that an administering authority must credit to its pension fund, including employer and employee contributions, interest, and investment capital and income. It also sets out the administering authority's responsibility to pay benefits entitled to members, and states that, except where prohibited by other regulations, costs of administering the fund can be paid by the fund.

(5) Restriction on power to borrow

This proposed regulation outlines the limited circumstances under which an administering authority can borrow money that the pension fund is liable to repay.

(6) Separate bank account

The draft regulation states that an administering authority must deposit all pension fund monies in a separate account, and lists those institutions that can act as a deposit taker. It also states that the deposit taker cannot use pension fund account to set-off any other account held by the administering authority or a connected party.

(7) Investment strategy statement

This draft regulation places an obligation on the administering authority to consult on and publish an investment strategy statement, which must be in accordance with guidance from the Secretary of State. The statement should demonstrate that investments will be suitably diversified, and it should outline the administering authority's maximum allocations for different asset classes, as well as their approach to risk and responsible investing.

In many respects, the investment strategy statement replaces the list of restrictions given in Schedule 1 of the 2009 Regulations and enables the criteria to be determined at local level. Schedule 1 of the 2009 Regulations will remain in force until such time that the new investment strategy statements have to be published.

Provision is made for authorities to publish their policy on the extent to which environmental, social and corporate governance factors are taken into account in the selection, retention and realisation of investments.

Separate guidance will be issued by the Secretary of State that will clarify how the Government's recent announcement on boycotts, sanctions and disinvestment will be exercised.

(8) Directions by the Secretary of State

This provision would grant the Secretary of State the power to intervene in the investment function of an administering authority if he is satisfied that the authority is failing to have regard to regulation and guidance. He can also initiate inquiries to determine if an intervention is warranted, and must consult with the authority concerned. Once it is determined that an intervention is needed, the Secretary of State can intervene by directing the authority undertake a broad range of actoins to remedy the situation.

(9) Investment managers

This draft regulation details how an administering authority must appoint external investment managers.

(10) Investments under section 11(1) of the Trustee Investments Act 1961

This draft regulation allows administering authorities to invest in Treasury-approved collective investment schemes.

(11) Consequential amendments

This proposed regulation lists the prior regulations that are amended by the draft amendments.

(12) Revocations and transitional provisions

The draft provision lists the regulations that would be revoked if the draft regulations come into effect. It also proposes transitional arrangements to ensure that the existing regulations governing the investment strategy remain in place until a new investment strategy statement is published by an authority under draft regulation seven. These transitional arrangements would apply for up to six months after the draft regulations came into effect.

Annex A: Members of the Investment Regulation Review Group

Alison Hamilton	Barnet Waddingham
Bob Claxton	Wandsworth Pension Fund
Clifford Sims	Squire Patton Boggs
Dawn Turner	Environment Agency Pension Fund
Geoff Reader	Bedford Pension Fund
Graeme Russell	Greater Gwent Pension Fund
Guy Sears	Investment UK
Loretta Stowers	Greater Manchester Pension Fund
Nick Buckland	Dorset Pension Fund
Nigel Keogh	Chartered Institute of Public Finance and Accountancy
Paul Dale	Bromley Borough Council
Peter Morris	Greater Manchester Pension Fund

Department for
Communities and
Local Government

Local Government Pension Scheme: Investment Reform Criteria and Guidance

November 2015
Department for Communities and Local Government

This document/publication is also available on our website at www.gov.uk/dclg

If you have any enquiries regarding this document/publication, complete the form at http://forms.communities.gov.uk/ or write to us at:

Department for Communities and Local Government
Fry Building
2 Marsham Street
London
SW1P 4DF
Telephone: 030 3444 0000

For all our latest news and updates follow us on Twitter: https://twitter.com/CommunitiesUK

November 2015

ISBN: 978-1-4098-4734-2

Contents

Ministerial Foreword

At the summer Budget 2015, the Chancellor announced our intention to invite administering authorities to bring forward proposals for pooling Local Government Pension Scheme investments, to deliver significantly reduced costs while maintaining overall investment performance.

We have been clear for some time that the existing arrangements for investment by the Local Government Pension Scheme are in need of reform, and the announcement made plain our expectation that authorities would be ambitious when developing their proposals. The publication of these criteria and their supporting guidance marks a significant milestone on the road to reform, placing authorities in a strong position to take the initiative and drive efficiencies in the Scheme, and ultimately deliver savings for local taxpayers.

The Scheme is currently organised through 89 separate local government administering authorities and a closed Environment Agency scheme, which each manage and invest their assets largely independently. Recognising the potential for greater efficiency in this system, the coalition government first began to consider the opportunity for collaboration in 2013 with a call for evidence. Since then, we have been exploring the opportunities to improve; gathering evidence, testing proposals, and listening to the views of administering authorities and the fund management industry.

The Chancellor's announcement draws on this earlier work and in particular the consultation, *Opportunities for collaboration, cost savings and efficiencies,* published in May 2014 by the coalition government. More than 200 consultation responses and papers were received and analysed, leading to the development of a framework for reform that has administering authorities at its centre. The criteria published today make clear the Government's expectation for ambitious proposals for pooling, and invite authorities to lead the design and implementation of their own pools. The criteria have been shaped and informed by earlier consultations, as well as several conversations with administering authorities and the fund management industry which took place over the summer.

Working together, authorities have a real opportunity to realise the benefits of scale that should be available to one of Europe's largest funded pension schemes. The creation of up to six British Wealth Funds, each with at least £25bn of Scheme assets, will not only drive down investment costs but also enable the authorities to develop the capacity and capability to become a world leader in infrastructure investment and help drive growth. I know that many authorities have already started to consider who they will work with and how best to achieve the benefits of scale. These early discussions place those authorities on a strong footing to deliver against our criteria, and I look forward to seeing their proposals develop over the coming months.

Marcus Jones

Criteria

1.1 In the July Budget 2015, the Chancellor announced the Government's intention to work with Local Government Pension Scheme (the Scheme) administering authorities to ensure that they pool investments to significantly reduce costs while maintaining overall investment performance. Authorities are now invited to submit proposals for pooling which the Government will assess against the criteria in this document. The Chancellor has announced that the pools should take the form of up to six British Wealth Funds, each with assets of at least £25bn, which are able to invest in infrastructure and drive local growth.

1.2 The following criteria set out how administering authorities can deliver against the Government's expectations of pooling assets.

1.3 It will be for authorities to suggest how their pooling arrangements will be constituted and will operate. In developing proposals, they should have regard to each of the four criteria, which are designed to be read in conjunction with the supporting guidance that follows. Their submissions should describe:

A. Asset pool(s) that achieve the benefits of scale: The 90 administering authorities in England and Wales should collaborate to establish, and invest through asset pools, each with at least £25bn of Scheme assets. The proposals should describe these pools, explain how each administering authority's assets will be allocated among the pools, describe the scale benefits that these arrangements are expected to deliver and explain how those benefits will be realised, measured and reported. Authorities should explain:

- The size of their pool(s) once fully operational.
- In keeping with the supporting guidance, any assets they propose to hold outside the pool(s), and the rationale for doing so.
- The type of pool(s) they are participating in, including the legal structure if relevant.
- How the pool(s) will operate, the work to be carried out internally and services to be hired from outside.
- The timetable for establishing the pool(s) and moving their assets into the pool(s). Authorities should explain how they will transparently report progress against that timetable.

B. Strong governance and decision making: The proposed governance structure for the pools should:

i. At the local level, provide authorities with assurance that their investments are being managed appropriately by the pool, in line with their stated investment strategy and in the long-term interests of their members;

ii. At the pool level, ensure that risk is adequately assessed and managed, investment implementation decisions are made with a long-term view, and a culture of continuous improvement is adopted.

Authorities should also revisit their internal processes to ensure efficient and effective decision making and risk management, while maintaining appropriate democratic accountability. Authorities should explain:

- The governance structure for their pool(s), including the accountability between the pool(s) and elected councillors, and how external scrutiny will be used.
- The mechanisms by which the authority can hold the pool(s) to account and secure assurance that their investment strategy is being implemented effectively and their investments are being well managed.
- Decision making procedures at all stages of investment, and the rationale underpinning this.
- The shared objectives for the pool(s), and any policies that are to be agreed between participants.
- The resources allocated to the running of the pool(s), including the governance budget, the number of staff needed and the skills and expertise required.
- How any environmental, social and corporate governance policies will be handled by the pool(s).
- How the authorities will act as responsible, long term investors through the pool(s), including how the pool(s) will determine and enact stewardship responsibilities.
- How the net performance of each asset class will be reported publically by the pool, to encourage the sharing of data and best practice.
- The extent to which benchmarking is used by the authority to assess their own governance and performance and that of the pool(s), for example by undertaking the Scheme Advisory Board's key performance indicator assessment.

C. **Reduced costs and excellent value for money:** In addition to the fees paid for investment, there are further hidden costs that are difficult to ascertain and so are rarely reported in most pension fund accounts. To identify savings, authorities are expected to take the lead in this area and report the costs they incur more transparently. Proposals should explain how the pool(s) will deliver substantial savings in investment fees, both in the near term and over the next 15 years, while at least maintaining overall investment performance.

Active fund management should only be used where it can be shown to deliver value for money, and authorities should report how fees and net performance in each listed asset class compare to a passive index. In addition authorities should consider setting targets for active managers which are focused on achieving risk-adjusted returns over an appropriate long term time period, rather than solely focusing on short term performance comparisons.

As part of their proposals, authorities should provide:

- A fully transparent assessment of investment costs and fees as at 31 March 2013.
- A fully transparent assessment of current investment costs and fees, prepared on the same basis as 2013 for comparison.
- A detailed estimate of savings over the next 15 years.

- A detailed estimate of implementation costs and when they will arise, including transition costs as assets are migrated into the pool(s), and an explanation of how these costs will be met.
- A proposal for reporting transparently against their forecast transition costs and savings, as well as how they will report fees and net performance.

D. An improved capacity to invest in infrastructure: Only a very small proportion of Local Government Pension Scheme assets are currently invested in infrastructure; pooling of assets may facilitate greater investment in this area. Proposals should explain how infrastructure will feature in authorities' investment strategies and how the pooling arrangements can improve the capacity and capability to invest in this asset class. Authorities should explain:

- The proportion of their fund currently allocated to infrastructure, both directly and through funds, or "fund of funds".
- How they might develop or acquire the capacity and capability to assess infrastructure projects, and reduce costs by managing any subsequent investments directly through the pool(s), rather than existing fund, or "fund of funds" arrangements.
- The proportion of their fund they intend to invest in infrastructure, and their ambition in this area going forward, as well as how they have arrived at that amount.

Addressing the criteria

Requirements and Timetable

2.1 Authorities are asked to submit their initial proposals to the Government to LGPSReform@communities.gsi.gov.uk by 19 February 2016. Submissions should include a commitment to pooling and a description of their progress towards formalising their arrangements with other authorities. Authorities can choose whether to make individual or joint submissions, or both, at this first stage.

2.2 Refined and completed submissions are expected by 15 July 2016, which fully address the criteria in this document, and provide any further information that would be helpful in evaluating the proposals. At this second stage, the submissions should comprise:

- for each pool, a joint proposal from participating authorities setting out the pooling arrangement in detail. For example, this may cover the governance structures, decision-making processes and implementation timetable; and
- for each authority, an individual return detailing the authority's commitment to, and expectations of, the pool(s). This should include their profile of costs and savings, the transition profile for their assets, and the rationale for any assets they intend to hold outside of the pools in the long term.

Assessing the proposals against criteria

2.3 The Government will continue to engage with authorities as they develop their proposals for pooling assets over the coming months. The initial submissions will be evaluated against the criteria, with feedback provided to highlight areas that may fall outside of the criteria, or where additional evidence may be required.

2.4 Once submitted, the Government will assess the final proposals against the criteria. A brief report will be provided in response, setting out the extent to which the criteria have been met and highlighting any aspects of the guidance that the Government believes have not been adequately addressed. In the first instance, the Government will work with authorities who do not develop sufficiently ambitious proposals to help them deliver a more cost effective approach to investment that draws on the benefits of scale. Where this is not possible, the Government will consider how else it can drive value for money for taxpayers, including through the use of the "backstop" legislation, should this be in place following the outcome of the consultation described below.

Transitional arrangements

2.5 Plans should be made to transfer assets to the pools as soon as practicable. Analysis commissioned by the Government from PricewaterhouseCoopers (PwC) indicates that, even those pooling mechanisms requiring supporting infrastructure, such as collective investment vehicles, could be established within 18 months. It is expected that liquid assets are transferred into the pools over a relatively short timeframe, beginning from April 2018. It is recognised that illiquid assets are likely to transition over a longer period of time. For the avoidance of doubt, investments with high penalty costs for early exit should not be wound up early on account of the pooling arrangements, but should be transferred across as soon as practicable, taking into account value for money considerations. Any assets that are held outside of the pool should be kept under review to ensure that arrangement continues to provide value for money.

2.6 While authorities will need to be mindful of their developing pooled approach, they should continue to manage both their investment strategies and manager appointments as they do now until the new arrangements are in place. In keeping with the investment regulations, they are still responsible for keeping both under regular review.

Support to develop proposals

2.7 To help authorities develop proposals quickly and efficiently, the Government has made available PwC's detailed technical analysis of the different collective investment vehicles and their tax arrangements at: https://www.gov.uk/government/publications/local-government-pension-scheme-investment-reform-criteria-and-guidance. This paper is provided for information only. It does not represent the view of Government, and authorities should seek professional advice as needed when developing their proposals. Authorities are also strongly encouraged to learn from those who have already begun to develop collective investment vehicles, such as the London Boroughs or Lancashire and the London Pension Fund Authority.

Legislative context

2.8 At the July Budget 2015, the Chancellor also announced the Government's intention to consult on "backstop" legislation that would require those administering authorities who do not come forward with sufficiently ambitious proposals to pool their assets with others. That consultation has now been published and is available on the Government's website at: https://www.gov.uk/government/consultations/revoking-and-replacing-the-local-government-pension-scheme.

2.9 The consultation proposes to introduce a power for the Secretary of State to intervene in the investment function of an administering authority where it has not had sufficient regard to guidance published by the Secretary of State. The intervention should be proportionate and subject to both consultation and review.

2.10 The draft regulations include a provision for the Secretary of State to issue guidance. Subject to the outcome of the consultation, authorities would then need to have regard to that guidance when producing their investment strategy. The Government proposes to issue this document as Secretary of State's guidance if the draft regulations come into effect. The guidance will be kept under review and may be updated, for example if the proposals for pooling that come forward are not sufficiently ambitious.

2.11 The consultation also proposes to replace and update the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 to make significant investment through pooled vehicles possible.

Supporting guidance

3.1 This guidance is to assist authorities in the design of ambitious proposals for pooling investments and to provide ongoing support as they seek to ensure value for money in the long term. It will be kept under review to ensure that it continues to represent best practice.

A. Asset pool(s) that achieve the benefits of scale

Headline criterion: The 90 administering authorities in England and Wales should collaborate to establish, and invest through asset pools, each with at least £25bn of Scheme assets. The proposals should describe these pools, explain how each administering authority's assets will be allocated among the pools, describe the scale benefits that these arrangements are expected to deliver and explain how those benefits will be realised, measured and reported.

3.2 The consultation, *Opportunities for collaboration, cost savings and efficiencies*, set out strong evidence that demonstrated how using collective investment vehicles and pooling investments can deliver substantial savings for the Local Government Pension Scheme without affecting investment performance. Additional advantages to pooling, which should further reduce costs and improve decision making in the long term, include:

- Increasing the range of asset classes to be invested in directly,
- Strengthening the governance arrangements and in-house expertise available to authorities,
- Improving transparency and long-term stewardship, and
- Facilitating better dissemination of best practice and performance data between authorities.

The case for collective investment

3.3 Published in May 2014, the analysis in the Hymans Robertson report evidenced that using collective investment vehicles could deliver savings. In the case of illiquid assets alone, they found that £240m a year could be saved if investments were channelled through a Scheme wide collective investment vehicle rather than the existing "fund of funds" approach.[1]

3.4 A review of the academic analysis available also supports the case for larger investment pools. For example, Dyck and Pomorski's paper, *Is Bigger Better? Size and performance in pension fund management*, established that larger pension funds were able to operate at lower cost than their smaller counterparts, through a combination of

---

[1] Hymans Robertson report: *Local Government Pension Scheme structure analysis,* p.3 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/307926/Hymans_Robertson_report.pdf

improved negotiating power, greater use of in-house management, and more cost effective access to alternative assets like infrastructure.[2]

> A third to a half of the benefits of size come through cost savings realized by larger plans, primarily via internal management. Up to two thirds of the economies come from substantial gains in both gross and net returns on alternatives.

3.5 A number of respondents to the May 2014 consultation also set out the case for larger funds being able to access lower cost investments. London Councils, for example, estimated that savings of £120m a year could be delivered if £24bn was invested through the London collective investment vehicle (CIV), as a result of reduced investment management fees, improved performance, and enhanced efficiency.

3.6 Formal mechanisms of pooling, such as collective investment vehicles, offer additional benefits to alternative arrangements such as procurement frameworks. For example, Hymans Robertson explained that larger asset pools would increase the opportunities for buy and sell transactions to be carried out within the Scheme, reducing the need to go to the market and so minimising transaction costs. Their analysis found that this could reduce transaction costs, which erode the value of assets invested, by £190m a year.[3]

3.7 Pooling investments will also create an opportunity to improve transparency and information sharing amongst authorities. By having a single entity responsible for negotiating with fund managers and reporting performance, authorities can see what they are paying and generating in returns and how it compares with other authorities. Similarly, Lancashire County Pension Fund and the London Pension Fund Authority, who are developing a pool for assets and liabilities, anticipate economies of scale driving improved performance. They have recently estimated that by pooling they can achieve enhanced investment outcomes of £20-£30m a year from their current levels.[4]

Achieving appropriate scale

3.8 The Government expects all administering authorities to pool their investments to achieve economies of scale and the wider benefits of sharing best practice.

3.9 A move to larger asset pools would also be in keeping with international experience. For example, in Ontario, smaller public sector pension funds are being required to come together to form pools of around $50bn Canadian (approximately £30bn at the time the proposal was made). Similarly, Australian pension funds have been consolidating in recent years, where a formal review in 2010 recommended that each MySuper pension fund be required to consider annually whether they have sufficient scale and membership to continue as a separate pension fund.[5]

---

[2] Dyck and Pomorski, *Is bigger better? Size and Performance in Pension Plan Management*, pp.14-15
[3] Hymans Robertson report, pp.14-15
[4] Sir Merrick Cockell, writing in the *Pensions Expert* on 30 September 2015
[5] Government Response to the Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System, Recommendation 1.6,

3.10 The May 2014 consultation sought views on the number of collective investment vehicles to be established. Respondents stressed the importance of balancing the need for scale with local input and practical governance arrangements. It was also argued that while larger asset pools would deliver greater savings, the potential difficulties of successfully investing large volumes of assets in a single asset class, particularly active strategies for listed assets, should also be taken into account. However, while individual managers may restrict the value of assets they are prepared to accept or are able to invest, the selection of a few managers for each asset class would help to mitigate this risk.

3.11 Having reflected on the views expressed in response to the consultation and the experience of pension funds internationally, the Government believes that in almost all cases, fewer, larger assets pools will create the conditions for lower costs and reduce the likelihood of activity being duplicated across the Scheme, for example by minimising pooled vehicle set-up and running costs. It therefore expects authorities to collaborate and invest through no more than six large asset pools, each with at least £25bn of Local Government Pension Scheme assets under management once fully operational.

3.12 However, the Government recognises that there may be a limited number of bespoke circumstances where an alternative arrangement may be more appropriate for a particular asset class or specific investment. As set out below, this may include pooling to invest in illiquid assets like infrastructure, direct holdings in property and locally targeted investments.

Investment in infrastructure and other illiquid or alternative assets

3.13 The Hymans Robertson report highlighted illiquid or alternative assets as an area for significant savings for the Scheme. They found that in 2012-2013, illiquid asset classes like private equity, hedge funds and infrastructure represented just 10% of investments made, but 40% of investment fees. They also demonstrated that changing the way these investments are made, moving away from "fund of funds" to a collective investment vehicle, could save £240m a year.[6]

3.14 The Government expects the pooling of assets to remove some of the obstacles to investing in these asset classes in a cost effective way. A separate criterion has been included on infrastructure, although similar benefits exist for other alternative or illiquid assets, such as private equity, venture capital, debt funds and new forms of alternative business finance. In light of this, authorities should consider how best to access these asset classes in a more cost-effective way. Regionally based pools, such as the London boroughs' collective investment vehicle, would allow authorities to make best use of existing relationships, while a single national pool for infrastructure or illiquid assets would deliver even greater scale and opportunity for efficiency.

3.15 A considerable shift in asset allocation would be needed to develop a pool of £25bn for investment in infrastructure and other illiquid or alternative assets, such as private equity or venture capital. The Government recognises that such a significant movement in

---

http://strongersuper.treasury.gov.au/content/Content.aspx?doc=publications/government_response/recommendation_response_chapter_1.htm

[6] Hymans Robertson report, p.24

asset allocation is unlikely in the near term. As such, should authorities elect to develop a single asset pool for illiquid investments or infrastructure, the Government recognises that a value of assets under management less than £25bn might be appropriate.

Investments outside of the pools

3.16 The Government's presumption is that all investments should be made through the pool, but we recognise that there may be a limited number of existing investments that might be less suitable to pooled arrangements, such as local initiatives or products tailored to specific liabilities. Authorities may therefore wish to explore whether to retain a small proportion of their existing investments outside of the pool, where this can demonstrate clear value for money. Any exemptions should be minimal and must be set out in the pooling proposal, alongside a supporting rationale.

Property

3.17 As of the 31 March 2014, authorities reported that they were investing around 2.5% of their assets in directly held property, with a further 4.1% invested through property investment vehicles.[7] However, the amount invested varies considerably between authorities, with some targeting investment of around 10% of their assets in direct holdings, for example.

3.18 A number of consultation responses stressed the importance of retaining direct ownership of property outside of any pooled arrangement, a view echoed in our discussions with interested parties over the summer. Directly held property is used by some authorities to match a particular part of an authority's liabilities, or to generate regular income. If these assets were then pooled, while the authority would receive the benefits of the pooled properties, there is a risk that this would not match the liability or cash-flow requirements that had underpinned the decision to invest in a particular property.

3.19 In light of the arguments brought forward by authorities and the fund management industry, the Government is prepared to accept that some existing property assets might be more effectively managed directly and not through a pool at present. However, pools should be used if new allocations are made to property, taking advantage of the opportunity to share the costs associated with the identification and management of suitable investments.

3.20 Where authorities invest more than the reported Scheme average of 2.5% in property directly, they should make this clear in their pooling submission.

Addressing the criterion

3.21 When developing their proposals for pooling, authorities should set out:

- The size of their pool(s) once fully operational.
- In keeping with the supporting guidance, any assets they propose to hold outside the pool(s), and the rationale for doing so.

---

[7] Scheme Advisory Board, Annual Report http://www.lgpsboard.org/index.php/investment-performance-2014

- The type of pool(s) they are participating in, including the legal structure if relevant.
- How the pool(s) will operate, the work to be carried out internally and services to be hired from outside.
- The timetable for establishing the pool(s) and moving their assets into the pool(s). Authorities should explain how they will transparently report progress against that timetable.

B. Strong governance and decision making

Headline criterion: The proposed governance structure for the pools should:

i. At the local level, provide authorities with assurance that their investments are being managed appropriately by the pool, in line with their stated investment strategy and in the long-term interests of their members;

ii. At the pool level, ensure that risk is adequately assessed and managed, investment implementation decisions are made with a long-term view, and a culture of continuous improvement is adopted.

Authorities should also revisit their internal processes to ensure efficient and effective decision making and risk management, while maintaining appropriate democratic accountability.

3.22 A number of consultation responses stressed the importance of establishing strong governance arrangements for pools. Securing the right balance between local input and timely, effective decision making was viewed as essential, but also a significant challenge. The management and governance arrangements of each pool will inevitably be defined by the needs of those participating. However, there are some underlying principles that the Government believes should be incorporated.

Maintaining democratic accountability

3.23 The May 2014 consultation was underpinned by the principle that asset allocation should remain with the administering authorities. Consultation respondents were strongly in favour of retaining local asset allocation, noting that each fund has a unique set of participating employers, liabilities, membership and cash-flow profiles, which need to be addressed by an investment strategy tailored to those particular circumstances.

3.24 Respondents also highlighted the transparency and accountability benefits offered by local asset allocation. If councillors are responsible for setting the investment strategy, then local taxpayers, who in part fund the Scheme through employer contributions, have an opportunity to hold their decisions directly to account through local elections. As one consultation response explained:

> The accountability of Members of the employing authorities playing a part in deciding locally how the assets of the Pension Fund are allocated is important. Employer contributions are paid, in the main, by local council tax payers who in turn vote for their local councillors. Those councillors should have the autonomy to make decisions relating to the investment strategy of that Pension Fund.

3.25 The Government agrees that this democratic link is important to the effective running of the Scheme and should not be wholly removed by the pooling of investments. As set out below, determining the investment strategy and setting the strategic asset allocation should remain with individual authorities. When developing a pool, authorities should ensure that there remains a clear link through the governance structure adopted, between the pool and the pensions committee. For example, this might take the form of a shareholding in the pool for the authority, which is exercised by a member of the pension committee.

Strategic asset allocation

3.26 Establishing the right investment strategy and strategic asset allocation is crucial to optimising performance. It is increasingly accepted that strategic asset allocation is one of the main drivers of investment returns, having far greater an impact than implementation decisions such as manager selection.

3.27 The majority of respondents to the May 2014 consultation supported local asset allocation, but discussions with interested parties over the summer have highlighted a lack of consensus as to what constitutes strategic asset allocation. Definitions have ranged from selecting high level asset classes such as the proportions in bonds, equities and property; to developing a detailed strategy setting out the extent and types of investments in each of the different equity or bond markets.

3.28 Informed by these discussions with fund managers and administering authorities, the Government believes that pension committees should continue to set the balance between investment in bonds and equities, recognising their authority's specific liability and cash-flow forecasts. Beyond this, it will be for each pool to determine which aspects of asset allocation are undertaken by the pool and which by the administering authority, having considered how best to structure decision making in order to deliver value for money. Authorities will need to consider the additional benefits of centralising decision making to better exploit synergies with other participating authorities' allocations and further drive economies of scale. When setting out their asset allocation authorities should be as transparent as possible, for example making clear the underlying asset class sought when using pooled funds.

Effective and timely decision making

3.29 Authorities should draw a distinction between locally setting the strategic asset allocation and centrally determining how that strategy is implemented. The Government expects that implementation of the investment strategy will be delegated to officers or the pool, in order to make the most of the benefits of scale and react efficiently to changing market conditions. As one consultation response suggested:

> We believe that high-level decisions about Fund objectives, strategy and allocation are best made by individual Funds considering their better knowledge of their liabilities, risk and return objectives and cash flow requirements. More detailed asset allocation decisions should however be centralised to achieve better economies of scale, and to allow more specialist management.

3.30 Authorities will need to revisit and review their decision-making processes as part of their move towards pools. For example, in order to maximise savings, manager selection will need to be undertaken at the pool level. Centralising manager selection would allow the pool to rationalise the number of managers used for a particular asset class. The resulting larger mandates should then allow the pool to negotiate lower investment fees. This approach would also give local councillors more time to dedicate to the fundamental issue of setting the overarching strategy.

3.31 A number of authorities have already delegated hiring and dismissing mangers to a sub-committee comprised predominantly of officers. This has allowed these authorities to react more quickly to changes in the market, taking advantage of opportunities as they arise. Similarly, delegating implementation decisions to the pool will allow the participating authorities to benefit not only from more streamlined decision making, but also from effecting those decisions at scale.

3.32 The creation of pools will necessarily lead to a review of decision making within each authority. The Government expects to see greater consolidation where possible. However, as a minimum, we would expect to see the selection of external fund managers and the implementation of the investment strategy to be carried out at the pooled level.

Responsible investment and effective stewardship

3.33 In June 2011, the Government invited Professor John Kay to conduct a review into UK equity markets and long-term decision making. The Kay Review considered how well equity markets were achieving their core purposes: to enhance the performance of UK companies and to enable savers to benefit from the activity of these businesses through returns to direct and indirect ownership of shares in UK companies. The review identified that short-termism is a problem in UK equity markets.[8]

3.34 Professor Kay recommended that Company directors, asset managers and asset holders adopt measures to promote both stewardship and long-term decision making. In particular, he stressed that 'asset managers can contribute more to the performance of British business (and in consequence to overall returns to their savers) through greater involvement with the companies in which they invest.'[9] He concludes that adopting such responsible investment practices will prove beneficial for investors and markets alike.

3.35 In practice, responsible investment could involve making investment decisions based on the long term, as well as playing an active role in corporate governance by exercising shareholder voting rights. Administering authorities will want to consider the findings of the Kay Review when developing their proposals, including what governance procedures and mechanisms would be needed to facilitate long term responsible investing and stewardship through a pool. The UK Stewardship Code, published by the Financial Reporting Council, also provides authorities with guidance on good practice in terms of monitoring, and engaging with, the companies in which they invest.

Enacting an environmental, social and corporate governance policy

3.36 The investment regulations currently require authorities to set out within the statement of investment principles the extent to which social, environmental or corporate governance considerations are taken into account in the selection, retention and realisation of investments. The draft regulations published alongside this document do not propose to amend this principle.

3.37 These policies should be developed in the context of the liability profile of the Scheme, and should enhance the authority's ability to manage down any funding deficit and ensure that pensions can be paid when due. Indeed, environmental, social and

---

[8] *The Kay Review of UK Equity Markets and Long-Term Decision Making*, pp. 9-10 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf
[9] The Kay Review, p.12

corporate governance policies provide a useful tool in managing financial risk, as they ensure that the wider risks associated with the viability of an investment are fully recognised.

3.38 As the Law Commission emphasised in its 2014 report on the fiduciary duty of financial intermediaries, the law generally is clear that schemes should consider any factors financially material to the performance of their investments, including social, environmental and corporate governance factors, and over the long-term, dependent on the time horizon over which their liabilities arise.

3.39 The Law Commission also clarified that, although schemes should make the pursuit of a financial return their predominant concern, they may take purely non-financial considerations into account provided that doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision.

3.40 The Government's intention is to issue guidance to authorities to clarify that such considerations should not result in policies which pursue municipal boycotts, divestments and sanctions, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government. Investment policies should not be used to give effect to municipal foreign or munitions policies that run contrary to Government policy.

3.41 Authorities will need to determine how their individual investment policies will be reflected in the pool. They should also consider how pooling could facilitate implementation of their environmental, social and corporate governance policy, for example by sharing best practice, collaborating on social investments to reduce cost or diversify risk, or using their scale to improve capability in this area.

Addressing the criterion

3.42 When developing their proposals for pooling, authorities will need to set out:

- The governance structure for their pool(s), including the accountability between the pool(s) and elected councillors, and how external scrutiny will be used.
- The mechanisms by which the authority can hold the pool(s) to account and secure assurance that their investment strategy is being implemented effectively and their investments are being well managed.
- Decision making procedures at all stages of investment, and the rationale underpinning this.
- The shared objectives for the pool(s), and any policies that are to be agreed between participants.
- The resources allocated to the running of the pool(s), including the governance budget, the number of staff needed and the skills and expertise required.
- How any ethical, social and corporate governance policies will be handled by the pool(s).
- How the authorities will act as responsible, long term investors through the pool(s), including how the pool(s) will determine and enact stewardship responsibilities.

- How the net performance of each asset class will be reported publically by the pool, to encourage the sharing of data and best practice.

- The extent to which benchmarking is used by the authority to assess their own governance and performance and that of the pool(s), for example by undertaking the Scheme Advisory Board's key performance indicator assessment.

C. Reduced costs and excellent value for money

Headline criterion: In addition to the fees paid for investment, there are further hidden costs that are difficult to ascertain and so rarely reported in most pension fund accounts. To identify savings, authorities are expected to take the lead in this area and report the costs they incur more transparently. Proposals should explain how the pool(s) will deliver substantial savings in investment fees, both in the near term and over the next 15 years, while maintaining overall investment performance.

Active fund management should only be used where it can be shown to deliver value for money, and authorities should report how fees and net performance in each listed asset class compare to a passive index. In addition authorities should consider setting targets for active managers which are focused on achieving risk-adjusted returns over an appropriate long term time period, rather than solely focusing on short term performance comparisons.

3.43 As set out in the July Budget 2015 announcement, the Government wants to see authorities bring forward proposals to reform the way their pension scheme investments are made to deliver long-term savings for local taxpayers. Authorities are invited to consider how they might best deliver value for money, minimising fees while maximising overall investment returns.

Scope for savings

3.44 Pooling investments offers an opportunity to share knowledge and reduce external investment management fees, as the fund manager is able to treat the authorities as a single client. There is already a considerable body of evidence in the public domain to support authorities in developing their proposals for investment reform and this continues to grow with new initiatives emerging from local authorities:

- **Passive management:** Hymans Robertson showed that annual fee savings of £230m could be found by moving from active to passive management of listed assets like bonds and equities, without affecting the Scheme's overall return.[10]
- Their analysis suggested that since passive management typically results in fewer shares being traded, turnover costs, which are a drag on the performance achieved through active management, might be reduced by £190m a year.[11]
- **Collective investment:** Hymans Robertson also demonstrated that £240m a year could be saved by using a collective investment vehicle instead of "fund of funds" for illiquid assets like infrastructure, hedge funds and private equity.[12]
- Similarly, the London Pension Fund Authority has estimated that they have reduced their external manager fees by 75% by bringing equity investments in-house, and hope to expand this considerably as part of their collective investment vehicle with Lancashire County Pension Fund.[13]

---

[10] Hymans Robertson report, p. 12
[11] Hymans Robertson report, pp. 14-15
[12] Hymans Robertson report, p. 3
[13] Chris Rule, LPFA Chief Investment Officer, reported in *Pension Expert* on 1 October 2015

- **Sharing services and procurement costs:** The National Procurement Framework has also helped authorities to address some of the other costs associated with investment, such as legal and custodian fees, reporting measurable savings of £16m so far.[14]

3.45 As Hymans Robertson's analysis shows, just tackling the use of "fund of funds" for illiquid assets like infrastructure could save around £240m a year, with clear opportunities to go further. It is in this context that the Government is encouraging authorities to bring forward their proposals for collaboration and cost savings. Although a particular savings target has not been set, the Government does expect authorities to be ambitious in their pursuit of economies of scale and value for money.

In-house management

3.46 Some authorities manage all or the majority of their assets internally and so can already show very low management costs. In these cases, a move to a collective investment vehicle with external fund managers is unlikely to deliver cost savings from investment fees alone. However, there are wider benefits of collaboration which authorities with in-house teams should consider when developing their proposals for pooling. A pool of internally managed assets could lead to further reductions in costs, for example by sharing staff, research and due diligence checks; it may improve access to staff with stronger expertise in particular asset classes; and could introduce greater resilience in staff recruitment, retention and succession planning. Alternatively, newly created pools might wish to work with existing in-house teams to build up expertise and take advantage of their lower running costs.

Active and passive management

3.47 The May 2014 consultation considered the use of active and passive management by the Local Government Pension Scheme. Active management attempts to select fund managers who actively choose a portfolio of assets in order to deliver a return against a specific investment target. In practice, this is often used to try and outperform a benchmark, for that class of assets over a specific period. In contrast, passive management tracks a market and aims to deliver a return in line with that market.

3.48 The consultation demonstrated that when considered in aggregate, the Scheme had been achieving a market return over the last ten years in each of the main equity markets. This suggested that collectively the Scheme could have delivered savings by using less costly passive management for listed assets like bonds and equities, without affecting overall performance. While the majority of consultation responses agreed that there was a role for passive management in a balanced portfolio, most also argued that authorities should retain the use of active management where they felt it would deliver higher net returns.

3.49 In response to that consultation, the Government has now invited authorities to bring forward proposals for pooling investments to deliver economies of scale. The extent to which passive management is used will remain a decision for each authority or pool,

[14] National LGPS Frameworks website, http://www.nationallgpsframeworks.org/national-lgps-frameworks-win-lgc-investment-award

based on their investment strategy, ongoing performance and ability to negotiate lower fees with fund managers. However, in light of the evidence set out in the Hymans Robertson report and the May 2014 consultation, authorities are encouraged to keep their balance of active and passive management under review to ensure they are delivering value for money. For example, should their net returns compare poorly against the index in a particular asset class over the longer term, authorities should consider whether they are still securing value for money for taxpayers and Scheme members.

3.50 When determining how to measure performance, authorities are encouraged to consider setting targets for active managers that are focused on achieving risk-adjusted returns over an appropriate long term time period, rather than solely focusing on short term performance comparisons.

Improving the transparency of costs

3.51 In addition to the fees paid to asset managers, there are considerable hidden costs of investment that are difficult to identify and so often go unreported by investors. In the case of the Local Government Pension Scheme, Hymans Robertson showed that investment costs in 2012-13 were at least £790m a year, in contrast to the £409m reported by the authorities.[15] Even the £790m understated the total investment costs as it excluded performance fees on alternative assets such as private equity and hedge funds (it included performance fees on traditional assets) and turnover costs (investment performance figures include the impact of turnover costs).

3.52 To really drive savings within the Scheme, it is essential that these hidden costs are better understood and reported as transparently as possible. Although many of these costs are not paid out in cash, they do erode the value of the assets available for investment and so should also be scrutinised and the opportunities for savings explored.

3.53 The Chartered Institute of Public Finance and Accountancy (CIPFA) has already made some changes to their guidance, Accounting for Local Government Pension Scheme management costs 2014, to encourage authorities to explore these costs and report some through a note to the accounts. For example, these include performance fees and management fees on pools deducted at source. Authorities should have regard to this guidance and ensure that they are reporting costs as transparently as possible.

3.54 In addition, the Scheme Advisory Board is commissioning advice to help authorities more accurately assess their transparent and hidden investment costs. Once available, authorities should take full advantage of this analysis when developing their proposals.

Addressing the criterion

3.55 As set out above, there is a clear opportunity for authorities to collaborate to deliver hundreds of millions in savings in the medium term. Although there is no overall savings target for the Scheme, the Government expects authorities to take full advantage of the benefits of pooling to reduce costs while maintaining performance.

---

[15] Hymans Robertson report, pp.10-11

3.56 To support the delivery of savings authorities bringing forward proposals are asked to set out their current investment costs in detail, and demonstrate how these will be reduced over time and the savings forecast. Where possible, costs should be reported back to 2012-2013 so that any cost reductions already achieved as a result of procurement frameworks and early fee negotiations are transparently captured.

3.57 Authorities are encouraged to provide:

- A fully transparent assessment of investment costs and fees as at 31 March 2013.
- A fully transparent assessment of current investment costs and fees, prepared on the same basis as 2013 for comparison.
- A detailed estimate of savings over the next 15 years.
- A detailed estimate of implementation costs and when they will arise, including transition costs as assets are migrated into the pool(s), and an explanation of how these costs will be met.
- A proposal for reporting transparently against their forecast transition costs and savings, as well as how they will report fees and net performance.

D. An improved capacity and capability to invest in infrastructure

Headline criterion: Only a very small proportion of Local Government Pension Scheme assets are currently invested in infrastructure; pooling of assets may facilitate greater investment in this area. Proposals should explain how infrastructure will feature in authorities' investment strategies and how the pooling arrangements can improve the capacity and capability to invest in this asset class.

3.58 Investment in infrastructure is increasingly being seen as a suitable option for pension funds, particularly amongst larger organisations. This may in part be the result of the typically long term nature of these investments, which may offer a useful match to the long term liabilities held by pension funds.

International experience

3.59 Multiple large international pension funds are investing a significant proportion of their assets in infrastructure. A recent OECD report, which analysed a sample of global pension funds as at 2012, showed that some Canadian and Australian funds (with total assets of approximately £35-40bn in 2014 terms) were investing up to 10-15% in this asset class.[16] The report also noted that those funds with the largest infrastructure allocations were investing directly, and that such investment was the result of the build up of sector-specific knowledge, expertise and resources.[17] This experience might be demonstrated through an organisation's ability to manage large projects, as well as the associated risk.

3.60 Figures published by the Scheme Advisory Board for the 2013 Annual Report show that around £550m, or 0.3%, of the Scheme's total assets of £180bn was invested in infrastructure.[18] This falls some way behind other large pension funds that have elected to invest in this area, such as those noted above and the Ontario Teachers Pension Plan which invested 6.1% according to the same 2014 report.

Creating the opportunity

3.61 The Scheme's current structure, where assets are locked into 90 separate funds, reduces scale and makes significant direct infrastructure investment more difficult for administering authorities. As a result, authorities may determine that they are unable to invest in infrastructure, or may invest indirectly, through the "fund of funds" structure. Such arrangements are expensive, as the Hymans Robertson report demonstrated and this paper sets out in paragraph 3.13.

3.62 Developing larger investment pools of at least £25bn will make it easier to develop or acquire improved capacity and capability to invest in infrastructure. In so doing, it should be possible to reduce the costs associated with investment in this area. This is likely to be the case particularly if authorities pool their infrastructure investment nationally, where the

---

[16] OECD, *Annual Survey of Large Pension Funds: report on pension funds' long-term investments*, p.32, available at: http://www.oecd.org/daf/fin/private-pensions/LargestPensionFunds2012Survey.pdf
[17] OECD report, p.14
[18] Scheme Advisory Board annual report http://www.lgpsboard.org/index.php/scheme-investments

resultant scale may allow them to buy-in or build-up in-house expertise in relevant areas, such as project and risk management.

3.63 In considering such investment, administering authorities might want to reflect on the wide range of assets that might be explored, such as railway, road or other transport facilities; utilities services like water and gas infrastructure; health, educational, court or prison facilities, and housing supply. Authorities should also examine the benefits of both:

- Greenfield infrastructure – projects involving the construction of brand new infrastructure, such as a new road or motorway junction to unlock a housing development, or the recent investment of £25m by the Greater Manchester Pension Fund to unlock new sites and build 240 houses; and
- Brownfield infrastructure – investing in pre-existing infrastructure projects, such as taking over the running of (or the construction of a new terminal building at) an airport.

3.64 As set out above, investment in infrastructure represents a viable investment for pension funds, offering long term returns to match their liabilities. Authorities will need to make their investments based on an assessment of risk, return and fit with investment strategy. However, the creation of large pools will make greater investment in infrastructure a more realistic prospect, opening up new opportunities to develop or buy-in the capacity and capability required.

3.65 In developing their proposals for pooling, authorities should take the opportunity to review their asset allocation decisions and consider how they can be more ambitious in their infrastructure investment. The Government believes that authorities can play a leading role in UK infrastructure and driving local growth, and encourages authorities to compare themselves against the example set by the leading global pension fund investors in their approach to allocating assets in this area.

Addressing the criterion

3.66 Authorities should identify their current allocation to infrastructure, and consider how the creation of up to six pools might facilitate greater investment in this area. When developing proposals, authorities should explain:

- The proportion of their fund currently allocated to infrastructure, both directly and through fund, or “fund of funds”.
- How they might develop or acquire the capability and capability to assess infrastructure projects, and reduce costs by managing any subsequent investments directly through the pool(s), rather than existing fund, or “fund of funds” arrangements.
- The proportion of their fund they intend to invest in infrastructure, and their ambition in this area going forward, as well as how they have arrived at that amount.

This page is intentionally left blank

Chris Megainey
Deputy Director, Workforce, Pay and Pensions
Department for Communities and Local Government
Fry Building
2 Marsham Street
London
SW1P 4DF

18 February 2016

Dear Chris,

Local Government Pension Scheme: Investment Reform Criteria and Guidance (DCLG, November 2015)

1. This response to the above criteria and guidance is sent on behalf of London LGPS CIV Limited (the "**London CIV**") and the 31 London local authorities (the "**boroughs**", listed at Attachment 1 for reference) that are currently active participants in establishing the Collective Investment Vehicle arrangements (the "**CIV**").

2. We note that the government requires all LGPS Administering Authorities to respond, collectively and/or individually, by 19 February 2016. We also note that this initial response should include a commitment to pooling and a description of the progress made towards that outcome. A refined and completed submission is required, and will be provided by London CIV, by 15 July 2016.

3. London Councils' Leaders' Committee had the foresight in 2012 to commission London Councils to facilitate work looking at what might be done to drive down the cost of pension's investment through greater collaboration. Since then the boroughs and London Councils have been at the forefront of working through the detail and laying the ground for others that are now starting to follow in our footsteps.

4. The CIV has taken two years to implement (facilitated by London Councils, for and on behalf of the boroughs), but is now established and operational. London CIV is fully authorised by the FCA as an Alternative Investment Fund Manager ("**AIFM**") with permission to operate a UK based Authorised Contractual Scheme fund (the "**ACS Fund**"). The ACS Fund, which is tax transparent in the UK and benefits from international tax treaties in other jurisdictions, is structured as an umbrella fund with a range of sub-funds providing access, over time, to the full range of asset classes that the boroughs require to implement their investment strategies.

5. The first sub-fund has been opened, an active global equities fund, and three authorities are the initial seed investors with £500m of assets transferred in on 2 December 2015. A further eight sub-funds, comprising a mix of active and passive equity funds, are being opened over the coming months, by the end of which it is anticipated that around £6 billion of assets will have been migrated into the ACS Fund delivering fee savings for the investing boroughs of some £3 million per annum.

6. London CIV's ambition is to be…

the investment vehicle of choice for Local Authority Pension Funds, through successful collaboration and delivery of compelling performance.

7. In summary, the key achievements we aim to deliver between now and 2020 are:

- **At least £23 billion of assets under management;**
- **Annual fund management savings rising to more than £30 million per annum;**
- **Greater access to and investment in infrastructure;**
- **Increased fund management industry influence;**
- **Wider benefits of collaboration and knowledge sharing;**

8. Turning to the specifics of the four criteria:

A. Asset pool(s) that achieve benefits of scale:

9. In consideration of the government's expectation that proposals will demonstrate commitment and be ambitious, it would seem clear that with 31 of the 33 London local authorities actively engaged in the development of the CIV such commitment and ambition is amply demonstrated.

10. The 31 boroughs participating at this time in the London CIV have assets under management, at 31 March 2015, totalling £27.6 billion. If all London LGPS funds were to participate, which it is hoped they will, total assets would increase to £29.1 billion. Clearly investment markets over the period since 31 March 2015 have been volatile and therefore assets may fall short of the above numbers. Nonetheless, if it is assumed that at least 90 per cent of borough assets will eventually be invested through the CIV (recognising that boroughs may wish to make the case for up to 10 per cent of their assets to remain outside of the CIV) then the government's threshold of each pool having assets of at least £25 billion will be met.

11. To date development of the CIV and the ACS Fund has been based on a three phase strategy as described below. This strategy reflects the principles that have been adopted to steer implementation (see Attachment 2) and the voluntary nature of participation, however it is recognised that the government's criteria and guidance have significantly changed the environment which has led to the strategy coming under review by London CIV's Board and the boroughs.

12. Despite this, London CIV and the boroughs still believe that individual boroughs should have the choice and flexibility to invest through the CIV or not, putting the onus on the CIV to demonstrate and prove its value through compelling performance, but allowing boroughs to

maintain investments outside of the CIV where they have specific needs that are not available through the Fund.

13. It should be noted that, at this stage, sub-funds will either be invested into 3rd party pooled funds or will be segregated funds with fund management being delegated to 3rd party Investment Managers ("**IM**"). However, London CIV is fully authorised to operate in-house fund management and this option will be explored at a later stage to assess whether it would deliver additional efficiencies and performance.

Phase 1 – Implementation and fund launch

14. Phase 1 is being delivered through what has become known as the "commonality" strategy. This broadly involves seeking to aggregate borough investments where two or more boroughs are invested with the same IM in the same or a very similar mandate, the aim being to increase efficiency and drive down cost.

15. The commonality strategy is a pragmatic approach that quickly delivers scale benefits for the boroughs and fee income for London CIV to cover operating costs.

16. Phase 1 is the prime focus of activity in terms of fund opening through the first half of 2016.

17. Implementation of the strategy began with the analysis of investment data gathered from across the boroughs in 2014, the aim of which was to discover which IMs the boroughs were invested through, in what asset classes and the underlying mandate strategies. This analysis showed that the 33 funds had holdings with close to 90 IMs through around 250 separate mandates. It also showed that while there was significant commonality in some asset classes (e.g. passive equity) other classes (e.g. fixed income) showed a high degree of dispersion.

18. Early discussions were held with 14 IMs where commonality could be seen, but over time, as the detail was explored, all but four decided to drop out of the process or were discounted. There were several influencing factors for this, the most prevalent of which was capacity constraint, but also included an unwillingness to reduce fees, especially for those IMs that have a 'most favoured nation' clause in their mandates.

19. In summary, the launch phase will deliver nine sub-funds:

- 2 x UK passive equity
- 2 x World Developed ex UK passive equity
- 2 x Emerging Markets passive equity
- 1 x Diversified Growth Fund (hard closed but nonetheless delivering lower fees for the boroughs currently invested)
- 2 x Global active equity

20. In aggregate, the Phase I sub-funds will account for £6.1bn, or around 23% of the boroughs' total assets under management and will involve 20 of the 31 participating authorities.

21. Total fee savings are estimated to be a minimum of £2.8 million per annum (simply through reduced IM Annual Management Charges) but could be £3 million or more per annum based

on assumptions about additional benefit derived from the tax efficient nature of the ACS Fund structure. These fee savings will not be spread equally across all the boroughs and this is largely influenced by each borough's current fee position – some boroughs have negotiated better fees than others at this point.

22. It should be noted that since passively managed equities generally have low fee scales, the ratio of fee savings to assets under management ("**AUM**") will increase as the more 'alternative' investments such as property and private equity are brought onto the fund.

23. In addition to the fee charged by each IM the London CIV will also apply a fee to each sub-fund as part of the company's cost recovery. These charges are applied at a rate appropriate to the nature of each sub-fund and range from 0.005% for the UK passive equity funds to 0.025% for the active funds.

Phase 2 – Establishing London CIV and developing the ACS Fund

24. The strategy for Phase 2, which has already commenced but with implementation starting in 2016-17, falls into two categories:

    i. Revisiting the Phase I 'commonality' strategy with those IMs that had early discussions but did not progress; and

    ii. Beginning the process of developing the fund with new manager selections in new asset classes.

25. In addition, the original nine launch sub-funds will be opened to investment from 'new' investors enabling any of the 11 boroughs (and indeed any other LGPS Fund) not included in the launch phase to transition assets from their current holdings should they wish to.

26. Attachment 3 presents analysis of the boroughs' current allocation by asset class, and from this it can be seen that the major asset classes by AUM are equities (active and passive), fixed income (active and passive) and multi-asset.

27. Category (i) will essentially follow the same process as was described in Phase I and will be applied to four Multi-Asset managers and, subject to on-going discussions with IMs and potentially one further passive equity manager.

28. The Multi-Asset products are significantly heterogeneous, and therefore it is sensible to present a fairly wide range of choice to the boroughs so that they can select a strategy which fits their particular risk appetite and investment strategy.

29. Category (ii) is driven by analysis of the borough's current holdings and the need to build AUM to deliver fee income that supports London CIV's operating costs. By reference to Attachment 3 it is clear that the focus should be on targeting the remainder of the passive and active equity assets and opening initial opportunities for Fixed Income sub-funds.

30. Passive Fixed Income mandates will be targeted in 2Q 2016-17. Earlier data collected from the boroughs suggests that the Fixed Income asset class has little in the way of commonality and conviction, so on current projections there may be approximately £500 million being transitioned each for Active and Passive. However, the active fixed income mandates are

likely to require more intensive search and selection, and therefore the bulk of the fixed income mandates will fall into the Phase 3 category (below).

31. It is anticipated that every participating borough will have opportunities to migrate to the CIV by March 2017.

32. As currently planned Phase 2 will conclude by March 2018. In terms of AUM, the end of Phase 2 will deliver an estimated £19 billion or 70 per cent of borough assets. However, the government should note that the opening of sub-funds is complex and time consuming and growth at that pace cannot be guaranteed.

Phase 3 – Business as Usual ("**BAU**")

33. BAU will be focussed initially on a continuation of developing the fund's offering and then its ongoing maintenance and enhancement. This phase will include:

    i. Opening of new asset classes (e.g. infrastructure);

    ii. The ongoing process of monitoring sub-funds, closing poor performers and opening new offerings; and

    iii. Development of the CIV's role in 'thought leadership' and being seen as a trusted source of support and advice for the boroughs.

34. Phase 3 could be seen as starting from April 2018 (i.e. the end of Phase 2), but in reality the transition from Phase 2 to Phase 3 is unlikely to be linear and there will be an overlap.

35. The successful migration of the boroughs' fixed income mandates together with the other mandates as detailed above, will lead to the asset base of London CIV increasing to an estimated £23 billion, or 86 per cent of total borough assets, by the end of 2019-20. Growth to the £25 billion threshold would be expected to happen over the following two or three years as more alternative asset classes are addressed.

36. Based on the fact that we are seeing fund management costs dropping by as much as 50 per cent (and in some cases more), and that we expect to have more negotiating power as the Fund develops, we expect to be delivering in the region of £30 million of fund management savings by 2020 (based on current fund management costs of £109 million). In addition we will be delivering other savings and benefits through greater tax efficiency, reduced procurement costs and lower fees for, for example, custody and brokerage.

37. In considering the extent to which boroughs may hold assets outside of the CIV, it can be seen from Attachment 3 that around 10 per cent of assets are held in property, private equity and infrastructure and it is in these asset classes that one would expect to find long term investments that may take several years to mature before transition to the CIV. It is of course for individual boroughs to make the case to government for holding assets outside of the CIV.

38. London CIV is focussed on delivering value for money for the participating boroughs and as such resources are tight and many tasks and activities are outsourced to 3rd parties. London CIV's current organisational structure is shown at Attachment 4. This in-house resource is augmented by expertise provided by members of the IAC (see paragraph 38) and the use of

3rd party providers including the Custodian, the Depositary, the Operating Reporting Partner, and Investment Consultants and Advisors.

39. Over time the level of resource will increase and more activity will be brought in-house, which might include in-house fund management. The company's business strategy is being reviewed at this time and more detail will be provided in the July submission.

B. Strong Governance and decision making:

40. Attachment 4 provides a diagram of the core governance structures for the CIV. Strong governance and mechanisms to ensure that participating boroughs have the assurance that they need to be confident that their investments are being managed appropriately by the pool have been critical factors in the design of this structure.

41. Taking each of the core governance structures in turn; the participating local authorities (London boroughs and potentially other non-London funds) continue to be responsible for their investment strategy and the asset allocation decisions to deliver it. As the CIV's ACS Fund develops the expectation would be that more and more of the underlying investments would be made through the CIV. Each participating borough is an equal shareholder in London CIV and a signatory to the Shareholders Agreement that sets out the relationship between and the responsibilities of each shareholder.

42. Representing the borough level, a Sectoral Joint Committee ("**PSJC**") has been established under the governing arrangements of London Councils. The PSJC effectively fulfils two roles, one is as a mechanism for convening elected Member representation from each borough (generally the borough's Pension Committee Chair), and the other is as the route to convening the boroughs as shareholders in London CIV. The committee meets most often in its first guise and has met five times since December 2014 to provide oversight and guidance as the CIV has been established. Going forward the PSJC will be the channel through which borough views about how the ACS Fund might be developed will be passed to London CIV and as a general reporting route for London CIV back to the boroughs. The committee's Terms of Reference are provided as Attachment 5. Agendas and minutes of the PSJC are published on London Councils'' website and its meetings are held in public.

43. Alongside the PSJC an Investment Advisory Committee ("**IAC**") has been established. This committee is comprised of representative borough Treasurers and Pension Fund Managers, and provides Officer level input to the oversight and development of London CIV.

44. These two committees ensure that the links with local democratic accountability for the London CIV are maintained.

45. The CIV itself is comprised of two parts, the operating company (London LGPS CIV Limited) and the ACS Fund, this structure is described in brief at paragraph 4 above.

46. As government will be aware, London CIV already has dedicated resources working for the company with a Chief Executive, Investment Oversight Director, and Chief Operating Officer, as well as support staff. In addition the Company has a highly respected Non-Executive Board in place, meeting the requirements for strong governance arrangements to be in place.

47. As an AIFM London CIV must comply with the Alternative Investment Manager Directive ("**AIFMD**") and falls under the regulatory scrutiny and reporting regime of the Financial Conduct Authority ("**FCA**"). This includes the requirement for robust systems and processes and for these to be documented appropriately in policies and manuals. Risk management is a particular focus for the FCA and London CIV has developed a risk framework and risk register covering all areas of it operations, including fund management.

48. In addition to the oversight and scrutiny arrangements described above, it is a requirement for London CIV to engage a Depositary to provide oversight of the Fund Custodian and London CIV as the fund operator. Northern Trust have been contracted to provide this service, which is effectively there to provide additional assurance and protection to the boroughs as investors.

49. As described above the participating boroughs will be closely involved in the development of the ACS Fund, including in the decisions about what new sub-funds might opened and in what asset class. The IAC is also expected to be involved in the search and selection process for IMs. However, the final due diligence consideration and appointment of IMs falls under the regulatory responsibilities of London CIV through its Investment Oversight Committee and Board. Boroughs will decide which of the sub-funds they wish to invest in to best deliver their investment strategy.

50. The processes for London CIV to report on fund performance to the investing boroughs are still being developed, but in broad terms will include regular written and verbal reports to the PSJC, the IAC and to individual borough Pension Committees as required. However, the development of final arrangements for reporting is likely to be an iterative process to ensure that they are efficient and fit for purpose for both the investors and for London CIV. It is the intention that every borough will receive performance reporting across every sub-fund (regardless of whether they are invested in that sub-fund or not), in this way boroughs will be able to easily compare performance of sub-funds they are invested in with other similar sub-funds.

51. With regards to providing assurance on environmental, social and governance issues and how this will be handled by the CIV, this has already been the subject of consideration by the company and the PSJC with an agreement that the London CIV should be a separate member of the Local Authority Pension Fund Forum (the "**LAPFF**") – a body which represents the majority of views of local authority pension funds on these matters. Discussions have commenced with the LAPFF to put this arrangement in place.

52. London CIV is also currently considering how it will meet the requirements of the Stewardship Code and anticipates being a signatory to this in due course.

53. The IAC has also established a working group to look at the whole issue of ESG matters and how funds can best access this through the London CIV and how to assist funds in acting as long term responsible shareholders.

54. For individual funds, they will of course need to maintain their own policies in respect of ESG matters and this will comprise part of their new Investment Strategy Statement which replaces the Statement of Investment Principles later this year.

C. Reduced costs and excellent value for money:

55. London CIV anticipates significant fee savings arising over time, from scale and increased negotiating power with managers. As described above, Phase 1 of the Fund development is expected to deliver around £3 million of savings p.a. for the 20 boroughs that will be invested. It should be recognised that the first phase represents relatively low cost asset classes with the majority being in passive asset classes, it is inevitable that as more complex and expensive assets are added then fee savings will significantly increase. To date London CIV has seen fee reductions of up 50 per cent.

56. In addition to the anticipated fee savings, we also expect to accrue significant advantages from the tax transparent nature of the ACS structure and savings across the entire spectrum of investment costs, including reduced custodian fees, lower procurement costs etc. In 2012 the Society of London Treasurers in 2012 had the foresight to commission a report from PWC that estimated that an additional £85 million could be derived in terms of improved investment returns by delivering superior performance. Whilst clearly this figure is open to some debate, it does give an indication of what might be achieved for funds through greater collaboration and delivering improved performance overall.

57. London CIV will be working with the participating boroughs to gather the data necessary to provide the requested assessment of investment costs and fees as at 31 March 2013, the current position and estimated savings over the next 15 years. This information will be provided in the July submission.

58. Transition costs are complex and extremely difficult to estimate in isolation from the case by case detail of each specific transition. Costs in this area can accrue from fees (e.g. transition managers, custodians and tax advisors) and transaction costs (e.g. the cost of buying and selling assets, including unavoidable tax in some jurisdictions). London CIV is working hard to bear down on transition costs and will continue to do so. It is anticipated that more detail can be provided in the July submission.

59. In addition to reduced costs and fees the wider governance benefits from information sharing and improved access to expertise at all levels should not under estimated as significant advantages from collaboration.

60. LGPS funds clearly understand the need to look at the risk adjusted returns over the longer time frame and that it is the net value-add that impacts on the fund’s ability to pay pensions over the longer term. It is clear that avoiding knee jerk reactions when managers experience periods of underperformance is an important factor and we are pleased to see the government has recognised this in asking for funds to consider what is achieved over an appropriate long term period, rather than solely focusing on short term performance comparisons. London CIV is firmly of the view that ‘churn’ of IMs will be reduced through the CIV as part of the enhanced governance arrangements and knowledge sharing that is being established.

D. An improved capacity to invest in infrastructure:

61. One of the big opportunities from creating the CIV is the potential to use the benefit of scale to enable the boroughs to access infrastructure as an asset class. London CIV and the

boroughs have begun to consider infrastructure as an asset class and what different and innovative approaches might be taken to deliver benefits both in London and nationally. Detailed proposals are likely to fall towards the end of Phase 2 of our development. Early discussions have been had with a number of IMs in this area and also with the Pensions Infrastructure Platform.

62. As can be seen from Attachment 3, LGPS funds across London currently have little or no assets invested in infrastructure. Most boroughs have limited resources to dedicate to considering this complex asset class and experience shows that there is a general lack of suitable investments at the scale that the average borough would wish to invest and with the required risk/return profile. However, there appears to be no evidence that any London LGPS fund is strategically opposed to infrastructure investment as an asset class per se.

63. Nonetheless, pooling of each borough's allocation to infrastructure and opening the opportunity for those that currently have no allocation will generate a greater capacity to invest, enabling the CIV to look at opportunities either direct or as co-investments that would not have been open to individual funds, often simply because of the cost of entry.

64. Determining the proportion of assets to allocate to infrastructure will be a decision for each investor to take as part of their Asset Allocation strategy. These decisions will depend on the opportunities that can be made available and on the level of risk and reward generated from those opportunities when compared against risk/reward in other asset classes.

In conclusion

65. London CIV believes that the work that has been undertaken by those London Boroughs that have contributed to the development of the CIV demonstrates a clear commitment to the principles of collaboration and collectivisation. The creation of London CIV has been instrumental in driving forward the investment reform agenda in London. The scale of asset pooling that we anticipate will be achieved in London is sufficiently large for the London CIV to meet the criteria for scale over the timescales being required. We believe that we have developed both the appropriate structure for London funds and that the governance structures in place mean that local accountability and decision making on asset allocation are retained.

66. Consequently we strongly believe given the willingness shown and progress made by the London funds over the last 2 years means that we are able to meet the criteria to be confirmed as one of the final pools of assets under the government's reform agenda.

67. We recognise that further work is required, but that London CIV and the participating boroughs are in a strong position to be able to come forward with comprehensive proposals to meet the government's criteria and guidance when submitting these in July 2016.

68. Despite the scale, complexity and untested nature of the London boroughs collaborations, the London CIV has successfully navigated these challenges and is now well on the way to achieving the government's four criteria of scale, costs savings, governance and access to infrastructure

Local Government Pension Scheme: Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations2009 (the "Regulations")

69. It is recognised that in application the Regulations do not apply directly to London CIV but do determine the way that the boroughs manage and invest their funds and therefore have an influence over how London CIV and its investors will operate in the future. As such London CIV expects that each borough will respond to the consultation and this response only covers issues that relate, or could relate to London CIV specifically.

70. London CIV is broadly supportive of relaxing the regulatory framework for LGPS investments and the move to a 'prudent' basis, but as a principle does not support wide ranging powers for the Secretary of State to intervene. This concern about powers of intervention is especially true in circumstances where the guidance setting out how the power will be used has not been published.

71. In the context of LGPS Funds being required to invest through pooling arrangements (e.g. London CIV) it is not clear whether the Funds would be required to apply Section 9 of the Regulations when deciding to invest through a pool. London CIV is structured as a Private Limited Company (wholly owned by the participating authorities) and is authorised by the FCA as an AIFM with permission to operate an ACS, effectively this means that London CIV is an Investment Manager. London CIV believes that 'recognised' pools should be explicitly addressed in the regulations to avoid confusion, prevent unnecessary bureaucracy and to give reassurance to individual LGPS Funds – especially in this period of change.

72. In addition, London CIV is of the view that care should be taken over the wording of Section 7(4) which, as currently drafted, may have the effect of preventing LGPS Funds from investing in pools where Members or officers of the authority have decision making roles in those pools as a part owner of that pool. Again specific measures relating to recognised pools would provide clarity.

73. On the question of the use of derivatives; it should be recognised that derivatives can be use d to control outcomes in many ways, it is not just about risk per se. Derivatives can be used to produce more certain outcomes, be more efficient as an instrument to use as an investment than an actual asset due to increased liquidity and visibility of pricing; be more liquid than some real assets might be; and allow investment managers to reflect macro-economic views without having to churn large parts of the portfolio. Although controlling these outcomes is all about balancing risk and return it is not just risk management – there is a clear difference between the two and accordingly we would urge that the regulations should not be explicit that derivatives should only be used as a risk management tool.

London CIV would welcome the opportunity to discuss this submission in more detail with government officials and Ministers.

Yours sincerely

Hugh Grover
Chief Executive

Hugh.grover@londonciv.org.uk
020 7934 9942

Attachment 1: Participating local authorities

City of London Corporation

London Borough of Barnet

London Borough of Barking and Dagenham

London Borough of Bexley

London Borough of Brent

London Borough of Camden

London Borough of Croydon

London Borough of Ealing

London Borough of Enfield

London Borough of Hackney

London Borough of Haringey

London Borough of Harrow

London Borough of Hammersmith and Fulham

London Borough of Havering

London Borough of Hounslow

London Borough of Islington

London Borough of Lambeth

London Borough of Lewisham

London Borough of Merton

London Borough of Newham

London Borough of Redbridge

London Borough of Southwark

London Borough of Sutton

London Borough of Tower Hamlets

London Borough of Waltham Forest

London Borough of Richmond upon Thames

Royal Borough of Greenwich

Royal Borough of Kensington and Chelsea

Royal Borough of Kingston upon Thames

Wandsworth London Borough Council

Westminster City Council

Attachment 2: London CIV guiding principles

1. Investment in the ACS should be voluntary, both entry and withdrawal.
2. Boroughs choose which asset classes to invest into, and how much.
3. Boroughs should have sufficient control over the ACS Operator.
4. Investing authorities will take a shareholding interest in the Operator.
5. Shareholders will have membership of the Pensions Joint committee.
6. ACS Operator will provide regular information to participating boroughs.
7. ACS will not increase the overall investment risk faced by boroughs.

Attachment 3: Analysis of current borough holdings

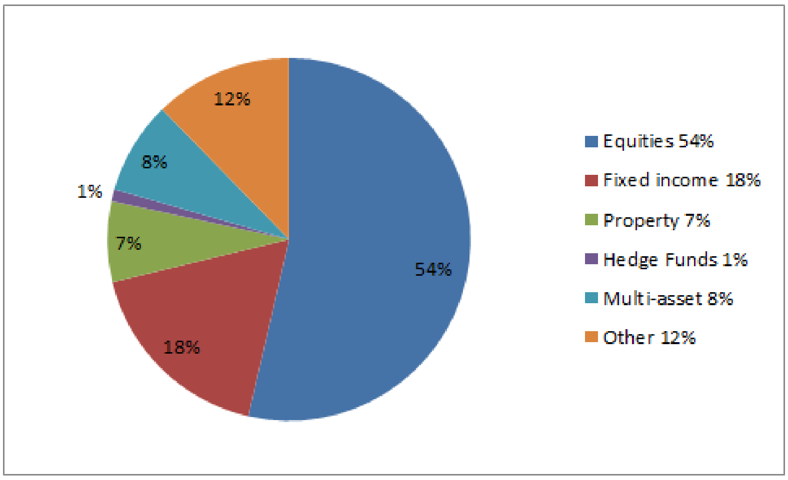
<u>Current asset allocation</u>

The breakdown of the pension fund assets as of 31 March 2015 for the 31 participating London boroughs can be seen below:

Table 1

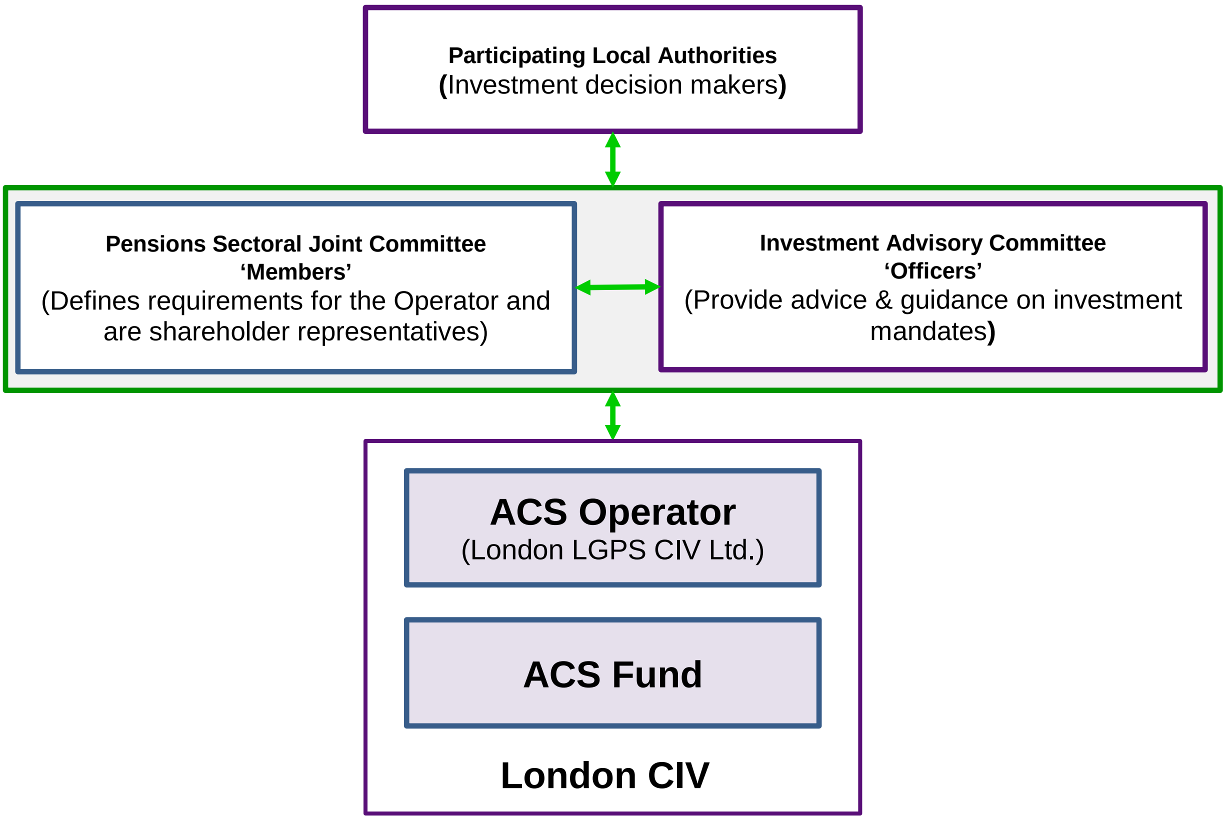
Allocation	£m, March 2015	Percentage
UK equities	5,077.39	18.9%
overseas equities	6,560.63	24.4%
unallocated	2,748.31	10.2%
total equities	**14,386.33**	**53.6%**
UK fixed interest	2,636.29	9.8%
overseas fixed interest	808.32	3.0%
unallocated	863.04	3.2%
total fixed interest	**4,307.65**	**16.0%**
UK index linked	312.52	1.2%
overseas index linked	30.01	0.1%
unallocated	80.43	0.3%
total index linked	**422.96**	**1.6%**
UK property	1,350.87	5.0%
overseas property	56.85	0.2%
unallocated	517.01	1.9%
total property	**1,924.73**	**7.2%**
UK hedge funds	32.40	0.1%
overseas hedge funds	-	0.0%
unallocated	256.56	1.0%
total hedge funds	**288.96**	**1.1%**
UK other	783.74	2.9%
overseas other	963.62	3.6%
Multi-asset	**2,214.31**	**8.2%**
Total unallocated	**3,961.67**	**14.8%**
infrastructure	193.53	0.7%
commodities	57.43	0.2%
private equity	525.05	2.0%
derivatives	- 2.28	0.0%
currency overlay	-	0.0%
cash	777.37	2.9%
Total investment assets	**26,843.38**	**100.0%**

NB the multi-asset allocation is done on a “best efforts basis” due to conflicting and out of date data.

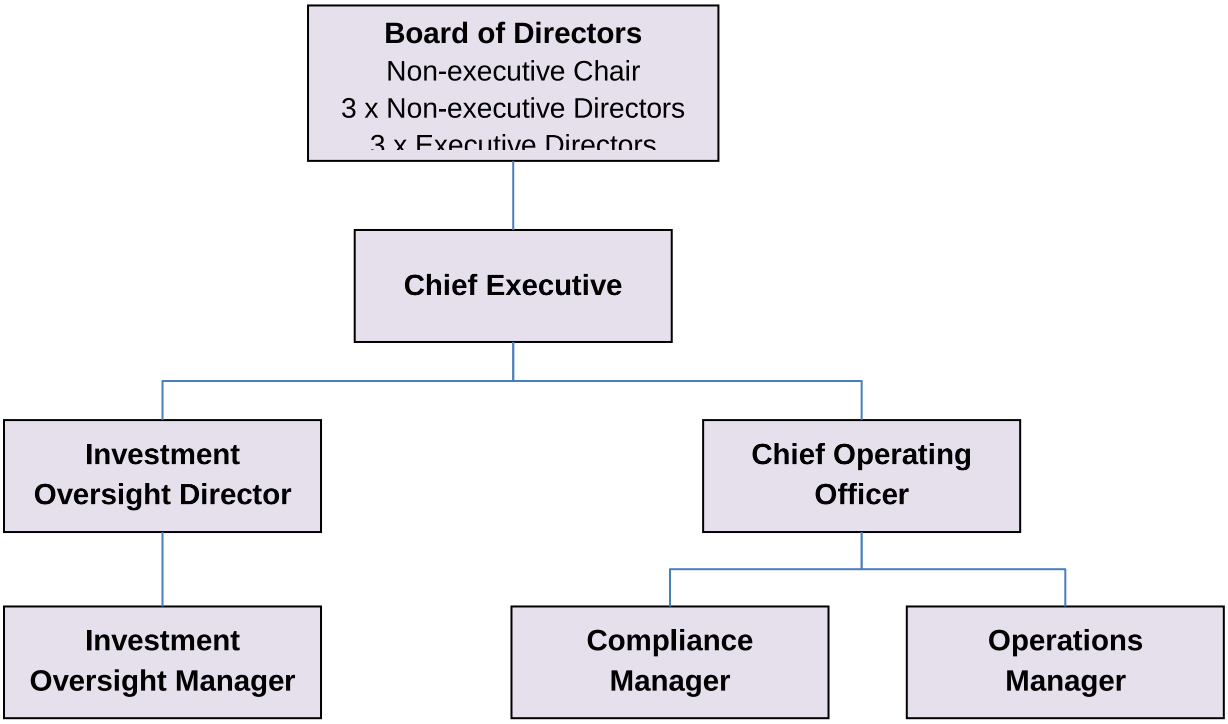


Attachment 4:

London CIV governance diagram



London CIV organisation chart



Attachment 5: Pensions Sectoral Joint Committee Terms of Reference

Constitution

1.a.1 The Pensions CIV Joint Committee is a sectoral joint committee operating under the London Councils governance arrangements.[1]

1.a.2 Each London local authority participating in the arrangements shall appoint a representative to the Pensions CIV Joint Committee being either the Leader of the local authority or the elected mayor as applicable or a deputy appointed for these purposes.[2]

1.a.3 The Pensions CIV Joint Committee shall appoint a Chair and Vice-Chair.

1.a.4 The Pensions CIV Joint Committee shall meet at least once each year to act as a forum for the participating authorities to consider and provide guidance on the direction and performance of the CIV, In addition, members of the Pensions CIV Joint Committee shall meet at least once each year at an Annual General Meeting of the ACS Operator in their capacity as representing shareholders of the ACS Operator.

1.a.5 Subject to Clause 1.1.4 above, meetings of the Pensions CIV Joint Committee shall be called in accordance with London Councils' Standing Orders and the procedure to be adopted at such meetings shall be determined in accordance with those Standing Orders.

1.a.6 If the Pensions CIV Joint Committee is required to make decisions on specialist matters in which the members of the Pensions CIV Joint Committee do not have expertise the Pensions CIV Joint Committee shall arrange for an adviser(s) to attend the relevant meeting to provide specialist advice to members of the Pensions CIV Joint Committee.

Quorum

1.a.7 The requirements of the Standing Orders of London Councils regarding quorum and voting shall apply to meetings of the Pensions CIV Joint Committee.

[1] The London Councils' Governing Agreement dated 13 December 2001 (as amended), London Councils' Standing Orders, Financial Regulations and other policies and procedures as relevant.

[2] Clause 4.5 of the London Councils' Governing Agreement dated 13 December 2001 (as amended).

Membership

[As amended from time to time]

Terms of Reference

1.a.8 To act as a representative body for those London local authorities that have chosen to take a shareholding in the Authorised Contractual Scheme (ACS) Operator company established for the purposes of a London Pensions Common Investment Vehicle (CIV).

1.a.9 To exercise functions of the participating London local authorities involving the exercise of sections 1 and 4 of the Localism Act 2011 where that relates to the actions of the participating London local authorities as shareholders of the ACS Operator company.

To act as a forum for the participating authorities to consider and provide guidance on the direction and performance of the CIV and, in particular, to receive and consider reports and information from the ACS Operator particularly performance information and to provide comment and guidance in response (in so far as required and permitted by Companies Act 2006 requirements and FCA regulations).

1.a.10 In addition, members of the Pensions CIV Joint Committee will meet at least once each year at an Annual General Meeting of the ACS Operator to take decisions on behalf of the participating London local authorities in their capacity as shareholders exercising the shareholder rights in relation to the Pensions CIV Authorised Contractual Scheme operator (as provided in the Companies Act 2006 and the Articles of Association of the ACS Operator company) and to communicate these decisions to the Board of the ACS Operator company. These include:

1.a.10.1 the appointment of directors to the ACS Operator board of directors;

1.a.10.2 the appointment and removal of auditors of the company;

1.a.10.3 agreeing the Articles of Association of the company and consenting to any amendments to these;

1.a.10.4 receiving the Accounts and Annual Report of the company;

1.a.10.5 exercising rights to require the directors of the ACS Operator company to call a general meeting of the company;

City of Westminster

Pension Fund Committee

Date:	**22nd March 2016**
Classification:	**General Release**
Title:	**Underlying risks in accepting admitted bodies to the pension scheme**
Report of:	**City Treasurer**
Financial Summary:	**The report has no immediate financial implications. However the absence of a clearly established admissions policy and on-going risk monitoring to manage the risks associated with admission bodies could result in costs falling upon the Fund in future.**
Report Author and Contact Details:	**George Bruce 0207 641 1067**

1. Executive Summary

1.1 At the 16th November 2015 meeting, the Pension Fund Committee requested a report on the underlying risks and mitigations in accepting admitted bodies to the pension fund. This report outlines the risks and the mitigation actions available.

2. Recommendation

2.1 That the Pension Fund Committee note the risks and mitigation actions available and agrees to the City Treasurer preparing an admissions policy and risk monitoring arrangements to be reported back to a subsequent meeting of the Committee.

3. Background

3.1 The Local Government Pension Scheme (LGPS) has two broad classes of membership, namely:

a) scheduled bodies largely comprising principal local authorities such as the City Council, but also a range of specific bodies, including academies, set out in Part 1 of Schedule 2 of the LGPS Regulations 2013, whose employees are members of the LGPS as of right; and

b) admission (or admitted) bodies whose employees can become members of the LGPS under an admission agreement.

3.2 When functions or services of the Council are out-sourced to a third party, the pay, terms and conditions of employment for any employees transferred from the Council are protected under the Transfer of Undertakings (Protection of Employment) Regulations 2006. This includes obligations to provide a pension. Consequently the recipient employer of those transferred staff can either become an admitted body of the LGPS or provide their own pension scheme.

3.3 Admission bodies fall into two broad categories:

a) Community admission bodies, which are largely bodies which provide a public service other than for gain, such as charitable bodies and joint committees of local authorities. These often have links to a local authority or another Scheme employer as defined in Part 2 of Schedule 2 to the LGPS Regulations 2013; and
b) Transferee admission bodies, which are either:
   i. bodies formed when a service provided by a local authority or another scheduled body is contracted out the private sector; or
   ii. bodies providing a public service in the United Kingdom approved in writing by the Secretary of State.

3.4 Admission bodies can only join the LGPS subject to an admission agreement. Admission varies:

a) Admission of community admission bodies and bodies providing a public service and approved by the Secretary of State is at the discretion of Westminster City Council as the administering authority;
b) Admission of transferee bodies formed when services are contracted out is mandatory provide they meet the requirements of the LGPS Regulations 2013.

4. Risks

4.1 The risks arising from admitting new employers as admission bodies to the City of Westminster Pension Fund include:

a) avoiding underfunded default by an admitted body leaving liabilities with the pension fund;
b) premature termination of a contract for outsourced services;
c) the ongoing solvency of the admitted body to meet pension contributions;
d) assets insufficient to pension liabilities particularly where there is a sudden spike in pension liabilities, such as a ill-health retirement;
e) transferring staff with an inherited pension deficit which creates a liability on the admitted body from the start of its operations.

5. Mitigating actions available

5.1 Under the LGPS Regulations 2013 the administering authority can either require an admission body to enter into:

a) an indemnity or bond approved by the Fund; or
b) a guarantee from another organisation or the Secretary of State where either funds or controls the admission body.

Paragraph 8.1 of the Funding Strategy Statement approved in 2014, requires all new admission bodies to have a bond or a guarantee from another employer in the Fund before they can be admitted.

5.2 Other ways to mitigate admitted body risk include ill-health insurance, and the use of stronger actuarial assumptions in determining contribution rates and deficit recovery periods. For example, contribution rates for admission bodies tend to be significantly higher than the Council's total contribution rate. Also deficit recovery periods are much shorter than the Council's recovery period and are usually linked to the length of the contract.

Paragraph 6.2 of the Funding Strategy Statement aligns the deficit recovery period for:

a) community admission bodies to the strength of the covenant and any guarantees; and
b) transferee admission bodies to the length of the contract.

5.3 The LGPS Regulations 2013 require the prospective admission body to carry out an assessment of the level of risk arising on premature termination of the provision of service or assets by reason of insolvency, taking account of actuarial advice. The risk assessment must be carried out to the satisfaction of the administering authority and any scheme employer in the case of an outsourcing.

5.4 The cost of the risk assessment falls upon the prospective admission body.

5.5 Where the level of risk identified by the risk assessment requires it, the admission body will be required to enter into an indemnity or bond in a form approved by the administering authority with a body specified in the Regulations.

5.6 The Fund would need to ensure that the level of indemnity or bond provided was sufficient to cover the identified risk.

5.7 In the event that it is not desirable for an admission body to enter into an indemnity or bond, the admission agreement must provide that the admission body secures a guarantee in a form satisfactory to the administering authority. The guarantor has to be either:

a) another organisation or Scheme employer which funds or controls the admission body or
b) the Secretary of State where the admission body is statutorily established and funded from central government.

5.8 In assessing any guarantee there would need to be an assessment of the strength of the parent organisation's covenant to make good the guarantee.

5.9 The LGPS Regulations 2013 require all admission agreements to include the following safeguards:

a) provision to terminate if the admission body ceases existence
b) provisions requiring the admission body to notify the administering authority of any matter which might affect its continuing participation in the LGPS;
c) specific obligations on the admission body to notify the administering authority of any change in status, including takeover, reconstruction, amalagamation, insolvency, winding up, receivership, liquidation or material change in the body's business or constitution;
d) a right of the administering authority to terminate the admission agreement in the event of insolvency, winding up, or liquidation of the admission body, a material breach of any obligations under the admission agreement or a failure to pay sums due to the Fund within a reasonable period of time after notice from the Fund.

These safeguards should enable the Fund to act fast, and recover any payments due.

6 Financial Implications

6.1 The absence of a clearly established admissions policy and ongoing risk monitoring to manage the risks associated with admission bodies could result in costs falling upon the Fund in future.

7. Legal Implications

7.1 The absence of clearly established admissions arrangements compliant with the LGPS Regulations 2013 could expose the City of Westminster Pension Fund to the risk of legal challenge.

If you have any questions about this report, or wish to inspect one of the background papers, please contact:
George Bruce Tel: 0207 641 1067

City of Westminster

Committee Report

Decision Maker:	**PENSION FUND COMMITTEE**
Date:	**22 March 2016**
Classification:	**General Release**
Title:	**Fund Financial Management**
Wards Affected:	**All**
Policy Context:	**Effective control over Council Activities**
Financial Summary:	**There are no immediate financial implications arising from this report.**
Report of:	**Steven Mair** ***City Treasurer*** **smair@westminster.gov.uk** **020 7641 2904**

1. Executive Summary

1.1 This report presents a variety of information that will assist the Pension Fund Committee in monitoring key areas to ensure effective control of the Fund's operations and help inform strategic decisions.

2. Recommendations

2.1 The Committee is asked approve the updated risk register for the Pension Fund.

2.2 The Committee is asked to note the Fund's compliance with the limits specified in Schedule 1 of the LGPS (Management and Investment of Funds) Regulations 2009.

2.3 The Committee is asked to note the Class Actions update.

2.4 The Committee is asked to note the cashflow position of the Fund and agree the proposed deferment of monthly cash transfers from the Fund Managers until May 2016.

3. Risk Register Monitoring

3.1 The risk register has been reviewed by officers and is attached as Appendix 1 for information. The rationale for the changes is set out on the first page of the Appendix.

4. Investment Regulations Limits Review

4.1 As at 31 December 2015, the Fund complied with the LGPS (Management and Investment of Funds) Regulations 2009 as documented in the Statement of Investment Principles.

4.2 In particular, the Fund had no self-investments (regulatory maximum of 5%), it had no single segregated holding great than 10% and its largest investment in a single vehicle was 23.05% with Majedie against the limit of 35%. The LGIM holding is split between two vehicles.

5. Class Actions Update

5.1 The report from SRKW provided by IPS on recent class action matters is attached as Appendix 2. This report highlights all new and on-going investor class actions and specifically identifies those relevant to the City of Westminster Pension Fund. There are no new actions recommended for consideration.

6. Consultations / Legislation Changes

<u>Pooling of Investments</u>

6.1 See item 5 on the agenda.

7. Cashflow Monitoring

7.1 At the November 2016 meeting, Committee members were presented with the Fund's actual cashflow position from the start of the financial year to October 2015 and the forecast to March 2020.

7.2 The cashflow forecast has been updated to reflect actuals to the end of February 2016 and is included at Appendix 3.

7.3 Currently the forecast cash balance for 31 March 2016 is £6.2m. This is an improvement of £1.1m on the forecast reported in November 2015. In view of the improved cash forecast, it is proposed that the monthly programme of cash transfers from the Fund Managers be deferred until May 2016.

If you have any questions about this report, or wish to inspect one of the background papers, please contact the report author:

Nikki Parsons nparsons@westminster.gov.uk or 020 7641 6925

BACKGROUND PAPERS: None

APPENDICES:

Appendix 1 – Pension Fund Risk Register
Appendix 2 – SRKW Report 1 October to 31 December 2015
Appendix 3 – Cash Flow Monitoring

This page is intentionally left blank

Appendix 1: Pension Fund Risk Register, March 2016

Changes to the risk register since previous quarter

Type	Ref	Risk	Rationale
New	24	**Operational: Administration** BT unable to provide an interface file in a format suitable for Surrey CC to update service records and undertake day to day operations.	Inaccuracies in service records held on the pensions administration system may impact on the triennial funding valuation at March 2016 and notifications to starters and leavers.

Pension Fund risk register, March 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
1	**STRATEGIC: INVESTMENT** That the combination of assets in the investment portfolio fails to fund the liabilities in the long term.	• Investment strategy in place and reviewed periodically. • Performance is measured against a liability based benchmark. • Fund performance is reviewed quarterly.	2	3	Low 6	City Treasurer	June 2016
2	**STRATEGIC: INVESTMENT** Fund managers fail to achieve the returns agreed in their management agreements.	• Independent monitoring of fund manager performance by custodian against targets. • Investment adviser retained to keep watching brief. • Fund manager performance is reviewed quarterly.	3	3	Low 9	City Treasurer	June 2016
3	**STRATEGIC: INVESTMENT** Failure of custodian or counterparty.	• At time of appointment, ensure assets are separately registered and segregated by owner. • Review of internal control reports on an annual basis. • Credit rating kept under review.	2	5	Low 10	City Treasurer	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
4	**STRATEGIC: FUNDING** The level of inflation and interest rates assumed in the valuation may be inaccurate leading to higher than expected liabilities.	• Review at each triennial valuation and challenge actuary as required. • Growth assets and inflation linked assets in the portfolio should rise as inflation rises.	4	3	Medium 12	City Treasurer	June 2016
5	**STRATEGIC: FUNDING** There is insufficient cash available in the Fund to meet pension payments leading to investment assets being sold at sub-optimal prices to meet pension payments.	• Cashflow forecast maintained and monitored. • Cashflow position reported to sub-committee quarterly. • Cashflow requirement is a factor in current investment strategy review.	2	1	Very Low 2	City Treasurer	June 2016
6	**STRATEGIC: FUNDING** Scheme members live longer than expected leading to higher than expected liabilities.	• Review at each triennial valuation and challenge actuary as required.	4	2	Low 8	City Treasurer	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
7	**STRATEGIC: FUNDING** Scheme matures more quickly than expected due to public sector spending cuts, resulting in contributions reducing and pension payments increasing.	• Review maturity of scheme at each triennial valuation. • Deficit contributions specified as lump sums, rather than percentage of payroll to maintain monetary value of contributions. • Cashflow position monitored monthly.	2	3	Low 6	City Treasurer	June 2016
8	**STRATEGIC: REGULATION** Pensions legislation or regulation changes resulting in an increase in the cost of the scheme or increased administration.	• Maintain links with central government and national bodies to keep abreast of national issues. • Respond to all consultations and lobby as appropriate to ensure consequences of changes to legislation are understood.	3	4	Medium 12	City Treasurer and Acting Director of HR	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
9	**STRATEGIC: REGULATION** Introduction of European Directive MiFID II results is a restriction of Fund's investment options and an increase in costs	• Officers are engaging with Fund Managers to understand the position better • Knowledge and Skills Policy in place for Officers and Members of the Committee • Maintain links with central government and national bodies to keep abreast of national issues.	4	3	Medium 12	City Treasurer	June 2016
10	**OPERATIONAL: GOVERNANCE** Failure to comply with legislation leads to ultra vires actions resulting in financial loss and/or reputational damage.	• Officers maintain knowledge of legal framework for routine decisions. • Eversheds retained for consultation on non-routine matters.	2	2	Very Low 4	City Treasurer	June 2016
11	**OPERATIONAL: GOVERNANCE** Committee members do not have appropriate skills or knowledge to discharge their responsibility leading to inappropriate decisions.	• External professional advice is sought where required • Knowledge and skills policy in place (subject to Committee Approval)	3	3	Low 9	City Treasurer	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
12	**OPERATIONAL: GOVERNANCE** Officers do not have appropriate skills and knowledge to perform their roles resulting in the service not being provided in line with best practice and legal requirements. Succession planning is not in place leading to reduction of knowledge when an officer leaves.	• Person specifications are used at recruitment to appoint officers with relevant skills and experience. • Training plans are in place for all officers as part of the performance appraisal arrangements. • Shared service nature of the pensions team provides resilience and sharing of knowledge.	3	3	Low 9	City Treasurer and Acting Director of HR	June 2016
13	**OPERATIONAL: GOVERNANCE** Inadequate, inappropriate or incomplete investment or actuarial advice is actioned leading to a financial loss or breach of legislation.	• At time of appointment ensure advisers have appropriate professional qualifications and quality assurance procedures in place. • Committee and officers scrutinise and challenge advice provided.	2	2	Very Low 4	City Treasurer	June 2016
14	**OPERATIONAL: FUNDING** Failure of an admitted or scheduled body leads to unpaid liabilities being left in the Fund to be met by others.	• Transferee admission bodies required to have bonds in place at time of signing the admission agreement. • Regular monitoring of employers and follow up of expiring bonds.	3	2	Low 6	City Treasurer and Acting Director of HR	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
15	**OPERATIONAL: FUNDING** Ill health costs may exceed “budget” allocations made by the actuary resulting in higher than expected liabilities particularly for smaller employers.	• Review “budgets” at each triennial valuation and challenge actuary as required. • Charge capital cost of ill health retirements to admitted bodies at the time of occurring. • Occupational health services provided by the Council and other large employers to address potential ill health issues early.	3	2	Low 6	City Treasurer and Acting Director of HR	June 2016
16	**OPERATIONAL: FUNDING** Transfers out increase significantly as members transfer to DC funds to access cash through new pension freedoms.	• Monitor numbers and values of transfers out being processed. • If required, commission transfer value report from Fund Actuary for application to Treasury for reduction in transfer values.	2	3	Low 6	City Treasurer and Acting Director of HR	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
17	**OPERATIONAL: ADMINISTRATION** Loss of funds through fraud or misappropriation leading to negative impact on reputation of the Fund as well as financial loss.	• Third parties regulated by the FCA and separation of duties and independent reconciliation procedures in place. • Review of third party internal control reports. • Regular reconciliations of pension payments undertaken by Pensions Finance Team. • Periodic internal audits of Pensions Finance and HR teams.	4	2	Low 8	City Treasurer and Acting Director of HR	June 2016
18	**OPERATIONAL: ADMINISTRATION** Failure of fund manager or other service provider without notice resulting in a period of time without the service being provided or an alternative needing to be quickly identified and put in place.	• Contract monitoring in place with all providers. • Procurement team send alerts whenever credit scoring for any provider changes for follow up action.	3	1	Very Low 3	City Treasurer and Acting Director of HR	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
19	**OPERATIONAL: ADMINISTRATION** Failure of financial system leading to lump sum payments to scheme members and supplier payments not being made and Fund accounting not being possible.	• Contract in place with BT to provide service enabling smooth processing of supplier payments • Process in place for Surrey CC to generate lump sum payments to members as they are due. • Officers undertaking additional testing and reconciliation work to verify accounting transactions	4	4	High 16	City Treasurer	June 2016
20	**OPERATIONAL: ADMINISTRATION** Failure of pension payroll system resulting in pensioners not being paid in a timely manner.	• In the event of a pension payroll failure we would consider submitting the previous months BACS file to pay pensioners a second time if a file could not be recovered by the pension administrators and our software suppliers.	1	5	Very Low 5	Acting Director of HR	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
21	**OPERATIONAL: ADMINISTRATION** Failure to pay pension benefits accurately leading to under or over payments.	• There are occasional circumstances where under or over payments are identified. Where under payments occur arrears are paid as soon as possible usually in the next monthly pension payment. Where an overpayment occurs, the member is contacted and the pension corrected in the next month. Repayment is requested and sometimes we collect this over a number of months.	2	3	Low 6	Acting Director of HR	June 2016
22	**OPERATIONAL: ADMINISTRATION** Failure of pension administration system resulting in loss of records and incorrect pension benefits being paid or delays to payment.	• Pension administration records are stored on the surrey servers they have a disaster recovery system in place and records should be restored within 24 hours of any issue, files are backed up daily.	1	5	Very Low 5	Acting Director of HR	June 2016

Ref	Risk	Mitigating Actions	Residual risk score		Risk Rating	Officer responsible	Review Date
			Likelihood	Impact			
23	**OPERATIONAL: ADMINISTRATION** Administrators do not have sufficient staff or skills to manage the service leading to poor performance and complaints.	• Surrey CC administers pensions for Surrey, East Sussex and is taking on our Triborough partners. They have a number of very experienced administrators two of whom tuped to them from LPFA with our contract. Where issues arise the Pensions Liaison Officer reviews directly with the Pensions Manager at Surrey. More detailed performance reports are being developed.	2	3	Low 6	Acting Director of HR	June 2016
24	**Operational: Administration** BT unable to provide monthly or end of year interface files in a format suitable for Surrey CC to update service records and undertake day to day operations. Inaccuracies in service records held on the pensions administration system may impact on the triennial funding valuation at March 2016 and notifications to starters and leavers.	• Issue has been escalated by the Chief Executive for high level resolution with BT • Test files are currently with SCC • Actuary undertakes data cleansing on the service records and is confident this will mitigate the inaccuracies in service records	4	3	Medium 12	Acting Director of HR	June 2016

This page is intentionally left blank

SRKW
SPECTOR ROSEMAN KODROFF & WILLIS PC

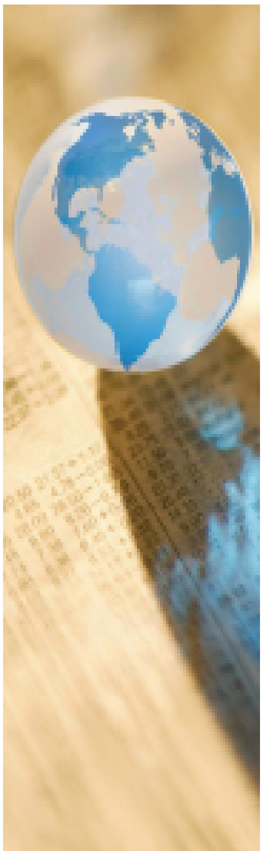
MONITORING REPORT

Fourth Quarter 2015

Prepared For:
CITY OF WESTMINSTER

Contents

- New Investor Actions
- Investor Alert: None
- Eligible – But Not Recommended



New Investor Actions

New Investor Actions
Fourth Quarter 2015

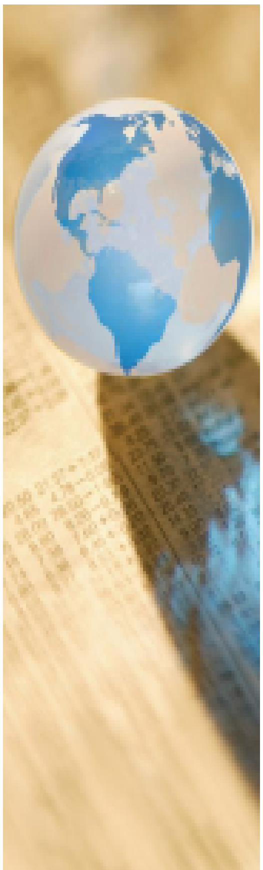
ELIGIBLE

Case Name[1]	Security Identifiers: Symbol	Security Identifiers: ID	Why You Are Eligible	We Recommend[2]	Filing Deadline
Fourth Quarter 2015					
U.S. Shareholder Class Actions					
The City of Westminster is not eligible to play an active role in any of the currently filed actions.					
U.S. Transaction, Derivative and Other Shareholder Actions					
The City of Westminster is not eligible to play an active role in any of the currently filed actions.					
Non-U.S. Shareholder Actions					
Fortis SA/NV (Deminor)[4] *(Netherlands)*	AGGSY AGS AGSb FORSY	BE0003801181 NL0000300038 US34956J3095 US00844W1099	Loss	Take No Action	Dec. 31, 2015
Petróleo Brasileiro S.A. (Securities Arbitration) *(Brazil)*	PETR3 PETR4	P78331132 P78331140 BRPETRACNOR9 BRPETRACNPR6	Loss To Be Determined	Recommendation Pending	Pending
SNS REAAL N.V. *(Netherlands)*	SR	Various	Loss To Be Determined	Recommendation Pending	Pending
Volkswagen AG (AKD Lawyers) *(Netherlands)*	VOW VLKAY VLKPY	Various	Loss To Be Determined	Recommendation Pending	Pending
Volkswagen AG (Bentham) *(Germany)*	VOW	Various	Loss To Be Determined	Recommendation Pending	Pending
Volkswagen AG (Deminor) *(Germany)*	VOW	Various	Loss To Be Determined	Recommendation Pending	Pending
Volkswagen AG (Rotter Rechtsanwaelte) *(Germany)*	VOW	Various	Loss To Be Determined	Recommendation Pending	Pending
Volkswagen AG (TILP & DRRT) *(Germany)*	VOW	Various	Loss To Be Determined	Recommendation Pending	Pending

NOT ELIGIBLE

Case Name[1]	Security Identifiers: Symbol	Security Identifiers: ID	Why You Are Not Eligible[3]	We Recomm.	Filing Deadline
Fourth Quarter 2015					
U.S. Shareholder Class Actions					
Liquid Holdings Group, Inc.	LIQD	53633A101	No Relevant Purchases	N/A	Nov. 20, 2015
Shiloh Industries, Inc.	SHLO	824543102	No Relevant Purchases	N/A	Nov. 20, 2015
LSB Industries, Inc.	LXU	502160104	No Relevant Purchases	N/A	Nov. 24, 2015
Sientra, Inc.	SIEN	82621J105	No Relevant Purchases	N/A	Nov. 24, 2015
Volkswagen AG	VLKAY VLKPY	928662204 928662303 928662402	No Relevant Purchases	N/A	Nov. 24, 2015
QLogic Corporation	QLGC	747277101	No Relevant Purchases	N/A	Nov. 27, 2015
Fifth Street Finance Corp.	FSC	31678A103	No Relevant Purchases	N/A	Nov. 30, 2015
Globus Medical, Inc.	GMED	379577208	No Relevant Purchases	N/A	Nov. 30, 2015
USA Technologies, Inc.	USAT	90328S500	No Relevant Purchases	N/A	Dec. 1, 2015
Amicus Therapeutics, Inc.	FOLD	03152W109	No Relevant Purchases	N/A	Dec. 7, 2015
Cytec Industries Inc.	CYT	232820100	No Relevant Purchases	N/A	Dec. 7, 2015
Hudson City Bancorp, Inc.	HCBK	443683107	No Relevant Purchases	N/A	Dec. 7, 2015
Rentech Nitrogen Partners, L.P.	RNF	760113100	No Relevant Purchases	N/A	Dec. 7, 2015
ChinaCache International Holdings Ltd.	CCIH	16950M107	No Relevant Purchases	N/A	Dec. 8, 2015
6D Global Technologies, Inc.	SIXD	184518209 83002F100	No Relevant Purchases	N/A	Dec. 14, 2015
Bofl Holding, Inc.	BOFI	05566U108	No Relevant Purchases	N/A	Dec. 14, 2015
Nobilis Health Corp.	HLTH	65500B103	No Relevant Purchases	N/A	Dec. 21, 2015
Valeant Pharmaceuticals International	VRX	91911K102	No Relevant Purchases	N/A	Dec. 21, 2015
Zafgen, Inc.	ZFGN	98885E103	No Relevant Purchases	N/A	Dec. 21, 2015
Extreme Networks, Inc.	EXTR	30226D106	No Relevant Purchases	N/A	Dec. 22, 2015
American Realty Capital Properties, Inc.	ARCP	02917T104 02917T401	No Relevant Purchases	N/A	Dec. 28, 2015
Cytec Industries Inc.	CYT	232820100	No Relevant Purchases	N/A	Dec. 28, 2015
GNC Holdings, Inc.	GNC	36191G107	No Relevant Purchases	N/A	Dec. 28, 2015
TerraForm Global, Inc.	GLBL	88104M101	No Relevant Purchases	N/A	Dec. 28, 2015
TICC Capital Corp.	TICC	87244T109	No Relevant Purchases	N/A	Dec. 28, 2015

Spector Roseman Kodroff & Willis



New Investor Actions

NOT ELIGIBLE

Case Name[1]	Security Identifiers: Symbol	Security Identifiers: ID	Why You Are Not Eligible[2]	We Recomm.	Filing Deadline
Fourth Quarter 2015					
SouFun Holdings Limited	SFUN	836034108	No Relevant Purchases	N/A	Dec. 29, 2015
Spectrum Pharmaceuticals, Inc.	SPPI	84763A108	No Relevant Purchases	N/A	Jan. 4, 2016
VimpelCom, Ltd.	VIP	92719A106	No Relevant Purchases	N/A	Jan. 4, 2016
Starz	STRZA STRZB	85571Q102 85571Q201	No Relevant Purchases	N/A	Jan. 8, 2016
Premiere Global Services, Inc.	PGI	740585104	No Relevant Purchases	N/A	Jan. 9, 2016
Checkpoint Systems, Inc.	CKP	162825103	No Relevant Purchases	N/A	Jan. 11, 2016
Flotek Industries, Inc.	FTK	343389102	No Relevant Purchases	N/A	Jan. 11, 2016
TCP International Holdings Ltd.	TCPI	H84689100	No Relevant Purchases	N/A	Jan. 11, 2016
Eros International Plc	EROS	G3788M114	No Relevant Purchases	N/A	Jan. 12, 2016
New Source Energy Partners LP	NSLP	64881E307	No Relevant Purchases	N/A	Jan. 12, 2016
Straight Path Communications, Inc.	STRP	862578101	No Relevant Purchases	N/A	Jan. 12, 2016
Capstone Turbine Corporation	CPST	14067D102 14067D409	No Relevant Purchases	N/A	Jan. 15, 2016
Marchex, Inc.	MCHX	56624R108	No Relevant Purchases	N/A	Jan. 18, 2016
Roadrunner Transportation Systems, Inc.	RRTS	76973Q105	No Relevant Purchases	N/A	Jan. 18, 2016
Clovis Oncology, Inc.	CLVS	189464100	No Relevant Purchases	N/A	Jan. 19, 2016
Party City Holdco Inc.	PRTY	702149105	No Relevant Purchases	N/A	Jan. 19, 2016
TECO Energy, Inc.	TE	872375100	No Relevant Purchases	N/A	Jan. 19, 2016
Osiris Therapeutics, Inc.	OSIR	68827R108	No Relevant Purchases	N/A	Jan. 22, 2016
ERBA Diagnostics, Inc.	ERB	29490B101	No Relevant Purchases	N/A	Feb. 1, 2016
SunEdison, Inc.	SUNE	86732Y109	No Relevant Purchases	N/A	Feb. 1, 2016
Vital Therapies, Inc.	VTL	92847R104	No Relevant Purchases	N/A	Feb. 1, 2016
XBiotech Inc.	XBIT	98400H102	No Relevant Purchases	N/A	Feb. 1, 2016
Sientra, Inc.	SIEN	82621J105	No Relevant Purchases	N/A	Feb. 2, 2016
Avalanche Biotechnologies, Inc.	AAVL	05337G107	No Relevant Purchases	N/A	Feb. 5, 2016
Identiv, Inc.	INVE	45170X106 45170X205	No Relevant Purchases	N/A	Feb. 5, 2016
OvaScience, Inc.	OVAS	69014Q101	No Relevant Purchases	N/A	Feb. 5, 2016
Vale S.A.	VALE	91912E105	No Relevant Purchases	N/A	Feb. 5, 2016
SuperCom Ltd.	SPCB	M87095119	No Relevant Purchases	N/A	Feb. 7, 2016
Dole Food Company, Inc.	DOLE	256603101	No Relevant Purchases	N/A	Feb. 8, 2016
AGL Resources, Inc.	GAS	001204106	No Relevant Purchases	N/A	N/A
Alibaba Group Holding Limited	BABA	01609W102 US01609W1027	No Relevant Purchases	N/A	N/A
Citibank N.A. (Residential Mortgage Backed Securities)	No Symbol	Various	No Relevant Purchases	N/A	N/A
U.S. Transaction, Derivative and Other Shareholder Actions					
Atmel Corp. *(Transaction Action)*	ATML	049513104	No Relevant Purchases	N/A	N/A
Astoria Financial Corporation *(Transaction Action)*	AF	046265104	No Relevant Purchases	N/A	N/A
Cablevision Systems Corporation *(Transaction Action)*	CVC	12686C109	No Relevant Purchases	N/A	N/A
Cameron International Corporation *(Transaction Action)*	CAM	13342B105	No Relevant Purchases	N/A	N/A
Campus Crest Communities, Inc. *(Transaction Action)*	CCG	13466Y105	No Relevant Purchases	N/A	N/A
Chambers Street Properties *(Transaction Action)*	CSG	157842105	No Relevant Purchases	N/A	N/A
Con-way Inc. *(Transaction Action)*	CNW	205944101	No Relevant Purchases	N/A	N/A
Cytec Industries Inc. *(Transaction Action)*	CYT	232820100	No Relevant Purchases	N/A	N/A
Diamond Foods, Inc. *(Transaction Action)*	DMND	252603105	No Relevant Purchases	N/A	N/A
Dyax Corp. *(Transaction Action)*	DYAX	26746E103	No Relevant Purchases	N/A	N/A
EMC Corporation *(Transaction Action)*	EMC	268648102	No Relevant Purchases	N/A	N/A
Envivio, Inc. *(Transaction Action)*	ENVI	29413T106	No Relevant Purchases	N/A	N/A

SRKW
Spector Roseman Kodroff & Willis

New Investor Actions

SRKW
Spector Roseman Kodroff & Willis

NOT ELIGIBLE

Case Name[1]	Security Identifiers		Why You Are Not Eligible[2]	We Recomm.	Filing Deadline
	Symbol	ID			
Eureka Financial Corp. *(Transaction Action)*	EKFC	29855C108	No Relevant Purchases	N/A	N/A
First Niagara Financial Group, Inc. *(Transaction Action)*	FNFG	33582V108	No Relevant Purchases	N/A	N/A
Furmanite Corporation *(Transaction Action)*	FRM	361086101	No Relevant Purchases	N/A	N/A
FX Energy, Inc. *(Transaction Action)*	FXEN	302695101	No Relevant Purchases	N/A	N/A
Good Technology Corporation *(Transaction Action)*	GDTC	382129104	No Relevant Purchases	N/A	N/A
Hubbell Incorporated *(Transaction Action)*	HUB.B	443510201	No Relevant Purchases	N/A	N/A
Hutchinson Technology Inc. *(Transaction Action)*	HTCH	448407106	No Relevant Purchases	N/A	N/A
Iron Mountain Incorporated *(Transaction Action)*	IRM	46284V101	No Relevant Purchases	N/A	N/A
Jacksonville Bancorp, Inc. *(Transaction Action)*	JAXB	469249205	No Relevant Purchases	N/A	N/A
KLA-Tencor Corp. *(Transaction Action)*	KLAC	482480100	No Relevant Purchases	N/A	N/A
Liberator Medical Holdings, Inc. *(Transaction Action)*	LBMH	53012L108	No Relevant Purchases	N/A	N/A
Meredith Corporation *(Transaction Action)*	MDP	589433101	No Relevant Purchases	N/A	N/A
Ocata Therapeutics, Inc. *(Transaction Action)*	OCAT	67457L100	No Relevant Purchases	N/A	N/A
Plum Creek Timber Company, Inc. *(Transaction Action)*	PCL	729251108	No Relevant Purchases	N/A	N/A
PMC-Sierra, Inc. *(Transaction Action)*	PMCS	69344F106	No Relevant Purchases	N/A	N/A
Rentrak Corporation *(Transaction Action)*	RENT	760174102	No Relevant Purchases	N/A	N/A
Rite Aid Corp. *(Transaction Action)*	RAD	767754104	No Relevant Purchases	N/A	N/A
Rockwell Medical, Inc. *(Derivative Action)*	RMTI	774374102	No Relevant Purchases	N/A	N/A
SanDisk Corp. *(Transaction Action)*	SNDK	80004C101	No Relevant Purchases	N/A	N/A
Security California Bancorp *(Transaction Action)*	SCAF	81412M103	No Relevant Purchases	N/A	N/A
Sirona Dental Systems, Inc. *(Transaction Action)*	SIRO	82966C103	No Relevant Purchases	N/A	N/A
SmartPros Ltd. *(Transaction Action)*	SPRO	83171G103	No Relevant Purchases	N/A	N/A
Solera Holdings, Inc. *(Transaction Action)*	SLH	83421A104	No Relevant Purchases	N/A	N/A
Southcoast Financial Corporation *(Transaction Action)*	SOCB	84129R100	No Relevant Purchases	N/A	N/A
Strategic Hotels & Resorts, Inc. *(Transaction Action)*	BEE	86272T106	No Relevant Purchases	N/A	N/A
Synergetics USA Inc. *(Transaction Action)*	SURG	87160G107	No Relevant Purchases	N/A	N/A
TC PipeLines, LP *(Transaction Action)*	TCP	87233Q108	No Relevant Purchases	N/A	N/A
The Pep Boys - Manny, Moe & Jack *(Transaction Action)*	PBY	713278109	No Relevant Purchases	N/A	N/A
The Phoenix Companies, Inc. *(Transaction Action)*	PNX	71902E604	No Relevant Purchases	N/A	N/A
TriVascular Technologies, Inc. *(Transaction Action)*	TRIV	89685A102	No Relevant Purchases	N/A	N/A
United Capital Corp. *(Transaction Action)*	UCAP	909912107	No Relevant Purchases	N/A	N/A
Wausau Paper Corp. *(Transaction Action)*	WPP	943315101	No Relevant Purchases	N/A	N/A
VAALCO Energy, Inc. *(Transaction Action)*	EGY	91851C201	No Relevant Purchases	N/A	N/A
Non-U.S. Shareholder Actions					
Aurona Industries Inc. *(Taiwan)*	8074:TW	Y0453T101 TW0008074008	No Relevant Purchases	N/A	Pending
Coland Holdings Ltd. *(Taiwan)*	4144:TW	KYG2379A1094	No Relevant Purchases	N/A	Pending
Eagle Cold Storage Enterprise Co Ltd. *(Taiwan)*	8905:TW	TW0008905001	No Relevant Purchases	N/A	Pending
FX Hotels Group Inc. *(Taiwan)*	2724:TW	G3704Y101 KYG3704Y1017	No Relevant Purchases	N/A	Pending
FX Instruments *(Canada)*	No Symbol	N/A	No Relevant Purchases	N/A	Pending
IOOF Holdings Limited *(Australia)*	IFL	Q49809108 AU000000IFL2	No Relevant Purchases	N/A	Pending

Case Name[1]	Security Identifiers Symbol	ID	Why You Are Not Eligible[3]	We Recomm.	Filing Deadline
Jetway Information Co. Ltd. (Taiwan)	6161.TW	Y4433N105 TW0006161003 TW000P006006	No Relevant Purchases	N/A	Pending
OW Bunker A/S (Bruun & Hjejle) (Denmark)	OW OW.CO	K7682O107 DK0060548386	No Relevant Purchases	N/A	Pending
Quindell Plc (United Kingdom)	QPP	GB00B0RETG60 GB00BMTS9H6	No Relevant Purchases	N/A	Pending
Sandhurst Trustees Limited (Wickham Securities) (Australia)	No Symbol	N/A	No Relevant Purchases	N/A	Pending
Slater & Gordon Ltd. (ACA) (Australia)	SGH	Q8510C101 AU000000SGH7	No Relevant Purchases	N/A	Pending
Slater & Gordon Ltd. (Maurice Blackburn) (Australia)	SGH	Q8510C101 AU000000SGH7	No Relevant Purchases	N/A	Pending
Valeant Pharmaceuticals International, Inc. (Canada)	VRX	91911K102	No Relevant Purchases	N/A	Pending
Wei Mon Industry Co. Ltd. (Taiwan)	8925.TW	6222671 TW0008925009	No Relevant Purchases	N/A	Pending

NOT ELIGIBLE

Notes		
1	Case Name	All actions listed in the "Case Name" column are U.S. securities class actions, unless otherwise noted.
2	Consider Action	We recommend your fund play an active role, either as a lead plaintiff in the class action, opting out of the class, or otherwise. This recommendation is based on our view that the action is meritorious, your fund's losses are sufficiently large to justify playing an active role (for class and opt out actions), the action meets our other relevant criteria, and yours. For actions in this category, we include a detailed Investor Alert, explaining the basis of our recommendation.
	Take No Action	Although your fund is eligible to play an active role, we recommend that it does not. In the "Eligible Cases Not Recommended" we explain why your fund should not play an active role (e.g., the case at present may not be sufficiently meritorious; your fund's losses are not likely large enough; or your stated criteria for activism are not met).
3	No Relevant Purchases	Your fund is ineligible to participate as it did not purchase the relevant securities during the stated class or time period (or its losses are below our $20,000 threshold). If, because the relevant time period is later expanded, your fund becomes eligible to participate at the settlement stage, we will alert you to help ensure it shares in these proceeds.
	Gain	If your fund experienced a gain in a particular security during the relevant period, it is ineligible to participate.
4	*Limited Data*	We have insufficient data from your custodian. Without complete data covering the relevant period we cannot perform a proper damage analysis to determine your fund's eligibility to participate.
5	*New Non-U.S. Action*	We've identified this non-U.S. action as part of our global portfolio monitoring service. The action is currently being organized and we are in the process of obtaining the relevant documents and information in order to recommend a course of action to you. When we have sufficient information to make such a recommendation, we will advise you.
6	Canadian *Action*	As part of our global portfolio monitoring service we've identified that you may be eligible to join this Canadian action. In Canada, institutional investors generally do not act as lead plaintiffs, both by practice and based on judicial determinations. Instead, retail investors tend to lead Canadian class actions (which is the opposite of U.S. practice). Therefore, when you are eligible to join a Canadian action, we will generally recommend that you do not play a lead or active role and will omit including these actions in our Eligible But Not Recommended section.
7	*Non-U.S. Action (Nominal Loss)*	We've identified this non-U.S. action as part of our global portfolio monitoring service. While you are eligible to join the action because you suffered a loss, we did not feel the likely recovery, after fees and expenses are deducted, warranted a recommendation to join the action. That said, if you would like to move forward, please let us know as we will gladly undertake the registration formalities on your behalf.

New Investor Actions

S R K W
SPECTOR ROSEMAN KODROFF & WILLIS

Eligible – But Not Recommended

Fourth Quarter 2015

Case Name	Security Identifiers Symbol	Security Identifiers ID	Why You Are Eligible	We Recommend	Filing Deadline
Fortis SA/NV (Deminor)[a] (Netherlands)	AGESY AGS AGSb FORSY	BE0003801181 NL0000200836 US34956J3095 US00844W1099	Loss	Take No Action	Dec 31, 2015

Company: Fortis SA/NV ("Fortis") ranked among Europe's largest financial groups with core activities in banking and insurance and total assets of €871 billion (as of 31 December 2007). The company's activities were mainly located in the Benelux region where the group presented itself as the leader in financial services.

Allegations: Defendants misrepresented that Fortis was relatively immune from the effects of the global credit crisis, that its capital position remained strong, and that its exposure to the subprime market was minimal. In addition, defendants failed to disclose the adverse effects that Fortis was experiencing as a result of its acquisition of the assets of ABN-AMRO Holding NV and its affiliates (collectively, "ABN AMRO") (the "Acquisition"). Ultimately, the market became concerned about the effect the Acquisition would have on the company's liquidity. Yet, Fortis downplayed those concerns by consistently reassuring the market and confirming its "sound capital and solvency position and unchanged dividend policy." By June 26, 2008, the market again became concerned about the company's liquidity. At this time, Fortis initiated a dilutive €1.5 billion capital increase at €10 per share (a 20% discount). The company also disclosed an "acceleration" of the execution of its solvency plan which included the decision not to pay an interim dividend in 2008 and to pay the full-year 2008 dividend in shares. On this news, the price of the company's shares lost 19% in value. Then, on October 5, 2008, Fortis was dismantled by the Dutch and Belgian governments. The company's Dutch bank and insurance activities were nationalized by the Dutch government while the remaining stake in Fortis Bank Belgium was transferred to the Belgian government which subsequently sold a 75% stake to BNP Paribas. On this news, trading in the company's shares was suspended and did not resume until October 14, 2008 when the share price closed at €1.22 – having lost 80% of its market value.

Recommendation: We believe the claims asserted in this Dutch action are strong and meritorious. This action, which is being organized by Deminor, is related to the Belgian action that Deminor launched several years ago. Following the launch of their Belgian action, Deminor received inquiries from many investors that wanted to join the Belgian action but were simply too late. In response to this investor interest, and in light of recent changes in Dutch law, Deminor is now organizing an action in the Netherlands for those investors that were unable to join their Belgian action. Because City of Westminster previously registered for Deminor's Belgian action, there is no need for it to join this Dutch action as its interests are already protected. In light of the foregoing, there is no need for City of Westminster to take any action with respect to the Dutch action.

E L I G I B L E

Eligible
But Not
Recommended

SRKW
Spector Roseman Kodroff & Willis

This page is intentionally left blank

Appendix 3: CASHFLOW MONITORING

Cashflow actuals and forecast for period April 2015 to March 2016

	Apr-15	May-15	Jun-15	Jul-15	Aug-15			Sep-15			Oct-15		
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
	Actual	Actual	Actual	Actual	F'cast	Actual	Var	F'cast	Actual	Var	F'cast	Actual	Var
Balance b/f	**1,995**	**3,583**	**1,520**	**9,045**	**7,615**	**7,615**	**0**	**6,025**	**6,008**	**17**	**8,225**	**9,337**	**(1,112)**
			[4]						[5]				
Contributions	1,066	2,178	10,927	2,621	2,600	2,385	215	9,800	10,127	(327)	1,400	2,782	(1,382)
Misc. Receipts[1]	73	41	112	611	100	8	92	100	79	21	100	215	(115)
Pensions	(2,852)	(2,883)	(2,877)	(2,874)	(2,900)	(2,922)	22	(2,900)	(2,901)	1	(2,900)	(2,890)	(10)
HMRC Tax	(506)	(526)	0	(537)	(540)	(511)	(29)	(540)	0	(540)	(540)	0	(540)
Misc. Payments[2]	(1,193)	(873)	(621)	(713)	(800)	(411)	(389)	(800)	(440)	(360)	(800)	(832)	32
Expenses[3]	0	0	(16)	(538)	(50)	(156)	106	(3,460)	(3,536)	76	(50)	(48)	(2)
Net cash in/(out) in month	(3,412)	(2,063)	7,525	(1,430)	(1,590)	(1,607)	17	2,200	3,329	(1,129)	(2,790)	(773)	(2,017)
Withdrawals from Fund Managers	5,000	0	0	0	0	0	0	0	0	0	0	0	0
Balance c/f	**3,583**	**1,520**	**9,045**	**7,615**	**6,025**	**6,008**	**17**	**8,225**	**9,337**	**(1,112)**	**5,435**	**8,564**	**(3,129)**

	Nov-15			Dec-15			Jan-16			Feb-16			Mar-16
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
	F'cast	Actual	Var	F'cast	Actual	Var	F'cast	Actual	Var	F'cast	Actual	Var	F'cast
Balance b/f	**8,481**	**8,564**	**(83)**	**5,463**	**6,980**	**(1,517)**	**23,873**	**12,167**	**11,706**	**8,833**	**9,948**	**(1,115)**	**8,523**
						[6]							
Contributions	2,600	2,510	90	2,600	(10,212)	12,812	(10,850)	2,948	(13,798)	2,600	2,386	214	4,100
Misc. Receipts[1]	100	17	83	100	12	88	100	259	(159)	100	959	(859)	100
Pensions	(2,900)	(2,960)	60	(2,900)	(2,904)	4	(2,900)	(2,909)	9	(2,900)	(2,901)	1	(2,900)
HMRC Tax	(2,128)	(522)	(1,606)	(540)	(546)	6	(540)	(2,116)	1,576	(540)	(536)	(4)	(540)
Misc. Payments[2]	(800)	(629)	(171)	(800)	(1,590) [7]	790	(800)	(969) [8]	169	(800)	(760)	(40)	(800) [9]
Expenses[3]	110	0	110	(50)	427	(477)	(50)	568	(618)	(550)	(573)	23	(753)
Net cash in/(out) in month	(3,018)	(1,584)	(1,434)	(1,590)	(14,813)	13,223	(15,040)	(2,219)	(12,821)	(2,090)	(1,425)	(665)	(793)
Withdrawals from Fund Managers	0	0	0	20,000	20,000	0	0	0	0	0	0	0	0
Balance c/f	**5,463**	**6,980**	**(1,517)**	**23,873**	**12,167**	**11,706**	**8,833**	**9,948**	**(1,115)**	**6,743**	**8,523**	**(1,780)**	**7,730**

Notes

[1] Includes Transfers in, Overpayments, Bank Interest, VAT reclaim, Recharges
[2] Includes Transfers out, Lump Sums, Death Grants, Refunds
[3] Payment of invoices impacted by the transition to the Council's new financial system on 1st April 2015
[4] Includes £6.25 million deficit payment from Westminster City Council
[5] Includes WCC upfront employer contributions of £7.2 million (equivalent of £1.2m per month)
[6] Includes repayment of £13.45m contributions to WCC
[7] Includes £725k refund of VAT from Majedie
[8] Includes £580k VAT reimbursement
[9] Includes £715k VAT due to HMRC

Cashflow actuals and forecast for period April 2016 to March 2017 and the following 3 financial years

	Apr-16	May-16	Jun-16	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast	F'cast
Balance b/f	**7,730**	**6,240**	**6,450**	**6,860**	**7,270**	**7,480**	**4,890**	**5,300**	**5,510**	**5,920**	**6,330**	**6,540**
Contributions	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800
Misc. Receipts[1]	100	100	100	100	100	100	100	100	100	100	100	100
Pensions	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)
HMRC Tax	(540)	(540)	(540)	(540)	(540)	(540)	(540)	(540)	(540)	(540)	(540)	(540)
Misc. Payments[2]	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)
Expenses[3]	(50)	(550)	(50)	(50)	(550)	(3,050)	(50)	(550)	(50)	(50)	(550)	(50)
Net cash in/(out) in month	(1,490)	(1,990)	(1,490)	(1,490)	(1,990)	(4,490)	(1,490)	(1,990)	(1,490)	(1,490)	(1,990)	(1,490)
Withdrawals from Fund Managers		2,200	1,900	1,900	2,200	1,900	1,900	2,200	1,900	1,900	2,200	1,900
Balance c/f	**6,240**	**6,450**	**6,860**	**7,270**	**7,480**	**4,890**	**5,300**	**5,510**	**5,920**	**6,330**	**6,540**	**6,950**

2017/18	2018/19	2019/20
£000	£000	£000
F'cast	F'cast	F'cast
6,950	**6,150**	**4,850**
35,000	37,000	39,000
1,200	1,300	1,400
(38,000)	(40,000)	(42,000)
(7,000)	(7,500)	(8,000)
(10,000)	(12,000)	(14,000)
(6,000)	(6,500)	(7,000)
(24,800)	(27,700)	(30,600)
24,000	26,400	28,800
6,150	**4,850**	**3,050**

This page is intentionally left blank

City of Westminster

Committee Report

Decision Maker:	**PENSION FUND COMMITTEE**
Date:	**22 March 2016**
Classification:	**General Release**
Title:	**External Audit Plan for City of Westminster Pension Fund 2015-16**
Wards Affected:	**All**
Policy Context:	**Effective control over Council Activities**
Financial Summary:	**There are no financial implications arising from this report.**
Report of:	**Steven Mair** ***City Treasurer*** **smair@westminster.gov.uk** **020 7641 2904**

1. Executive Summary

1.1 This report presents the external audit plan for the pension fund for 2015-16.

2. Recommendation

2.1 The Committee note the contents of this paper.

If you have any questions about this report, or wish to inspect one of the background papers, please contact the report author:

Nikki Parsons nparsons@westminster.gov.uk or 020 7641 6925

BACKGROUND PAPERS: None

APPENDICES:

Appendix 1 – Grant Thornton - Annual Audit plan for City of Westminster Pension Fund 2015-16

This page is intentionally left blank

The Audit Plan
for the City of Westminster Pension Fund

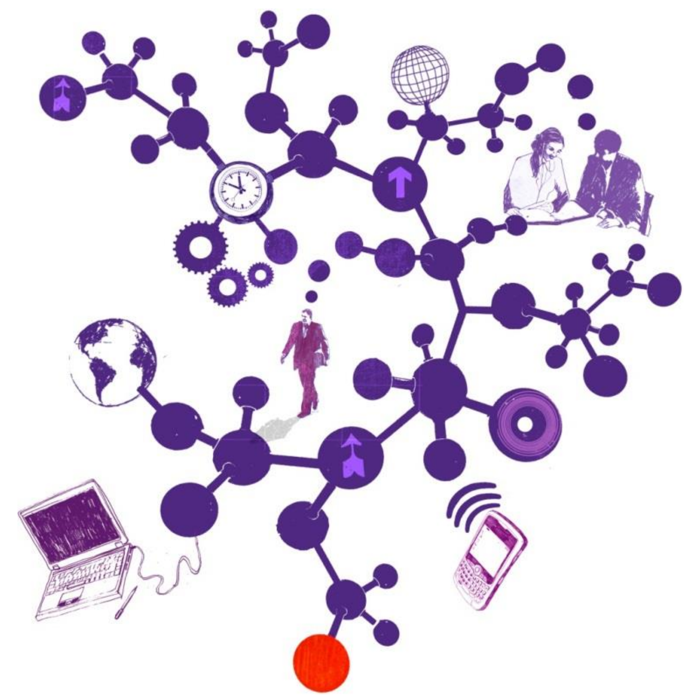
Year ending 31 March 2016

March 2016

Elizabeth olive
Engagement Lead
T 020 7728 3329
E elizabeth.l.olive@uk.gt.com

Geoffrey Banister
Engagement Manager
T 020 7728 3023
E geoffrey.c.banister@uk.gt.com

Dale Connelly
In-charge auditor
T 020 7383 5100
E dale.s.connelly@uk.gt.com



Grant Thornton UK LLP
Grant Thornton House
Melton Street
London NW1 2EP

T +44 (0)20 7383 5100

www.grant-thornton.co.uk

City of Westminster Pension Fund
Westminster City Hall
64 Victoria Street
LONDON
SW1E 6QP

22 March 2016

Dear Members of the Pension Fund Committee

Audit Plan for City of Westminster Pension Fund for the year ending 31 March 2016

This Audit Plan sets out for the benefit of those charged with governance (in the case of City of Westminster Pension Fund, the Audit & Performance Committee), an overview of the planned scope and timing of the audit, as required by International Standard on Auditing (UK & Ireland) 260. This document is to help you understand the consequences of our work, discuss issues of risk and the concept of materiality with us, and identify any areas where you may request us to undertake additional procedures. It also helps us gain a better understanding of the Pension Fund and your environment. The contents of the Plan have been discussed with management.

We are required to perform our audit in line with the Local Audit and Accountability Act 2014 and in accordance with the Code of Practice issued by the National Audit Office (NAO) on behalf of the Comptroller and Auditor General in April 2015.

Our responsibilities under the Code are to:

- give an opinion on the Fund's financial statements
- give an opinion on the Pension Fund Annual Report.

As auditors we are responsible for performing the audit, in accordance with International Standards on Auditing (UK & Ireland), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

Yours sincerely

Elizabeth Olive

Engagement Lead

Contents

Understanding your business

In planning our audit we need to understand the challenges and opportunities the Pension Fund is facing. We set out a summary of our understanding below.

Challenges/opportunities

1. Pooling of Investments

- As part of the summer budget 2015 the government has invited LGPS administering authorities to submit proposals for investing their assets through pools of at least £25 billion, with the intention of reducing investment management costs and potentially improving returns.
- The government anticipates that this will improve both capacity and capability to invest in large scale infrastructure projects.
- Initial proposals were to be submitted to DCLG by mid February, with final plans agreed by 15 July 2016.

2. Changes to the investment regulations

- In November 2015 DCLG published draft proposals in relation to the investment regulations governing LGPS funds.
- The proposals seek to remove some of the existing prescribed means of securing a diversified investment strategy and instead give funds greater responsibility to determine the balance of their investments and take account of risk.

3. Governance arrangements

- Local pension boards have been in place since April 2015, and were introduced to assist with compliance and effective governance and administration of the scheme.
- There remains a continued focus on the affordability, cost and management of the scheme, and as such it remains critical that appropriate governance arrangements are in place for the fund.

4. Local Government Outsourcing

- As many Council's look to outsourcing and the set up of external companies as a more cost effective way to provide services, the impact on the LGPS fund needs to be considered.
- Funds need to carefully consider requests for admission to the scheme and where possible mitigate any risks to the fund.
- An increased number of admitted bodies may increase the risks for the fund in the event of those bodies failing. it is also likely to increase the administration costs of the scheme overall.

Our response

1. Pooling of Investments

- We will continue to discuss with officers their plans for asset pooling in the London CIV and the implications that this will have on both the investment policy and governance arrangements of the fund.

2. Changes to the investment regulations

- We will discuss with officers their plans to respond to these changes and consider the impact on the fund's investment strategy and its risk management approach to investments.

3. Governance arrangements

- We will continue our on-going dialogue with officers around their governance arrangements, particularly in light of their proposals for pooling investments.
- We will continue to share emerging good practice with officers.

4. Local Government Outsourcing

- Through our regular liaison with officers we will consider the impact of any planned large scale TUPE transfers of staff and the effect on the fund.

Developments and other requirements relevant to your audit

In planning our audit we also consider the impact of key developments in the sector and take account of national audit requirements as set out in the Code of Audit Practice and associated guidance.

Developments and other requirements

1. Financial Pressures

- There is increasing pressure on pension funds to have an investment strategy that pays benefits and this may lead to disinvestment decisions from investment assets. There is a need to fund cash flow demands on benefit and leaver payments that are not covered by contributions and investment income as the fund matures and there are fewer active contributors.
- Pension fund investment strategies need to be able to respond to these demands as well as the changing nature of the investment markets

2. Financial Reporting

- There are no significant changes to the Pension Fund financial reporting framework as set out in the CIPFA Code of Practice for Local Authority Accounting (the Code) for the year ending 31 March 2016, however the Pension Fund needs to ensure on going compliance with the Code.

3. LGPS 2014

- Funds have implemented the requirements of LGPS 2014 and moved to a career average scheme.
- This will continue to increase the complexity of the benefit calculations and the arrangements needed to ensure the correct payment of contributions.
- In addition, this places greater emphasis on the employer providing detailed information to the scheme administrator, while also requiring the scheme to have enhanced information systems In place to maintain and report on this data.

4. Accounting for Fund management costs

- There continues to be a spotlight on the costs of managing the LGPS, and in particular investment management costs.
- CIPFA produced guidance in 2014 aimed at improving the transparency of management cost data. This suggested that funds should include a note to the accounts with a breakdown of management costs that they are contractually liable for across the areas of investment management expenses, administration expenses and oversight and governance costs.
- This guidance is currently being updated.

Our response

1. Financial Pressures

- We will monitor any changes to the Pension Fund investment strategy through our regular meetings with management.
- We will consider the impact of changes on the nature of investments held by the Pension Fund and adjust our testing strategy as appropriate.

2. Financial Reporting

- We will ensure that the Pension Fund financial statements materially comply with the requirements of the Code through our substantive testing.

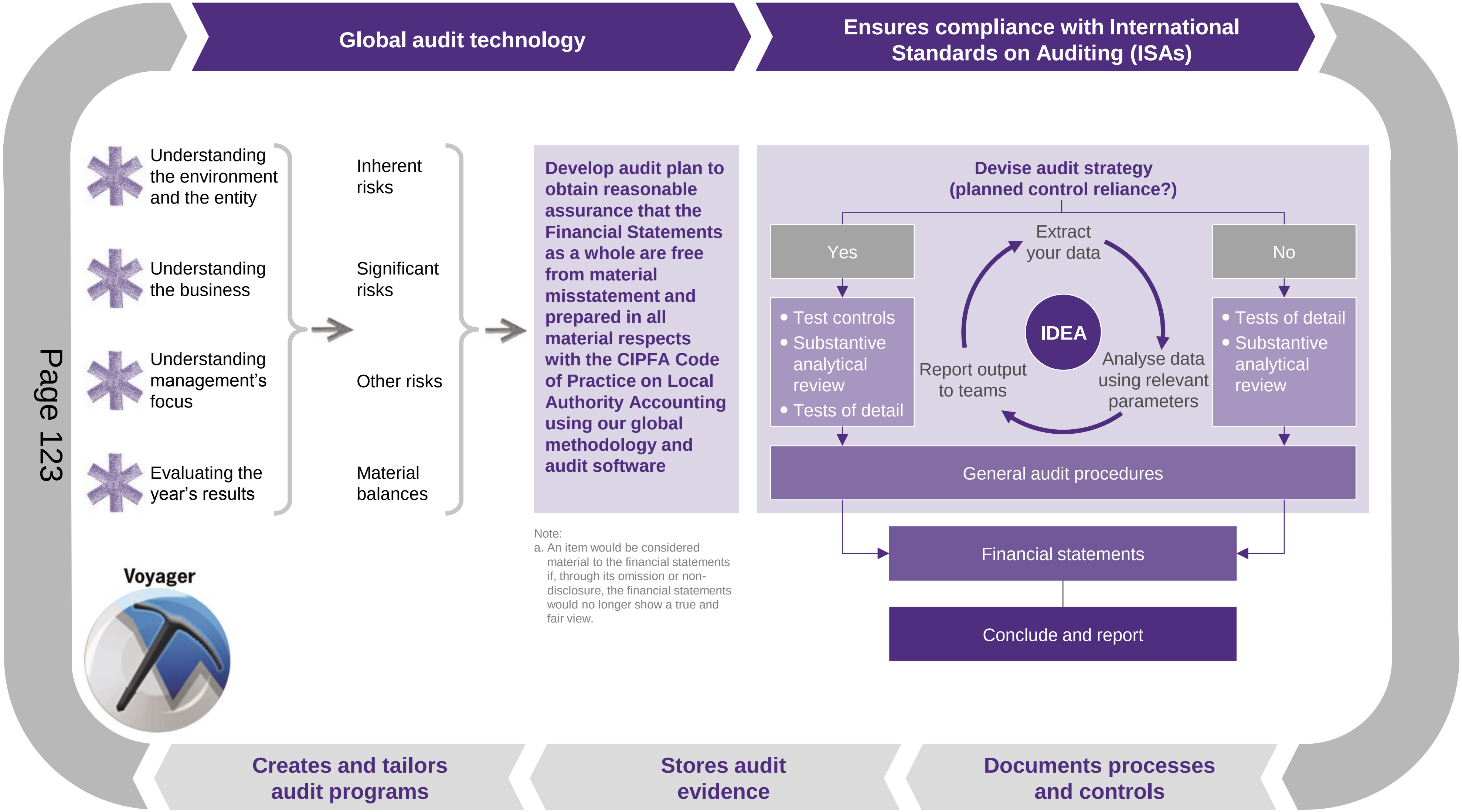
3. LGPS 2014

- We will continue to review the arrangements that the fund has in place for the quality of its' membership data.

4. Accounting for Fund management costs

- We will continue to discuss with officers their plans for increasing the level of transparency associated with the costs of managing the fund.

Our audit approach



Page 123

Materiality

In performing our audit, we apply the concept of materiality, following the requirements of International Standard on Auditing (UK & Ireland) (ISA) 320: Materiality in planning and performing an audit.

The standard states that 'misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements'.

As is usual in pension schemes, we have determined materiality for the statements as a whole as a proportion of net assets for the fund. For purposes of planning the audit, we have determined overall materiality in the context of a reader of the whole statement of accounts to be £9,891k (being 0.9% of net assets). We will consider whether this level is appropriate during the course of the audit and will advise you if we revise this. Our reason for selecting this level of materiality is based on the risks associated with the new financial ledger system which was implemented from 1 April 2015 under the Managed Services programme. This programme has resulted in significant risk to the Council and impacts on the Pension Fund as the journals processed during the year and for accounts preparation are through the system.

Under ISA 450, auditors also set an amount below which misstatements would be clearly trivial in the context of a reader of the whole statement of accounts and would not need to be accumulated or reported to those charged with governance because we would not expect that the accumulation of such amounts would have a material effect on the financial statements. "Trivial" matters are clearly inconsequential, whether taken individually or in aggregate and whether judged by any criteria of size, nature or circumstances. We have defined the amount below which misstatements would be clearly trivial to be £494k.

ISA 320 also requires auditors to determine separate, lower, materiality levels where there are 'particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users'.

We have not identified any items where separate materiality levels are appropriate.

Significant risks identified

"Significant risks often relate to significant non-routine transactions and judgmental matters. Non-routine transactions are transactions that are unusual, either due to size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty" (ISA 315). In this section we outline the significant risks of material misstatement which we have identified. There are two presumed significant risks which are applicable to all audits under auditing standards (International Standards on Auditing - ISAs) which are listed below:

Significant risk	Description	Substantive audit procedures
The revenue cycle includes fraudulent transactions	Under ISA 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue. This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.	Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Westminster City Council Pension Fund, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: • There is little incentive to manipulate revenue recognition • Opportunities to manipulate revenue recognition are very limited • The culture and ethical frameworks of local authorities, including Westminster City Council who act as the administrators of the pension fund, mean that all forms of fraud are seen as unacceptable • The split of responsibilities between the Authority, the Custodian and its Fund Managers provide a very strong separation of duties reducing the risk around investment income • Transfers into the scheme are all supported by an independent actuarial valuation of the amount which should be transferred and which is subject to agreement between the transferring and receiving funds.
Management over-ride of controls	Under ISA 240 it is presumed that the risk of management over-ride of controls is present in all entities.	**Work planned:** • Review of accounting estimates, judgments and decisions made by management • Testing of journal entries • Review of unusual significant transactions

Significant risks identified (continued)

Significant risk	Description	Substantive audit procedures
Managed services partnership (*risk of incomplete transfer of data from the old system to the new system*)	The tri-borough councils implemented a new financial ledger through a managed services partnership with BT from 1 April 2015. There have been a number of difficulties with the implementation which give rise to a significant risk of completeness of the balances in the financial statements, including: • Reconciliations are not carried out timely and there are a large number of unreconciled items in the income and cash balances • Expenditure payments are not being made correctly • Some income received by the council is unallocated and being held in a suspense account • Payroll information is not up to date and not all employees are being routinely paid The Council is proactively managing the service problems and is in regular contact with BT, including finance officers visiting the BT office on a monthly basis. Improvements are being made in the transactional processing every month but there remains a risk to the audit opinion.	**Work completed to date:** • We have gained an understanding of the Council's relationship with the managed service provider, including the position as at December 2015 for the service issues currently being faced in delivering the expected contractual commitments for the council • Review of the testing carried out by the finance team to date to gain assurance over the accuracy of transactions being made by BT. **Further work planned:** • We will review the latest service provision arrangements to ensure that the Council has sufficient information to prepare the financial statements in line with the planned closedown and audit timetable of April and May 2016 • Discussions with Internal Audit to review the work completed and assurance level planned for the Head of Internal Audit opinion • IT audit review of the general controls in operation in the financial ledger and overall IT control environment • We will carry out substantive testing of all items in the financial statements that are greater than tolerable error set for the Pension Fund accounts. The main focus will be on the journal testing and contributions.

Other risks identified

"The auditor should evaluate the design and determine the implementation of the entity's controls, including relevant control activities, over those risks for which, in the auditor's judgment, it is not possible or practicable to reduce the risks of material misstatement at the assertion level to an acceptably low level with audit evidence obtained only from substantive procedures"(ISA (UK & Ireland) 315).

In this section we outline the other risks of material misstatement which we have identified as a result of our planning.

Other risks	Description	Audit approach
Investment values – Level 2 investments	Valuation is incorrect – fair value measurements priced using inputs that are observable either directly or indirectly (Valuation net)	**Work completed to date:** • We have performed a walkthrough to gain assurance that the in-year controls were operating in accordance with our documented understanding. No material issues were arising from this work • We have sent letters to the custodian and fund managers requesting direct confirmation of ownership, existence and valuation of investment balances at 31st March 2016 and of income receivable throughout the year **Work planned:** • We will review the latest AAF 01/06 or ISAE 3402 audited reports on internal controls, published by the respective investment managers and Custodian, where available • We will review the reconciliation between information provided by the custodian, fund managers and the Fund's own records and seek explanations for any variances • We will select a sample of the individual investments held by the fund at the year end and then test the valuation of the sample by agreeing prices to third party sources where published (quoted investments) and an overall unit reconciliation for all material unitised pooled investment vehicles
Investment Income	Investment activity not valid / Investment income not accurate (Valuation Gross)	**Work completed to date:** • We have performed a walkthrough to gain assurance that the in-year controls were operating in accordance with our documented understanding. No material issues were arising from this work **Work planned:** • We will test a sample of investment income back to fund manager reports to ensure it is appropriate • We will complete a predictive analytical review for different types of investments
Investment purchases and sales	Investment activity not valid (Valuation Gross)	**Work completed to date:** • We have performed a walkthrough to gain assurance that the in-year controls were operating in accordance with our documented understanding. No material issues were arising from this work **Work planned:** • We will test a sample of purchases and sales to fund manager records to ensure they are appropriate

Other risks identified (continued)

Other risks	Description	Audit approach
Contributions	Recorded contributions not correct (Existence, Occurrence)	**Work completed to date:** • We have performed a walkthrough to gain assurance that the in-year controls were operating in accordance with our documented understanding. No material issues were arising from this work **Work planned:** • We will test a sample of contributions to source data to gain assurance over their accuracy and occurrence. • We will rationalise contributions received with reference to changes in member body payrolls and numbers of contributing pensioners to ensure that any unexpected trends are satisfactorily explained.
Benefits payable	Benefits improperly computed/claims liability understated (Completeness)	**Work completed to date:** • We have performed a walkthrough to gain assurance that the in-year controls were operating in accordance with our documented understanding. No material issues were arising from this work **Work planned:** • We will test a sample of individual pensions in payment by reference to member files. • We will perform controls testing over, completeness, accuracy and occurrence of benefit payments, • We will rationalise pensions paid with reference to changes in pensioner numbers and increases applied in the year to ensure that any unusual trends are satisfactorily explained.
Member Data	Member data not correct. (Rights and Obligations)	**Work completed to date:** • We have performed a walkthrough to gain assurance that the in-year controls were operating in accordance with our documented understanding. No material issues were arising from this work **Work planned:** • We will document the existence of key controls and reconciliations covering the determination of member eligibility, the input of evidence onto the Pensions Administration System and the maintenance of member records. With a view to reducing the level of substantive testing required, we will therefore test the key controls identified in these areas. • We will perform sample testing of changes to member data made during the year to source documentation

Page 128

Other risks identified (continued)

Other material balances and transactions

Under International Standards on Auditing, "irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance and disclosure". All other material balances and transaction streams will therefore be audited. However, the procedures will not be as extensive as the procedures adopted for the risks identified in the previous section but will include:

- Cash deposits
- Current Assets
- Actuarial Valuation and Actuarial Present Value of Promised Retirement Benefits
- Financial Instruments
- Level 1 investments

Other audit responsibilities

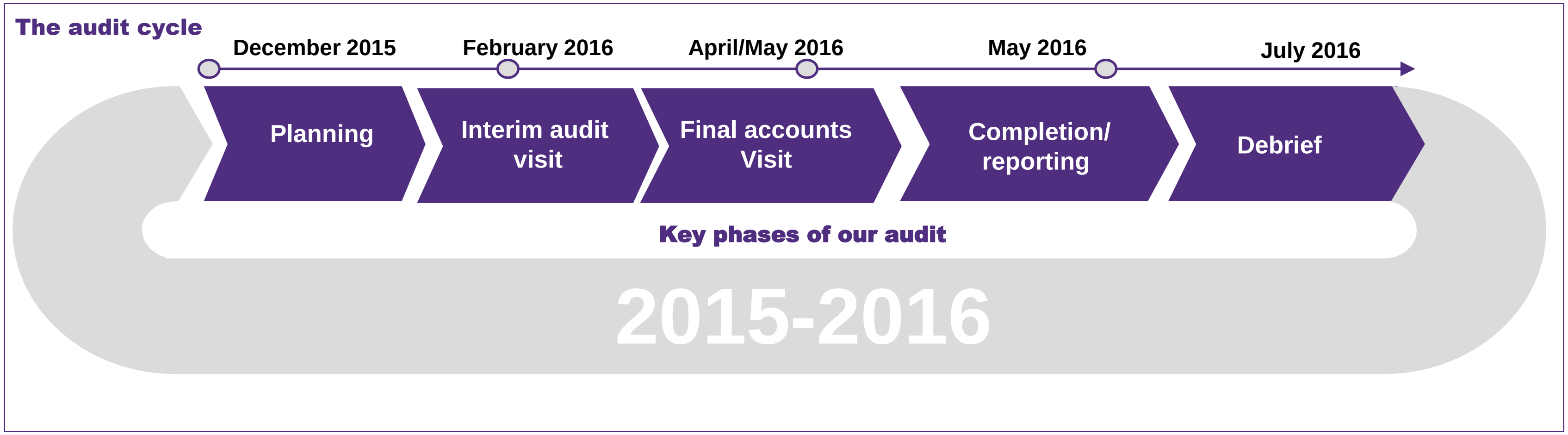
- We will read the Narrative Statement and check that it is consistent with the statements on which we give an opinion and disclosures are in line with the requirements of the CIPFA Code of Practice. Westminster City Council will provide a statement that covers both the Council and Pension Fund.

Results of interim audit work

The findings of our interim audit work, and the impact of our findings on the accounts audit approach, are summarised in the table below:

	Work performed	Conclusion
Internal audit	We have completed a high level review of internal audit's overall arrangements. Our work has not identified any issues which we wish to bring to your attention.	Our review of internal audit work has not identified any material weaknesses which impact on our audit approach.
Entity level controls	We are obtaining an understanding of the overall control environment relevant to the preparation of the financial statements including: • Communication and enforcement of integrity and ethical values • Commitment to competence • Participation by those charged with governance • Management's philosophy and operating style • Organisational structure • Assignment of authority and responsibility • Human resource policies and practices	Our work to date has identified no material weaknesses which are likely to adversely impact on the fund's financial statements.
Walkthrough testing	We have completed walkthrough tests of the Fund's controls operating in areas where we consider that there is a risk of material misstatement to the financial statements. Our work has not identified any issues which we wish to bring to your attention. Internal controls have been implemented by the Fund in accordance with our documented understanding.	Our work has not identified any material weaknesses which impact on our audit approach.

Key dates



Page 131

Date	Activity
December 2015	Planning
February 2016	Interim site visit
22 March 2016 / (3 February 2016)	Presentation of audit plan to Pension Fund Committee / (Risks presented to those charged with governance – Audit & Performance Committee)
11 April - 6 May 2016	Year end fieldwork
3 May 2016	Audit findings clearance meeting with the City Treasurer
12 May 2016	Report audit findings to those charged with governance (Audit and Performance Committee)
21 June 2016	Report audit findings to the Pension Fund Committee

Fees and independence

Fees

	£
Pension Fund Scale Fee (excluding VAT)	21,000

Fees for other services

Service	Fees £
Audit related services:	Nil
Non-audit services	Nil

Our fee assumptions include:

- Supporting schedules to all figures in the accounts are supplied by the agreed dates and in accordance with the agreed upon information request list.
- The scope of the audit, and the Fund and its activities, have not changed significantly.
- The Fund will make available management and accounting staff to help us locate information and to provide explanations.
- The accounts presented for audit are materially accurate, supporting working papers and evidence agree to the accounts, and all audit queries are resolved promptly.

Fees for other services

Fees for other services reflect those agreed at the time of issuing our Audit Plan. Any changes will be reported in our Audit Findings Report and the Annual Audit Letter of the Administering Authority.

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

Full details of all fees charged for audit and non-audit services will be included in our Audit Findings Report at the conclusion of the audit.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

Communication of audit matters with those charged with governance

International Standards on Auditing (UK & Ireland) (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table opposite.

This document, The Audit Plan, outlines our audit strategy and plan to deliver the audit, while The Audit Findings Report will be issued prior to approval of the financial statements and will present key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

We will communicate any adverse or unexpected findings affecting the audit on a timely basis, either informally or via a report to those charged with governance.

Respective responsibilities

This plan has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by Public Sector Audit Appointments Limited (http://www.psaa.co.uk/appointing-auditors/terms-of-appointment/)

We have been appointed as the Administering Authority's independent external auditors by the Audit Commission, the body responsible for appointing external auditors to local public bodies in England at the time of our appointment. As external auditors, we have a broad remit covering finance and governance matters.

Our annual work programme is set in accordance with the Code of Audit Practice ('the Code') issued by the NAO and includes nationally prescribed and locally determined work (https://www.nao.org.uk/code-audit-practice/about-code/). Our work considers the fund's key risks when reaching our conclusions under the Code.

It is the responsibility of the fund to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the fund is fulfilling these responsibilities.

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	✓	
Overview of the planned scope and timing of the audit. Form, timing and expected general content of communications	✓	
Views about the qualitative aspects of the entity's accounting and financial reporting practices, significant matters and issues arising during the audit and written representations that have been sought		✓
Confirmation of independence and objectivity	✓	✓
A statement that we have complied with relevant ethical requirements regarding independence, relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged. Details of safeguards applied to threats to independence	✓	✓
Material weaknesses in internal control identified during the audit		✓
Identification or suspicion of fraud involving management and/or others which results in material misstatement of the financial statements		✓
Non compliance with laws and regulations		✓
Expected modifications to the auditor's report, or emphasis of matter		✓
Uncorrected misstatements		✓
Significant matters arising in connection with related parties		✓
Significant matters in relation to going concern		✓

Page 134

grant-thornton.co.uk

City of Westminster

Committee Report

Decision Maker:	**PENSION FUND COMMITTEE**
Date:	**22 March 2016**
Classification:	**General Release**
Title:	**Performance of the Council's Pension Fund**
Wards Affected:	**All**
Policy Context:	**Effective control over Council Activities**
Financial Summary:	**There are no immediate financial implications arising from this report, although investment performance has an impact on the Council's employer contribution to the Pension Fund and this is a charge to the General Fund.**
Report of:	**Steven Mair** ***City Treasurer*** **smair@westminster.gov.uk** **020 7641 2904**

1. Executive Summary

1.1 This report presents a summary of the Pension Fund's performance to 31 December 2015, together with an estimated valuation position.

2. Recommendation

2.1 The Committee note the contents of this paper, the performance report from Deloitte and the current actuarial assumptions and valuation.

3. Background

Performance of the Fund

3.1 This report presents a summary of the Pension Fund's performance and estimated funding level to 31 December 2015. The investment report (Appendix 1) has been prepared by Deloitte, the Fund's investment adviser, who will be attending the meeting to present the key points and answer questions.

3.2 The Investment Performance Report shows that over the quarter to 31 December 2015, the market value of the assets increased by £23.3million as a result of the positive returns across the board with the exception of the gilt sub-portfolio with Insight.

3.3 The Funding update (Appendix 2) has been provided by the Fund Actuary, Barnett Waddingham. This indicates that the funding level has fallen from 74% to 73% over the quarter to 31 December 2015. The current funding level matches that reported at the last triennial valuation at 31 March 2013.

If you have any questions about this report, or wish to inspect one of the background papers, please contact the report author:

Nikki Parsons nparsons@westminster.gov.uk or 020 7641 6925

BACKGROUND PAPERS: None

APPENDICES:

Appendix 1 - Deloitte Investment Report, Quarter Ending 31 December 2015
Appendix 2 - Barnett Waddingham Funding Update Report as at 31 December 2015

Deloitte.

City of Westminster Pension Fund

Investment Performance Report
to 31 December 2015 – Executive Summary

Deloitte Total Reward and Benefits Limited
February 2016

Contents

1 Market Background

Three and twelve months to 31 December 2015

The UK equity market showed some volatility over the 3 months to 31 December 2015 given the persistent uncertainty around the strength of the global economy and China in particular. Markets rallied in late December following the Fed's announcement to raise rates, ending the fourth quarter in positive territory (FTSE All Share Index: 4.0%).

Mid and small cap companies outperformed the largest UK firms over the fourth quarter, with the FTSE 250 and FTSE Small Cap indices returning 5.0% and 4.1% respectively. At the sector level, Technology was the strongest performer (10.9%), whilst the poorest performing sector was once again Basic Materials (-11.1%). This sector continues to be affected by falling commodity prices and concerns over an economic slowdown in China.

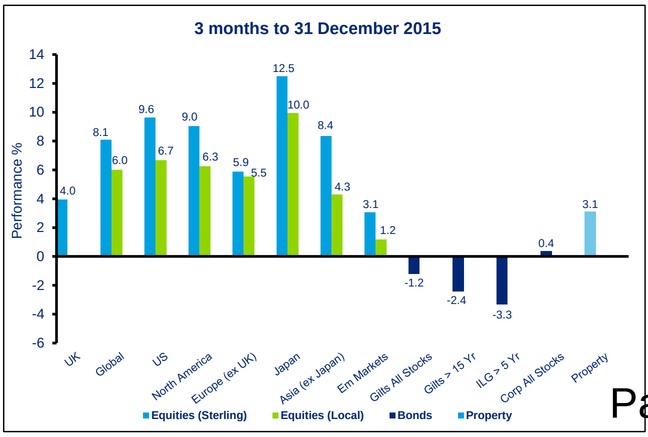
Global equity markets outperformed the UK in both local currency terms (6.0%) and sterling terms (8.1%), with the pattern of returns over the quarter broadly in line with that seen in the UK. Currency hedging was generally detrimental to sterling investors investing globally over the quarter, as sterling depreciated against the dollar and yen, and was broadly flat against the euro. At the regional level, Japanese equities offered the highest return of 12.5% in sterling terms and 10.0% in local currency terms. The emerging markets were the poorest performing region over the quarter, returning 3.1% in sterling terms and 1.2% in local currency terms.

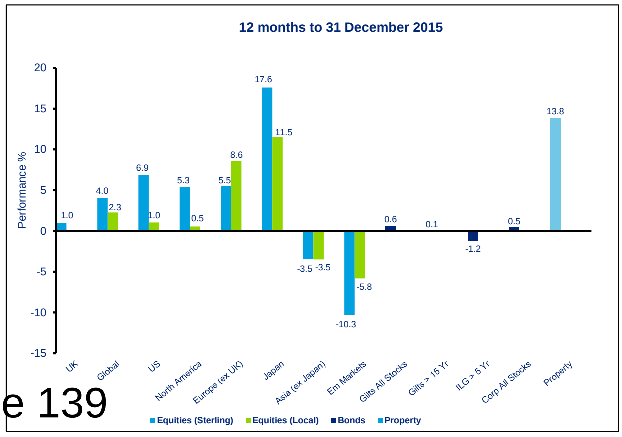
UK nominal gilts delivered negative returns over the fourth quarter as yields increased across all but the shortest maturities, with the All Stocks Gilt Index returning -1.2%. Real yields on UK index-linked gilts also increased over the period, with the Over 5 Year Index-linked Gilt Index returning -3.3%. Corporate bonds posted marginally positive returns over the quarter, with the iBoxx All Stocks Non Gilt Index returning 0.4%. Returns on corporate bonds were ahead of gilts as credit spreads narrowed.

Over the 12 months to 31 December 2015, the FTSE All Share Index returned 1.0%, although returns were volatile over the year, and varied across sectors. Technology delivered the highest return at 16.8%, whilst the Basic Materials and Oil & Gas sectors suffered dramatically over 2015 in an environment of falling commodity prices, returning -42.1% and -20.7% respectively. Global equity markets outperformed the UK, with the FTSE All World Index returning 4.0% and 2.3% in sterling and local currency terms respectively.

UK nominal gilts delivered marginally positive returns over 2015. Positive returns can be attributed to coupon payments, as gilt yields rose across all maturities (and therefore gilt prices fell). The All Stocks Gilt Index returned 0.6% over the 12 month period and the Over 15 Year Gilt Index returned just 0.1%. There were more significant increases in real yields over the year, causing the Over 5 year Index-linked Gilt Index to return -1.2%. Corporate bond returns were marginally positive, with the iBoxx All Stocks Non Gilt Index returning 0.5% over the 12 months to 31 December 2015. This was again due to the effect of coupon payments, as gilt yields increased and credit spreads widened over the year.

The UK property market performed strongly in 2015, returning 3.1% over the quarter and 13.8% over the year to 31 December 2015.





2 Total Fund

2.1 Investment Performance to 31 December 2015

The following table summarises the performance of the Fund's managers.

Manager	Asset Class	Last Quarter (%)			Last Year (%)			Last 3 Years (% p.a.)[1]			Since inception (% p.a.)[1]		
		Fund		B'mark	Fund		B'mark	Fund		B'mark	Fund		B'mark
		Gross	Net[1]		Gross	Net[1]		Gross	Net[1]		Gross	Net[1]	
Majedie	UK Equity	1.4	1.3	4.0	-0.3	-0.7	1.0	10.3	10.0	7.3	9.6	9.2	5.4
LGIM	Global Equity	5.9	5.9	5.9	1.3	1.2	1.3	12.2	12.1	12.1	12.1	12.0	12.1
Baillie Gifford	Global Equity	10.6	10.5	8.1	8.6	8.2	3.8	n/a	n/a	n/a	10.3	9.9	8.3
Longview	Global Equity	5.5	5.3	8.4	n/a	n/a	n/a	n/a	n/a	n/a	7.7	7.1	4.9
Insight	Gilts	-0.4	-0.5	-0.5	0.9	0.8	0.9	1.8	1.7	1.7	5.0	4.9	5.1
	Non Gilts	0.6	0.5	0.3	1.4	1.1	1.1	4.5	4.2	4.0	5.6	5.4	5.2
Hermes	Property	3.7	3.6	2.9	15.0	14.6	13.0	15.5	15.1	13.1	10.2	9.8	9.3
Standard Life	Property	1.5	1.4	-0.7	8.3	7.8	2.6	n/a	n/a	n/a	10.3	9.8	7.3
Total		4.3	4.2	4.4	3.4	3.0	2.5	10.4	10.0	9.6	6.2	5.9	5.8

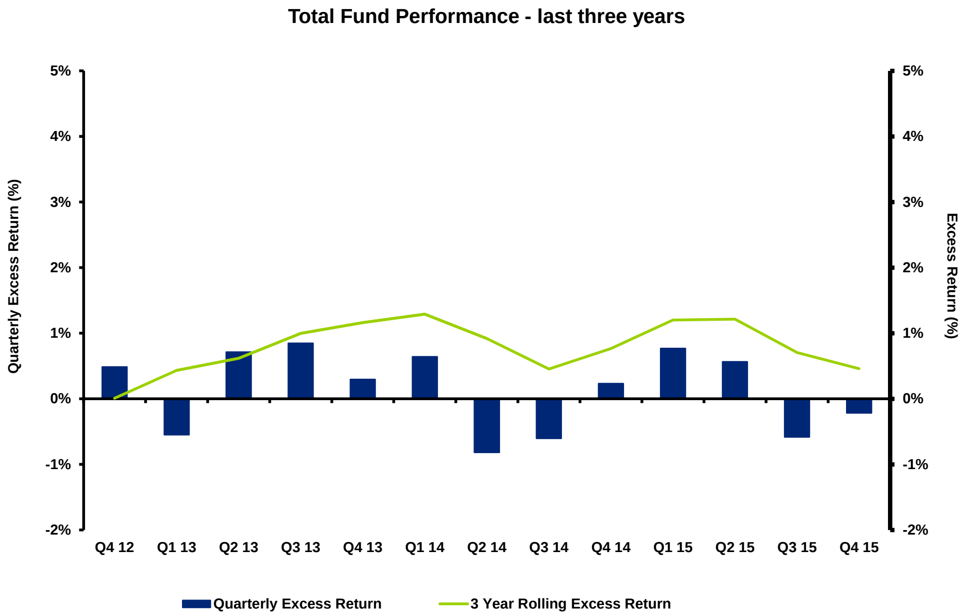
Source: Investment Managers

(1) Estimated by Deloitte when manager data is not available.

See appendix 1 for more detail on manager fees and since inception dates

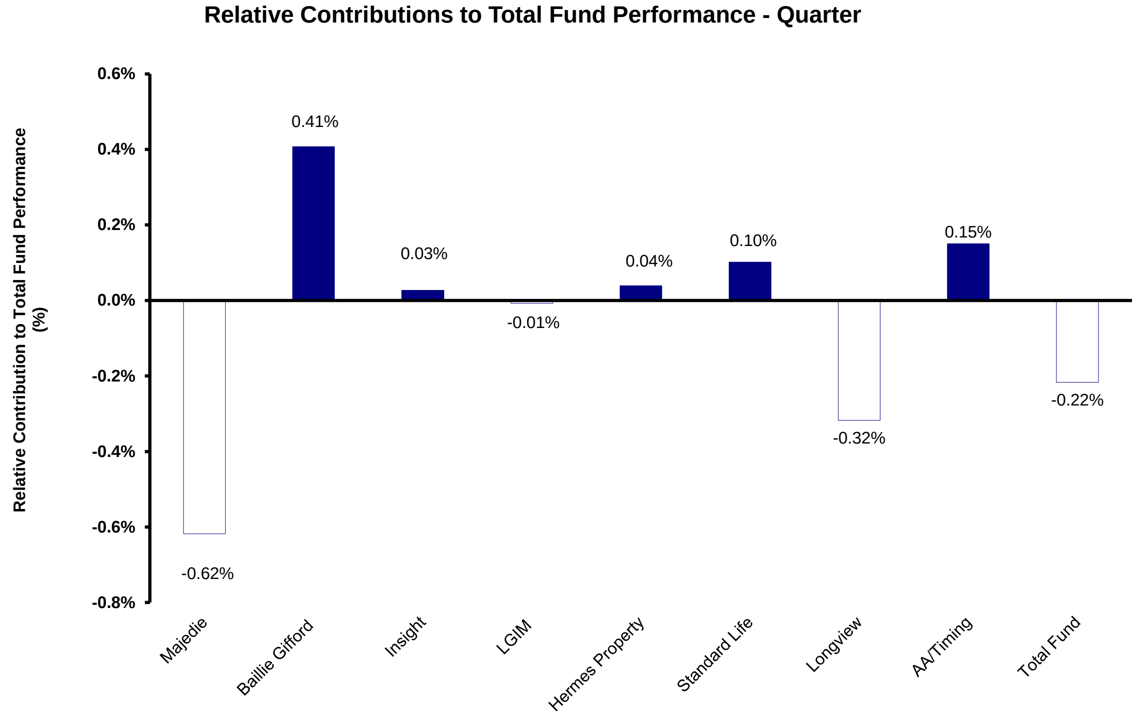
Over the quarter the Fund underperformed its benchmark, mostly due to the underperformance of the active equity managers Majedie and Longview.

The chart below shows the performance of the Fund over the last three years, highlighting that the rolling three-year performance has been positive since 2013, with Majedie, Baillie Gifford and Hermes contributing positively. Please note that performance is shown net of fees versus the benchmark.

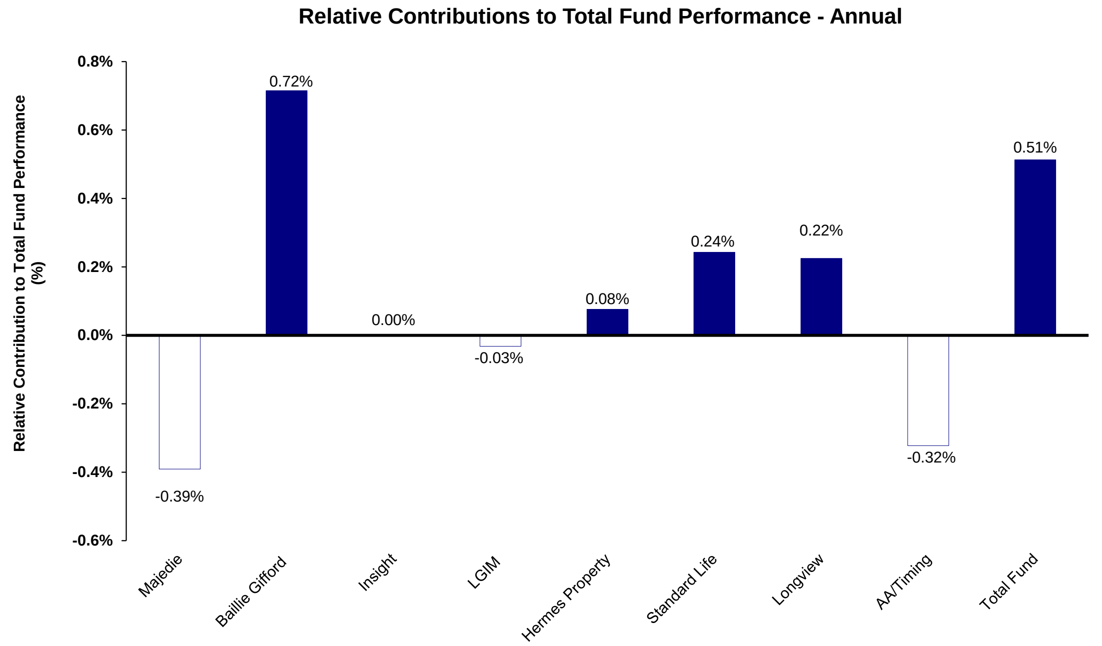


Page 140

2.2 Attribution of Performance to 31 December 2015



The Fund underperformed its composite benchmark by 0.2% over the fourth quarter of 2015, largely as a result of weak performance from the active equity managers Majedie and Longview. However, the Fund's overall overweight to equities was beneficial over the quarter.



The Fund outperformed over the year, largely due to strong performance from Baillie Gifford, Longview and Standard Life. The AA/Timing bar largely reflects the fact that the actual allocation has differed from the benchmark. The average underweight allocation to Hermes and Standard Life and overweight allocation to Majedie over the year have contributed to the negative contribution from AA/Timing.

Asset Allocation as at 31 December 2015

The table below shows the assets held by manager and asset class as at 31 December 2015.

Manager	Asset Class	End Sept 2015 (£m)	End Dec 2015 (£m)	End Sept 2015 (%)	End Dec 2015 (%)	Benchmark Allocation* (%)
Majedie	UK Equity	238.5	241.8	23.3	23.1	22.5
LGIM	Global Equity (Passive)	253.2	243.2	24.7	23.2	22.5
Baillie Gifford	Global Equity	161.0	178.1	15.7	17.0	25
Longview	Global Equity	101.7	107.1	9.9	10.2	
	Total Equity	**754.4**	**770.2**	**73.6**	**73.5**	**70**
Insight	Fixed Interest Gilts (Passive)	17.9	17.9	1.7	1.7	20
Insight	Sterling Non-Gilts	153.9	154.7	15.0	14.8	
	Total Bonds	**171.8**	**172.6**	**16.8**	**16.5**	**20**
Hermes	Property	48.9	54.9	4.8	5.2	5
Standard Life	Property	49.8	50.5	4.9	4.8	5
To be Determined	Property / Infrastructure	-	-	-	-	-
	Total Property	**98.7**	**105.4**	**9.6**	**10.1**	**10**
	Total	**1,024.9**	**1,048.2**	**100**	**100**	**100**

Source: Investment Managers Figures may not sum to total due to rounding

* The benchmark allocation has been set to 70% equity, 20% bonds and 10% property to better align the benchmark performance calculation with the allocation and performance of the Fund. The Fund's long term strategic benchmark includes a 5% allocation to Property / Infrastructure, which will be funded from the equity portfolio.

Over the quarter the market value of the assets increased by c. £23.3m as a result of the positive returns across the board with the exception of the gilt sub-portfolio with Insight. There was a disinvestment over the quarter of c. £25m from LGIM Global Equity mandate.

As at 31 December 2015, the Fund was overweight equities by c. 3.5% when compared with the amended benchmark allocation, with overweight allocations to UK equities and both passive and active global equities. As a result of these overweight positions, the Fund was underweight bonds by c. 3.5% while the allocation to property was broadly in line with benchmark.

Yield analysis as at 31 December 2015

The following table shows the yield on each of the Fund's investments.

Manager	Asset Class	Yield as at 31 December 2015
Majedie	UK Equity	3.35%
LGIM	Global Equity (Passive)	0.27%
Baillie Gifford	Global Equity	0.00%*
Longview	Global Equity	2.07%
Insight	Fixed Interest Gilts (Passive)	1.23%
Insight	Sterling Non-Gilts	3.14%
Hermes	Property	3.60%
Standard Life	Property	4.49%
	Total	**1.93%**

* Baillie Gifford does not quote a yield for the Global Alpha strategy – the yield on the benchmark index was 2.7%.

3 Summary of Manager Ratings

The table below summarises Deloitte's ratings of the managers employed by the Fund and triggers against which managers should be reviewed.

Manager	Mandate	Triggers for Review	Rating
Majedie	UK Equity	Further turnover within the core investment team Re-opening the UK equity products with no clear limits on the value of assets that they would take on	1
Baillie Gifford	Global Equity	Loss of key personnel Change in investment approach Lack of control of asset growth	1
Longview	Global Equity	Loss of key personnel Change in investment approach Lack of control in growth of assets under management	1
LGIM	Global Equity (passive)	Major deviation from benchmark returns Significant loss of assets under management	1
Insight	Sterling Non-Gilts	Departure of any of the senior members of the investment team Steps to broaden their product offering beyond the current UK and European focus without first bringing in the additional expertise	1
Insight	Fixed Interest Gilts (Passive)		n/a
Hermes	Property	Significant growth in the value of assets invested in the fund Changes to the team managing the mandate	1
Standard Life	Property	Richard Marshall leaving the business or ceasing to be actively involved in the Fund without having gone through an appropriate hand-over A build up within the Fund of holdings with remaining lease lengths around 10 years	1

Majedie UK Equity

Business

Majedie continues to see steady growth in the Global Equity and Focus Funds which have AUM of $52m and $26m respectively as at 31 December 2015.

Majedie has been investing internally in their client management system and a "Hive" project to encourage closer ties within the investment teams.

Majedie is having discussions with the London CIV regarding its products, specifically the UK Equity Strategy, which 3 of the London Boroughs invest in. Majedie is open to making the Fund available through the CIV, assuming it can agree terms which will benefit the current London LGPS investors although negotiations are still ongoing at this stage.

Personnel

There were 2 new joiners over the quarter (James Dudgeon to the US Equity team, and Emily Barnard to the UK Income team) although the team managing the UK Equity Fund remains unchanged.

Deloitte view – We continue to rate Majedie positively for its UK equity capabilities.

Baillie Gifford

Business

Total assets under management increased over the fourth quarter of 2015 from £110.6bn as at 30 September 2015 to £123bn as at 31 December 2015. The increase was largely due to positive investment returns as net client flows were marginally negative. Baillie Gifford gained 19 new clients over the quarter and lost 11 from a broad range of strategies.

Baillie Gifford closed the Global Alpha Fund to new investors at the start of the 2015 and will only accept inflows from existing clients subject to capacity remaining available.

From 1 January 2016, Baillie Gifford changed its commission arrangements with brokers to an execution only basis. This means that dealing commission charges will only include the cost of trading stocks and no other services provided by the brokers (e.g. research costs). Baillie Gifford now pays any additional costs directly so this will increase the cost to Baillie Gifford but reduce the trading costs for clients. The cost saving for clients is expected to be small, likely in the low single digits of basis points per annum.

Personnel

Baillie Gifford announced that two new partners, John MacDougall and Tim Garratt will be appointed from 1 May 2016 to coincide with the retirement of one partner, Peter Hadden.

- John MacDougall is an investment manager who joined Baillie Gifford in 2000 and spent time in the Japanese team and Global Discovery team before recently transferring to the Long Term Global Growth team. John moved to the Long Term Global Growth team to bring his experience of analysing and selecting rapidly growing small companies which he developed when working in the Global Discovery team.
- Tim Garratt is a Director in the Clients Department and joined Baillie Gifford in 2007.
- Peter Hadden is a Director in the Clients Department and announced his decision to retire after 15 years with Baillie Gifford.

Within Baillie Gifford, Tom Slater, one of the Long Term Global Growth portfolio managers, became head of the North American equity team. Tom will continue to be a portfolio decision maker in the Long Term Global Growth team.

Deloitte view – We continue to rate Baillie Gifford positively for its global equity capabilities.

LGIM

Business

As at 30 September 2015, Legal & General Investment Management (“Legal & General”) had total assets under management of c. £717bn (including derivative overlays and advisory assets). As at 30 September, the AUM on equity amounted to c. £296bn.

Personnel

There were no personnel changes over the fourth quarter of 2015. The transitioning of Ali Toutounchi’s responsibilities was completed during the quarter.

Deloitte View: We continue to rate Legal & General positively for its passive capabilities.

Longview

Business

As at 31 December 2015, Longview had AUM of c. £13.6bn. Longview saw some outflows from the DB corporate sector and as such, have re-opened the fund to try to recycle some of this excess capacity. Longview aren’t currently advertising the re-opening of the fund, but are looking for c. $1bn to $2bn from previous contacts in Australia and America.

Personnel

There have been no changes to the investment team over the quarter.

Phil Corbet (Managing Director who sat on the Company's Board) announced his retirement from 31 December 2015. Phil has been replaced by Barbara Sanderson as Managing Director and Stuart Tostevin takes over his seat on the Board.

At a more junior level, Aimee Foster joined the compliance team in London.

Deloitte view – We continue to rate Longview for its global equity capabilities.

Insight

Business

Insight continued to see a strong inflow of assets over the quarter. Assets under management were £407bn as at 31 December 2015.

There were no material changes to the Fixed Income Group over the fourth quarter. Tamara Burnell joined as a credit analyst and will work particularly on emerging market financials. The integration of the Cutwater team in the US appears to have progressed smoothly, giving Insight further capacity across a number of credit focused strategies.

Deloitte view – We continue to rate Insight positively for its Fixed Income capabilities.

Hermes

Business

The total value of the Trust increased over the quarter to c. £1.28bn at 31 of December 2015.

Hermes continues to see strong interest from prospective unit holders with a waiting list for new investment of c. £100m.

In the fourth quarter of 2015, it was announced that Hermes lost a significant bond mandate from BT Pension Scheme (who owns Hermes). Hermes maintains that this loss accounted for just 3% of revenue and was only marginally profitable.

Personnel

There were no changes to the team over the quarter.

Deloitte view – We continue to rate the team managing HPUT. We will continue to monitor Hermes in light of the loss of the bond mandate but we do not expect there to be any impact on the management of the property Trust.

Standard Life

Business

The Fund's assets under management increased slightly to £1.61bn over the fourth quarter following positive performance, with no significant inflows or outflows over the quarter.

In relation to our previous concerns about the Fund's supermarket exposure, there was an arbitration on rent for a Sainsburys (Southport) asset. Despite expectations that rent would increase by 13%, the arbitrators imposed no increase in rent, bringing the value of the individual asset down by c. 10%. While the supermarket sector as a whole contributed negatively over the fourth quarter there were positive contributions from some of the Fund's Tesco and Aldi holdings

Personnel

There were no changes to the team over the quarter with Richard Marshall, the lead portfolio manager, having now relocated to London.

Deloitte View: We rate SLI positively for its long lease property capabilities but will continue to engage with the manager and monitor the supermarket exposure within the Long Lease Property Fund

4 Baillie Gifford – Global Equity

Baillie Gifford was appointed to manage an active Global Equity mandate from 18 March 2014. The manager is remunerated on an asset based fee, reflecting the total value of assets invested in the strategy across the Tri-borough. The target is to outperform the benchmark of 2% p.a.

4.1 Global equity – Investment performance to 31 December 2015

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
Baillie Gifford - Gross of fees	10.6	8.6	n/a	10.3
Net of fees[1]	10.5	8.2	n/a	9.9
MSCI AC World Index	8.1	3.8	n/a	8.3
Relative (net of fees)	2.4	4.4	n/a	1.6

Source: Baillie Gifford

(1) Estimated by Deloitte

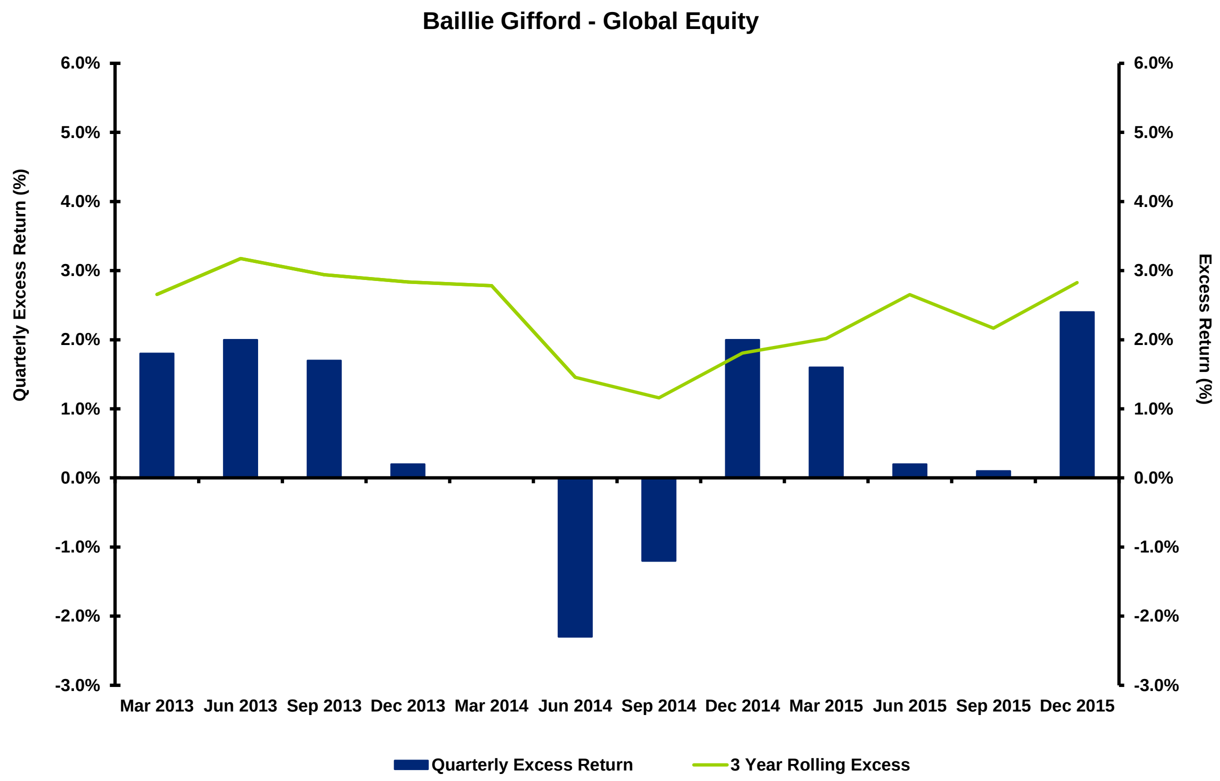
See appendix 1 for more detail on manager fees

Inception date taken as 18 March 2014

The Baillie Gifford Global Equity fund has outperformed its benchmark over the quarter, year and period since inception. The main contributors to the outperformance over the quarter were the Fund's overweight holdings in Amazon.com, Alibaba and Baidu.com.

The main detractors over the quarter were the overweight positions in Harley-Davidson and Ultra Petroleum Corp. Not holding Microsoft also detracted versus the benchmark.

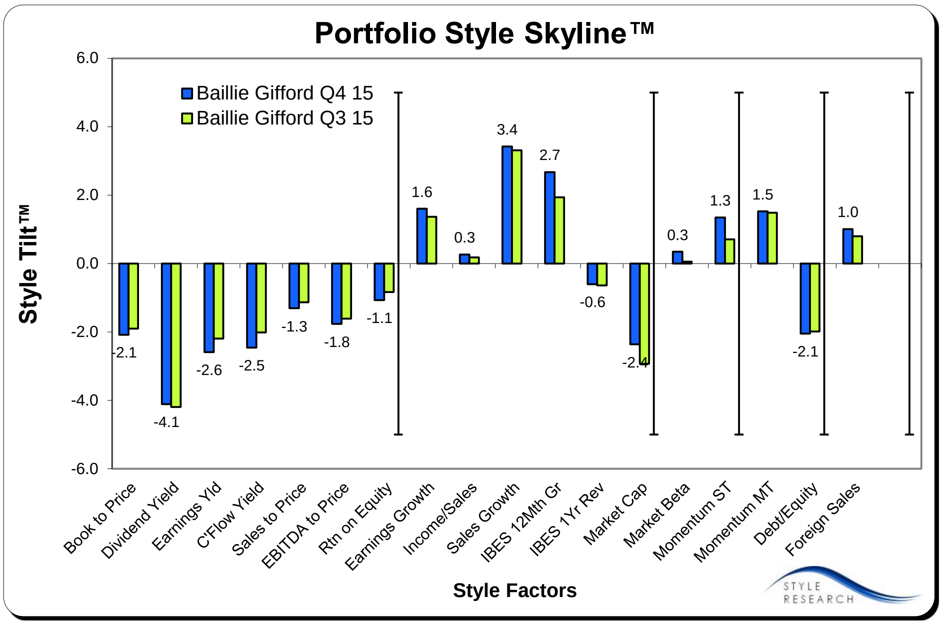
The graph below shows the net quarterly returns and the rolling three year excess returns relative to the benchmark. Note that the Fund only invested in this fund from 18th March 2014 and previous periods are shown for information only. The Fund's current thee year excess return is ahead of target (+2% p.a.) having outperformed the benchmark by 2.8% p.a.



Page 147

4.2 Style analysis

We have analysed the Style of Baillie Gifford's Global Alpha portfolio as at 31 December 2015, the results can be seen in the below graph. When considering the analysis it should be borne in mind that any figures in excess of +/- 1 are considered to be meaningful.



As can be seen, Baillie Gifford has a marked negative bias to value related factors and a positive bias to growth factors which is consistent with the manager's stated investment approach. This is a similar position to last quarter.

The top 10 holdings in the Baillie Gifford fund account for c. 28.5% of the fund and are detailed below.

Top 10 holdings as at 31 December 2015	Proportion of Baillie Gifford fund
Royal Caribbean	4.1%
Amazon.com	4.0%
Prudential	3.6%
Naspers	2.9%
CHR	2.6%
Alphabet	2.5%
Taiwan Semi	2.3%
Anthem	2.1%
Ryanair Holdings	2.1%
Markel	2.1%
Total	**28.5%**

Baillie Gifford	30 September 2015	31 December 2015
Total Number of holdings	97	99
Active risk	4.0%	4.1%
Coverage	7.2%	7.6%
Top 10 holdings	27.6%	28.5%

As at 31 December 2015, Baillie Gifford held 99 stocks, with an overlap with the FTSE All World index of 7.6%. The active risk, as at 31 December 2015, was 4.1% - a marginal increase from the previous quarter although most of this can be attributed to a general pick-up in market volatility.

5 LGIM – Global Equity (Passive)

LGIM was appointed to manage a passive global equity mandate from the 31 October 2012.The manager is remunerated on a fixed fee based on the value of assets. The target is to deliver performance in line with the stated benchmarks.

5.1 Passive Global Equity – Investment Performance to 31 December 2015

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
LGIM - Gross of fees	5.9	1.3	n/a	12.1
Net of fees[1]	5.9	1.2	n/a	12.0
FTSE World GBP Hedged	5.9	1.3	n/a	12.1
Relative (net of fees)	0.0	-0.1	n/a	-0.1

Source: LGIM

(1) Estimated by Deloitte

See appendix 1 for more detail on manager fees

Inception date taken as 1 November 2012 (prior to that the mandate was an active equity mandate). The portfolio aims to track the benchmark.

The investment objective of the Fund is to track the performance of the FTSE AW-World Index (less withholding tax if applicable) - GBP Hedged (with the exception of advanced emerging markets) to within +/-0.5% p.a. for two years out of three.

The LGIM Fund has performed broadly in line with the benchmark over the quarter, one year and since the inception of the mandate.

Deloitte is currently working with LGIM with regards to the Fund’s mandate, looking at the options for how this should be moved on to the London CIV platform in the most cost effective way, as and when the passive options become available. Analysis is being carried out to consider the restructuring and rebalancing costs, particularly relating to the Fund’s emerging markets exposure and a formal proposal will be discussed once this has been finalised.

6 Majedie – UK Equity

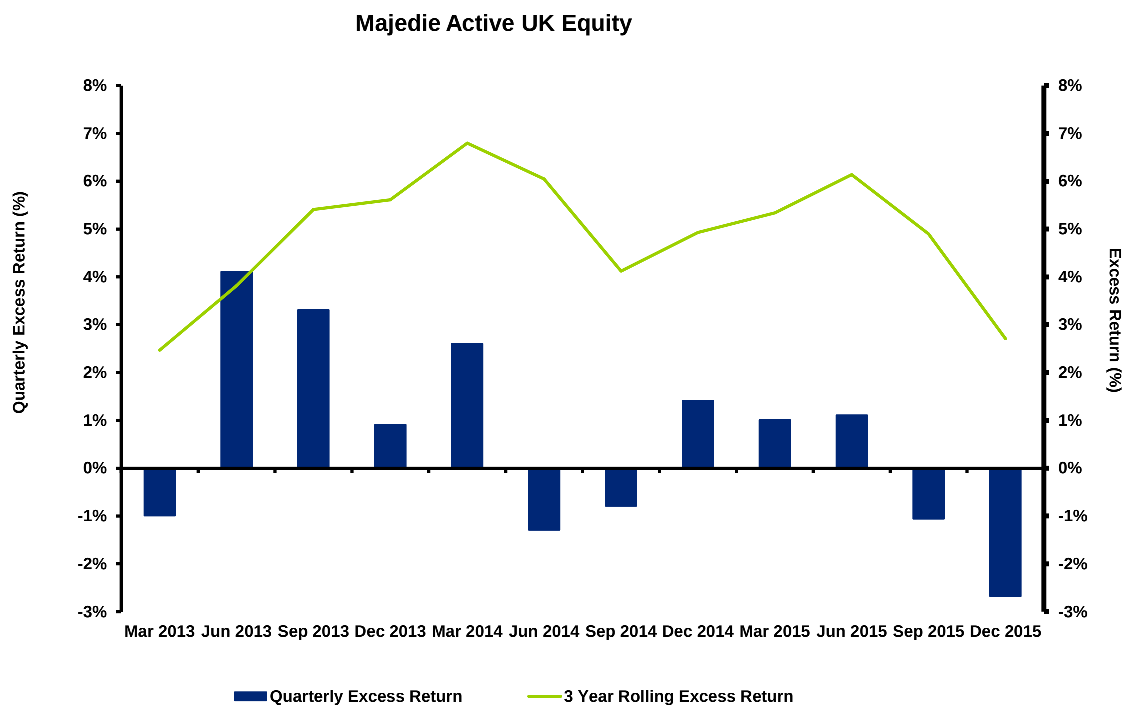
Majedie was appointed to manage an active UK equity mandate. The manager's remuneration is a combination of a fixed fee based on the value of assets and a performance related fee which is payable when the excess return of the portfolio over a rolling 3 year period is more than 1% p.a. The target is to outperform the benchmark by 2% p.a.

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
Majedie - Gross of base fees	1.4	-0.3	10.3	9.6
Net of base fees[1]	1.3	-0.7	10.0	9.2
FTSE All-Share Index	4.0	1.0	7.3	5.4
Relative (net of fees)	-2.7	-1.7	2.7	3.8

Source: Majedie

See appendix 1 for more detail on manager fees

Inception date taken as 31 May 2006.



Majedie underperformed its benchmark over the quarter by 2.7% and over the year by 1.7% on a net of fees basis. However, over the longer timeframes of three years and since inception, the manager has outperformed its benchmark on a net basis by 2.7% p.a. and 3.8% p.a. respectively.

The main detractors from performance were Majedie's holding in supermarkets Tesco and Morrisons, banks Barclays and RBS, and mining company Anglo American.

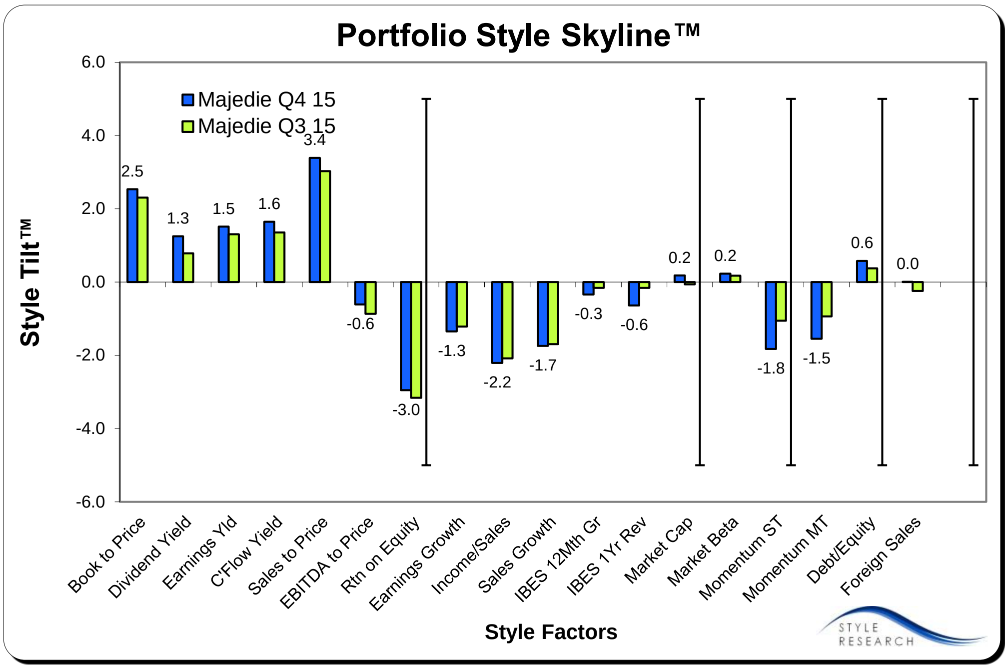
Majedie remains convinced of its allocation to Anglo American, stating that it was simply too early into this market. Tesco did not manage to convince investors that it had turned a corner in Q4 with the market worried of the sector's decline to the discount stores. Majedie does not believe that this is the case, but rather that Tesco made some mistakes in the past by pushing margins up in the UK to fund its US ventures. Tesco is working to rectify these mistakes but the recovery has taken longer than Majedie anticipated. One a like-for-like basis, sales over the Christmas period increased for Morrisons and Tesco, and declined for Aldi which helps to cement Majedie's convictions.

RBS continues to suffer from bad press with the investment bank and conduct issues worrying investors. Majedie remains convinced that RBS has cleaned up its balance sheet and that the big risks lie with the insurers and large investment managers instead rather than in the banking sector.

On the positive side, Majedie's holding in Orange performed well with the increase in mobile data and relaxation to regulations driving returns. Electrocomponents released details of substantial management led changes which were received well by the market. Being underweight in Rolls-Royce also helped Majedie over the quarter, as investors realised that the company had been allowing for maintenance cashflows in its projections unlike its peers.

6.1 Style analysis

We have analysed the Style of Majedie as at 31 December 2015. When considering the analysis it should be borne in mind that any figures in excess of +/- 1 are considered to be meaningful.



While the portfolio continues to show a modest positive bias to value factors and a modest negative bias to growth factors, it is not particularly strong and we would not be surprised to see this change over time depending on where Majedie finds appropriate opportunities.

The top 10 holdings in the Majedie fund account for c. 42% of the fund and are detailed below.

Top 10 holdings as at 31 December 2015	Proportion of Majedie fund
HSBC	7.3%
BP	5.7%
Vodafone	5.2%
Royal Dutch Shell	5.0%
GlaxoSmithKline	3.6%
Orange	3.5%
Barclays	3.4%
Cash	3.1%
RBS	2.8%
BT Group	2.8%
Total	**42.4%**

Majedie	30 September 2015	31 December 2015
Total Number of holdings	196*	167
Active risk	2.7%	2.8%
Coverage	40.7%	39.5%
Top 10 holdings	39.7%	42.4%

*includes 120 stocks in the Majedie UK Smaller Companies Fund, which the fund invests in.

As at 31 December 2015, Majedie held 167 stocks in total, with an overlap with the FTSE All Share index of 39.5%. This coverage is significantly higher than both Baillie Gifford and Longview, reflecting to an extent the multi manager approach. Majedie's active risk, as at 31 December 2015, was 2.8%.

7 Longview – Global Equity

Longview was appointed on 15 January 2015 to manage an active global equity mandate. The manager's remuneration is based on the value of assets invested across the Tri-borough. The expectation is that the fund will outperform the benchmark by 3% p.a.

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
Longview - Gross of base fees	5.5	n/a	n/a	7.7
Net of base fees[1]	5.3	n/a	n/a	7.1
MSCI World Index	8.4	n/a	n/a	4.9
Relative (net of fees)	-3.1	n/a	n/a	2.2

Source: Longview

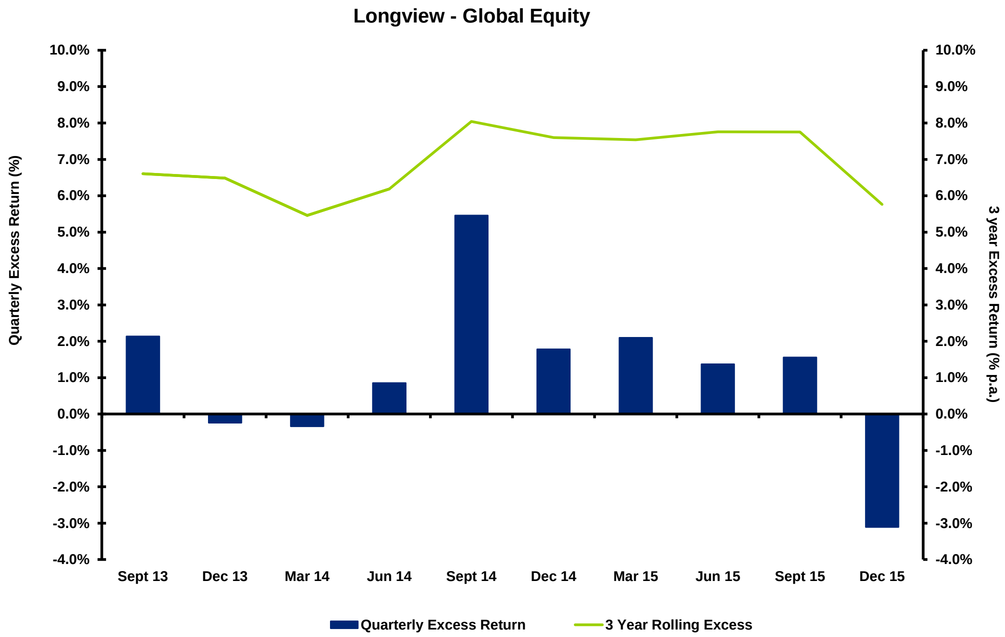
(1) Estimated by Deloitte

See appendix 1 for more detail on manager fees

Longview underperformed the benchmark by 3.1% on a net of fees basis, over the fourth quarter of 2015. Since inception, the fund has outperformed by 2.2%.

Both Pearson and Yum! Brands performed poorly over the quarter and have been downgraded in Longview's analysis and therefore sold. Pearson (the publishing and education company) has posted weak results for several quarters now – citing lower than expected US enrolments in higher education and the loss of various testing contracts. Yum! Brands, who are the largest fast food providers in China (owning brands such as KFC and Pizza Hut), has not recovered as well as Longview had anticipated following various chicken food scares in China (which accounts for approximately 50% of their business). As a result, its business fundamentals score was downgraded and the stock was subsequently sold.

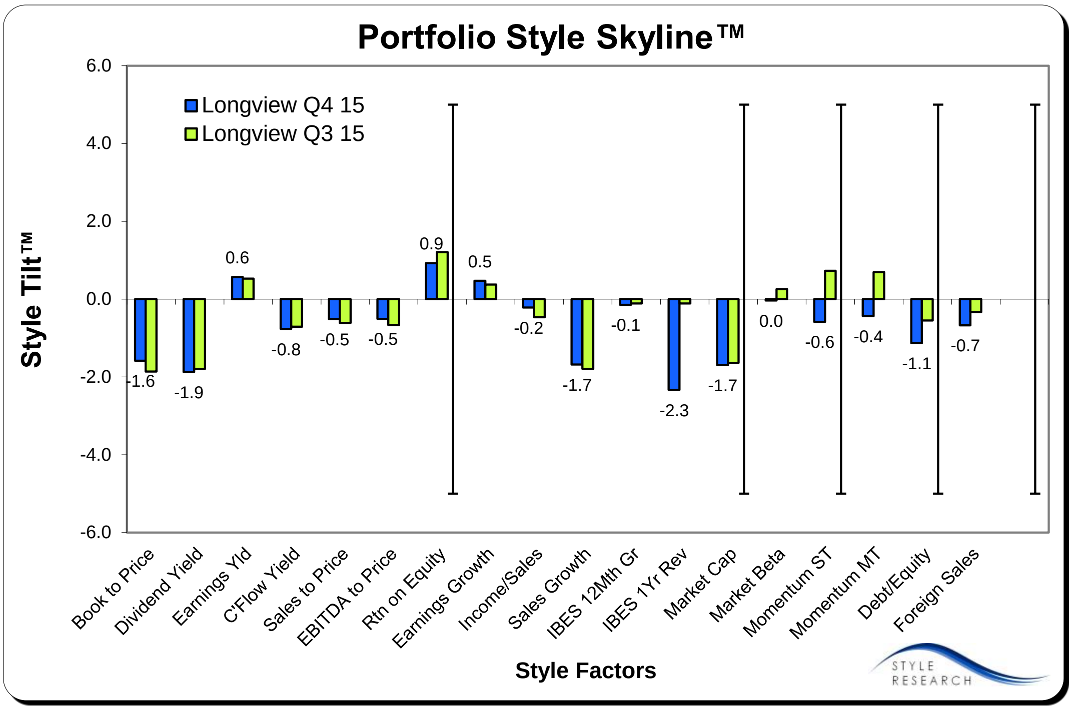
Longview's holding in SAP (the software company) performed well, helped by improving margins and revenue. Continental and Delphi Automotive recovered from the Volkswagen scandal, contributing positively to performance over the quarter. In addition, Thermo Fisher Scientific (a life science research company purchased last quarter) posted good results and WPP (the advertising company) profited from the weakness in sterling and recovered from a low position over the previous quarter.



For information purposes we have included the longer run performance history for the strategy.

7.1 Style analysis

The Style "skyline" for Longview's global equity portfolio as at 31 December 2015 is shown below graph. When considering the analysis it should be borne in mind that any figures in excess of +/- 1 are considered to be meaningful.



As can be seen from the above, Longview does not currently have a strong bias to either value or growth factors, showing little change from the previous quarter's "skyline".

The top 10 holdings in the Longview fund account for c. 35.8% of the fund and are detailed below.

Top 10 holdings as at 31 December 2015	Proportion of Longview fund
AON	4.1%
Delphi Automotive	4.0%
Bank of New York Mellon	3.6%
Thermo Fisher Scientific	3.6%
Compass	3.5%
SAP	3.4%
Accenture	3.4%
WPP	3.4%
Zimmer Biomet Holdings	3.4%
Wells Fargo	3.4%
Total	**35.8%**

Longview	30 September 2015	31 December 2015
Total Number of holdings	36	35
Active risk	4.2%	4.1%
Coverage	4.7%	4.4%
Top 10 holdings	35.5%	35.8%

As at 31 December 2015, Longview held 35 stocks in total, with an overlap with the FTSE All World index of only 4.4%. This coverage is low due to the high conviction investing that Longview undertakes, which also leads to an active risk of 4.1% as at 31 December 2015.

8 Insight – Bonds

Insight was appointed to manage two bond portfolios – an actively managed corporate bond (non – Gilt) portfolio and a passively managed gilt portfolio. The manager's fee is based on the value of assets. The target of the Non-Gilt portfolio is to outperform the benchmark by 0.9% p.a.

8.1 Insight – Active Non Gilts

8.1.1 Investment Performance to 31 December 2015

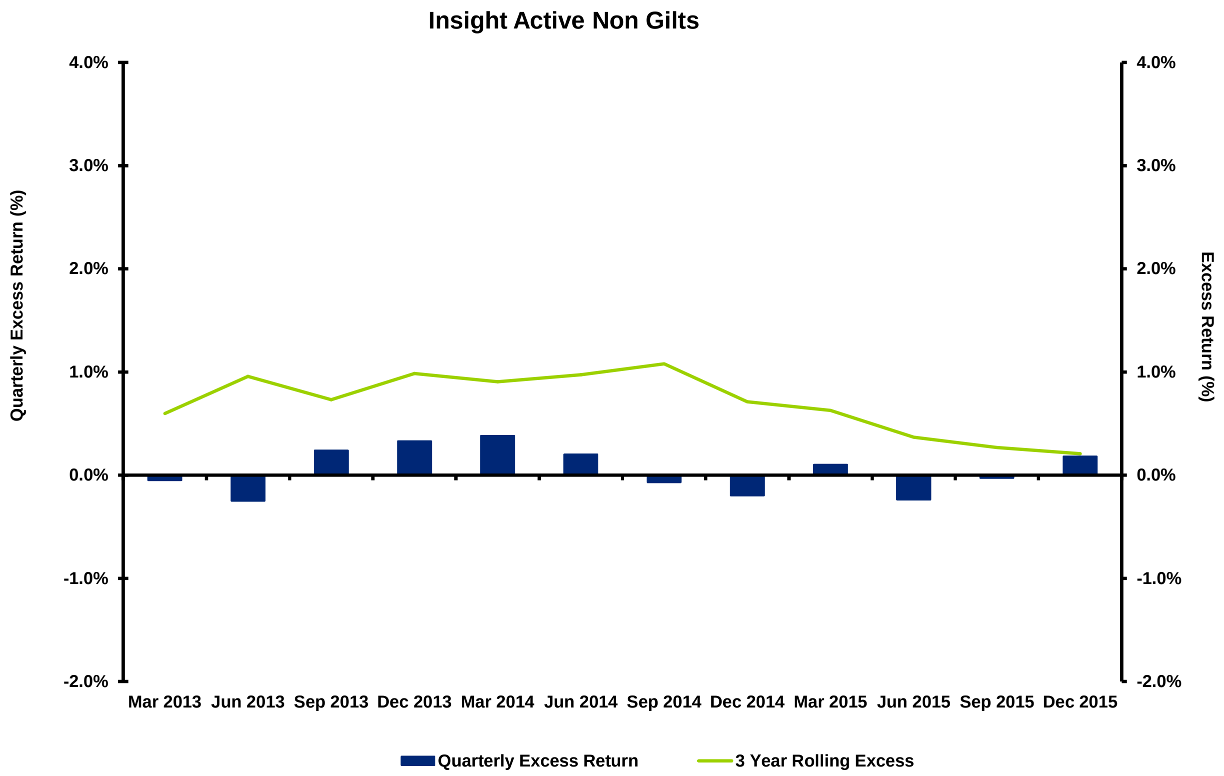
	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
Insight (Non-Gilts) - Gross of fees	0.6	1.4	4.5	5.6
Net of fees[1]	0.5	1.1	4.2	5.4
iBoxx £ Non-Gilt 1-15 Yrs Index	0.3	1.1	4.0	5.2
Relative (net of fees)	0.2	0.0	0.2	0.2

Source: Insight

(1) Estimated by Deloitte

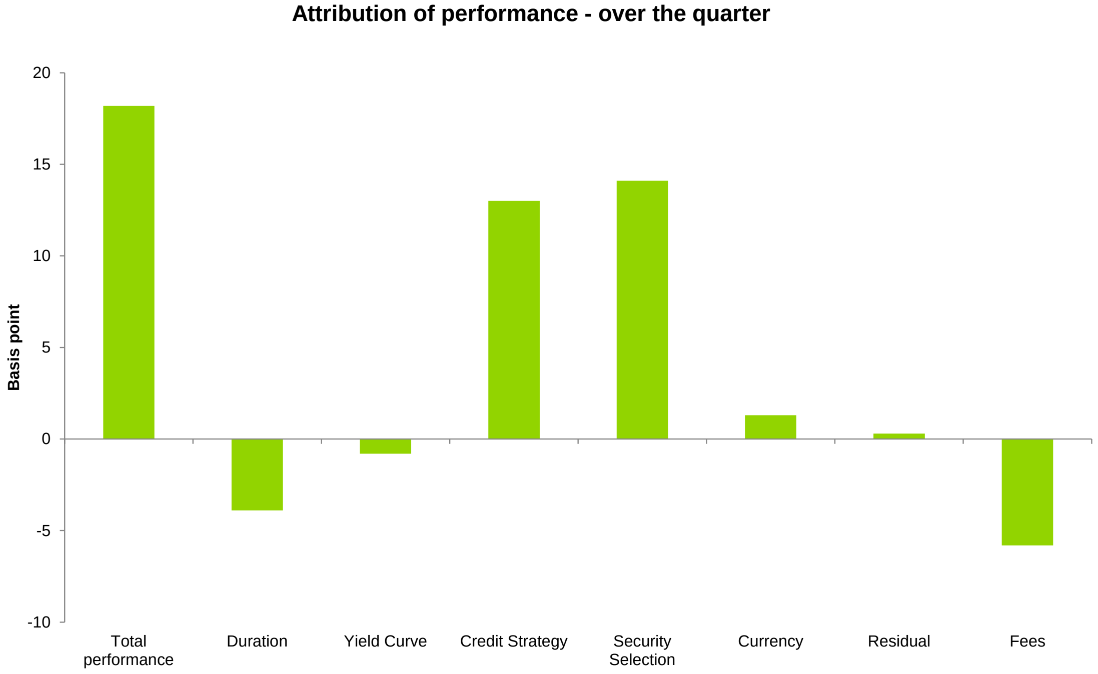
See appendix 1 for more detail on manager fees

Inception date taken as 31 May 2006.



Over the quarter the portfolio marginally outperformed the benchmark by 0.2% net of fees. Over the year to 31 December 2015, the fund has performed in line with the benchmark and marginally outperformed by 0.2% p.a. over the 3 years and since inception.

8.1.2 Attribution of Performance



Source: Estimated by Insight

Insight's outperformance this quarter has been driven by security selection and credit strategy, with the duration positioning (being slightly long relative to the benchmark) offsetting some of this performance.

8.2 Insight – Government Bonds

8.2.1 Investment Performance to 31 December 2015

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
Insight (Passive Bonds) - Gross	-0.4	0.9	1.8	5.0
Net of fees[1]	-0.5	0.8	1.7	4.9
FTSE A Gilts up to 15 Yrs Index	-0.5	0.9	1.7	5.1
Relative (net of fees)	0.0	-0.1	0.0	-0.2

Source: Insight

(1) Estimated by Deloitte

See appendix 1 for more detail on manager fees

Inception date taken as 30 June 2008.

The gilt portfolio has performed in line with its benchmark over the quarter and broadly in line over the longer periods to 31 December 2015.

8.3 Duration of portfolios

	End Sept 2015		End Dec 2015	
	Fund (Years)	Benchmark (Years)	Fund (Years)	Benchmark (Years)
Non-Government Bonds (Active)	5.5	5.3	5.6	5.3
Government Bonds (Passive)	4.3	4.7	4.4	4.9

Source: Insight

9 Hermes – Property

Hermes was appointed to manage a core UK property portfolio. The manager is remunerated on a fixed fee based on the value of assets. The target is to outperform the benchmark by 0.5% p.a.

9.1 Portfolio Monitoring Summary

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)[1]
Hermes - Gross of fees	3.7	15.0	15.5	10.2
Net of fees[1]	3.6	14.6	15.1	9.8
Benchmark	2.9	13.0	13.1	9.3
Relative (net of fees)	0.7	1.6	2.0	0.5

Source: Hermes

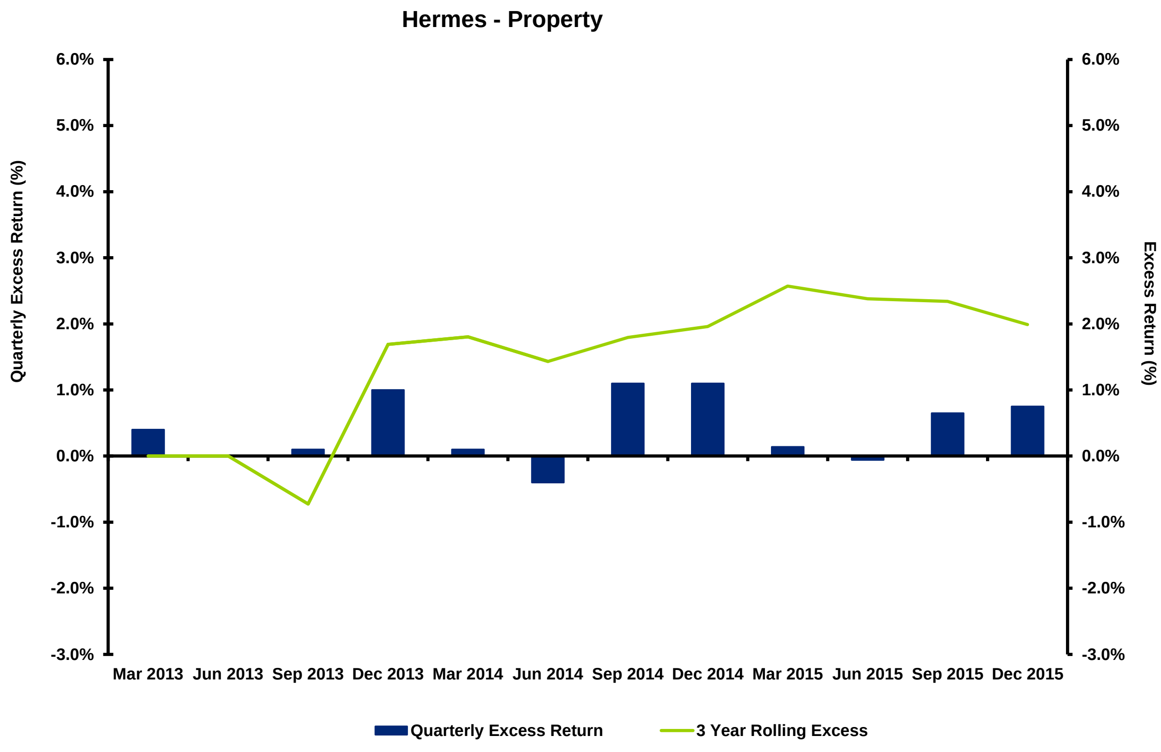
(1) Estimated by Deloitte

See appendix 1 for more detail on manager fees

Inception date is taken as 26 October 2010

Hermes outperformed its benchmark by 0.7% over the quarter with longer term performance also ahead of benchmark.

Outperformance over the quarter was driven primarily by the Trust's holdings in the Industrial and "Other" sectors. Over the year to 31 December 2015, the Trust's investments in the office sector (West End, City and Reset of UK) have performed well.



9.2 Sales and Purchases

The team completed two purchases over the quarter:

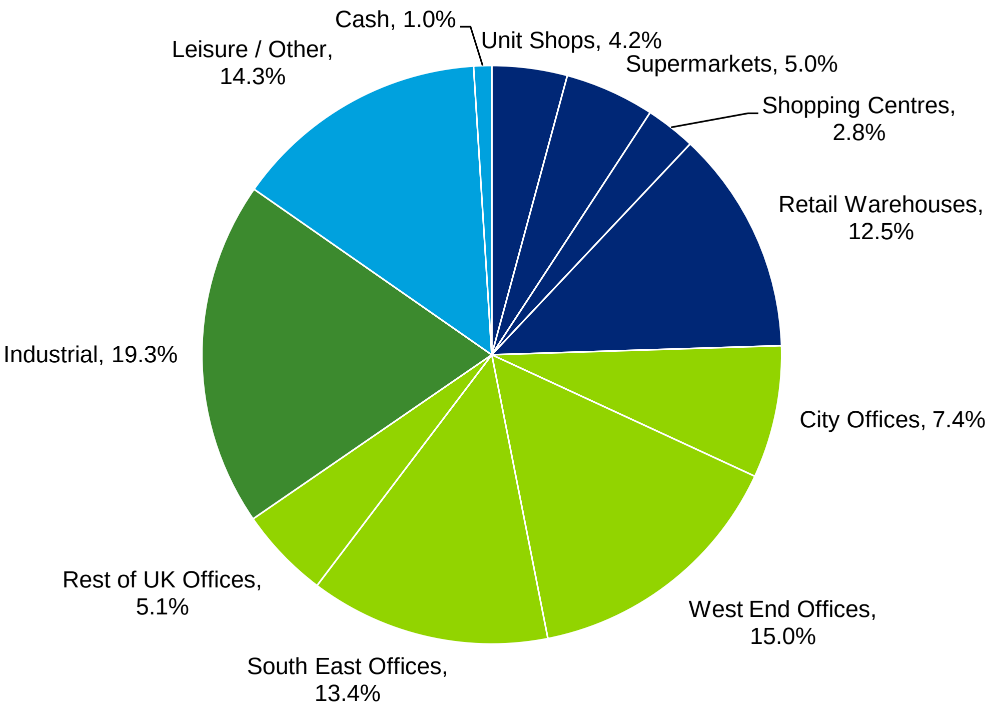
- Polar Park, Heathrow: a £31m industrial use investment with initial income yield of 5.5%, located in Heathrow. This estate is very well located and currently benefits from a low average passing rent against the average.

- Fairway Trading, Hounslow: a £15.95m freehold multi-let industrial estate with a new initial yield of 5.4%. This estate is located to the south east of the airport and has a comparatively low average passing rent against the average.

The team also sold Allport, Southall for £21.89m. The sale reflects a net initial yield of 4.9% and a 2.1% premium above the end-November 2015 valuation of £21.45m. The sale achieves a premium price for an asset with limited reversionary and asset management potential over the next five years given the 10+ year unexpired term.

9.3 Portfolio Summary as at 31 December 2015

The Hermes Property Unit Trust invests across retail, offices, industrials and other sectors, with the split as at 31 December 2015 shown below.



The table below shows the top 10 directly held assets in the fund as at 31 December 2015.

Asset	Sub-sector	Value (£m)
Maybird Shopping Park, Stratford-upon-Avon	Retail Warehouses	112.3
8/10 Great George Street, London	West End Offices	58.0
27 Soho Square, London	West End Offices	44.6
Sainsbury's, Maxwell Road, Beaconsfield	Supermarkets	42.9
2 Cavendish Square, London	West End Offices	41.5
Hythe House, Hammersmith	Standard Offices SE	35.9
Christopher Place, St Albans	Shopping Centres	35.8
Boundary House, London	City Offices	33.6
Camden Works, London	Standard Offices SE	33.4
Broken Wharf House, London	City Offices	32.6
Total		**470.6**

10 Standard Life – Long Lease Property

Standard Life Investments ("SLI") was appointed to manage a UK property portfolio investing in core assets where the focus is on properties with long leases let to high quality tenants. The manager is remunerated on a fixed fee based on the value of assets. The target is to outperform the FT British Government All Stocks Index benchmark +2.0% p.a. by 0.5% p.a.

10.1 Portfolio Monitoring Summary

	Last Quarter (%)	Last Year (%)	Last 3 Years (% p.a.)	Since Inception (% p.a.)
Standard Life - Gross of fees	1.5	8.3	n/a	10.3
Net of fees[1]	1.4	7.8	n/a	9.8
Benchmark	-0.7	2.6	n/a	7.3
Relative (net of fees)	2.1	5.2	n/a	2.5

Source: Standard Life

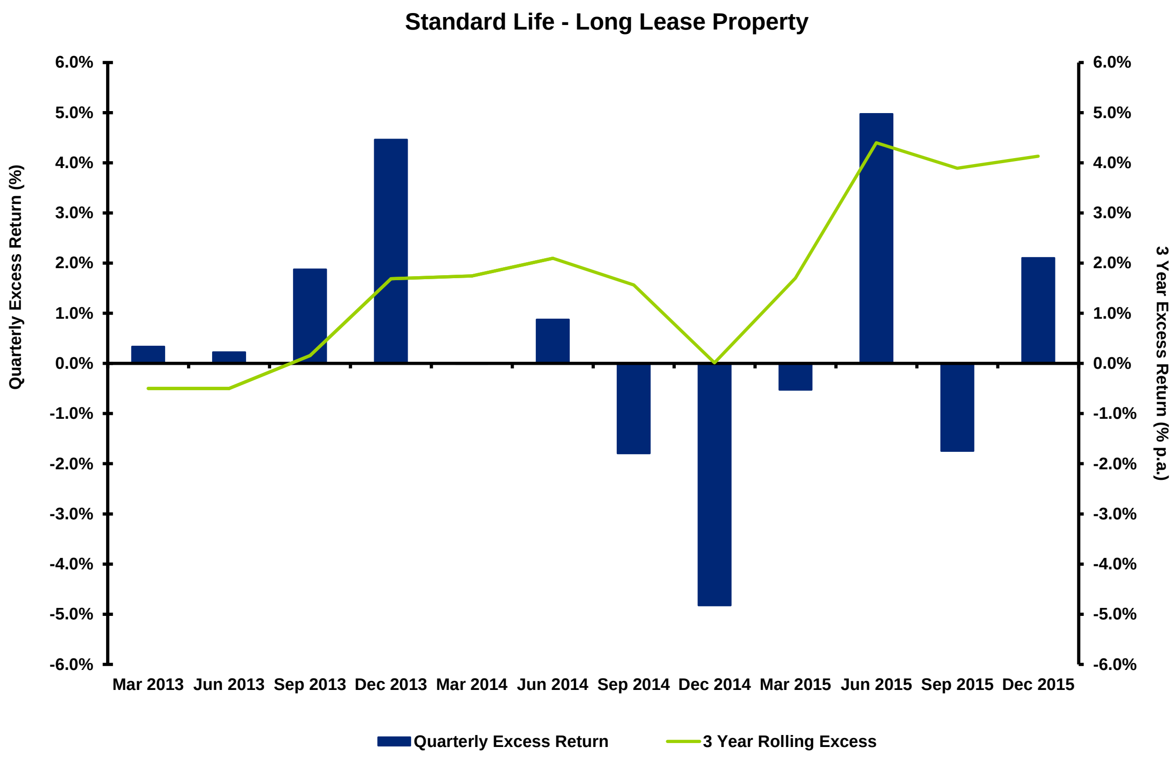
(1) Estimated by Deloitte

See appendix 1 for more detail on manager fees

Since inception: 14 June 2013

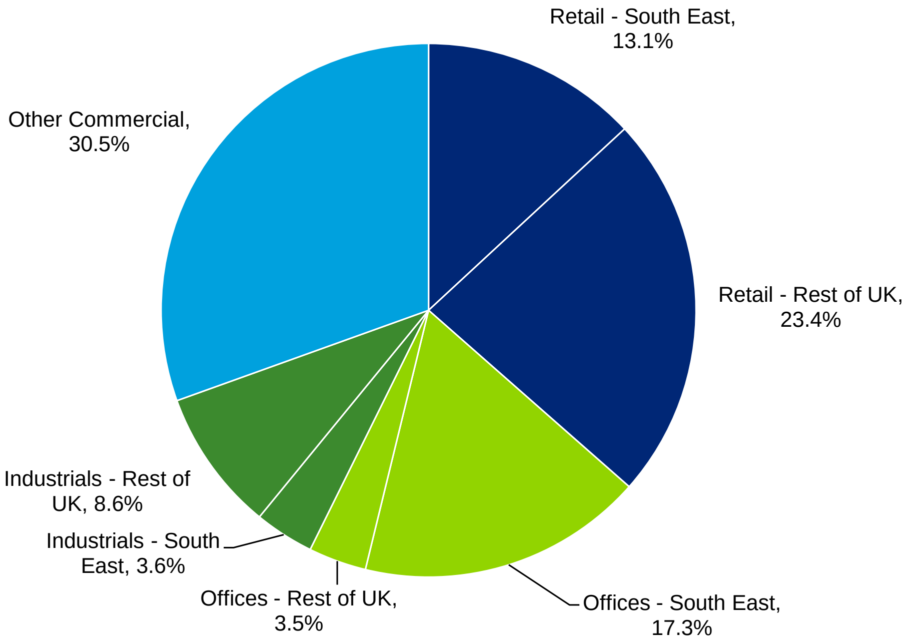
The SLI Long Lease Property Fund returned 1.4% over the fourth quarter of 2015, outperforming the benchmark of the FTSE Gilt All Stocks Index + 2% by 2.1% net of fees The fund continues to lag the wider property market, which returned 3.1% over the fourth quarter, where high quality secondary assets have been performing well – in particular South East Offices.

Net performance of the Long Lease Fund is shown below. Please note that the Fund only invested in this fund from June 2013 and previous periods are shown for information only.



Page 159

The sector allocation in the Long Lease Property Fund as at 31 December 2015 is shown in the graph below.



When compared to an IPD benchmark, the Fund remains underweight the office sector (20.8% compared to 35.2%) and remains underweight to the industrial sector (12.2% compared to 19.6%) at the end of the fourth quarter. The Fund is also slightly underweight the retail sector (36.5% compared to 38.6%) which is dominated by supermarkets and contains no shopping centres or retail warehouses which form a significant part of the IPD universe (c. 25%).

The table below shows details of the top ten tenants in the Fund measured by percentage of net rental income:

Tenant	Property/Location	Total Rent £m p.a.	% Net Income
Tesco Stores Limited	Various	7.8	10.8
Premier Inn Limited	Fountainbridge	5.1	7.0
Sainsbury's Supermarkets	Various	4.9	6.7
Asda Stores Limited	Various	4.5	6.2
University of Salford	Peel Park Campus	3.6	5.0
Marstons PLC	Various	3.6	5.0
Save the Children Fund	1 St Johns Lane, London	3.6	5.0
WM Morrisons Supermarkets	Various	3.5	4.8
Glasgow City Council	Various	3.1	4.3
Travis Perkins (Properties)	Various	3.0	4.1
Total		**42.7**	**59.0**

The top 10 tenants contribute 59.0% of the total net income into the Fund. Supermarkets continue to dominate the Fund, with Tesco, Sainsbury's, Asda and Morrison's contributing 28.5% to the Fund's total net rental income.

The Fund's average unexpired lease term fell over the quarter from 26.2 years to 25.9 years.

The proportion of the Fund invested in assets with fixed, part-fixed, CPI or RPI-linked rental increases remained broadly unchanged over the quarter at 90.3%.

10.2 Sales and Purchases

A £20.6m Z Hotel in Shoreditch, London was purchased over the fourth quarter with the 34 year lease having RPI(2,5) linked annual rent reviews, representing an initial yield of 3.75%. Despite this development not having an investment grade covenant, SLI viewed it as an attractive asset for the Fund given the developments within the Shoreditch area, as well as the property's vacant possession value being 60% higher than the agreed purchase price.

The development funding of the VW showroom was completed in January 2016, on a 25 year lease. Although VW suffered high profile negative press over the emissions scandal, SLI believes the strength of VW's balance sheet will be strong enough to withstand any subsequent fines without adversely impacting its ability to make lease payments.

Appendix 1 – Fund and Manager Benchmarks

The tables in this Appendix detail the benchmarks and outperformance targets, for the Total Fund and each individual manager.

Total Fund

Inception: 1 June 2006. Current benchmark allocation effective from 25 March 2015.

Manager	Asset Class	Long Term Strategic Benchmark Allocation	Benchmark	Outperformance Target	Inception Date	Fees (p.a.)	Tracking Error p.a.
Majedie	UK Equity	20.0	FTSE All-Share Index	+2.0 p.a. (net of fess)	31/05/06	c.35bps base fees +20 performance fee on 1 outperformance over 3 year rolling	2.0-6.0
LGIM	Global Equity	20.0	FTSE World GBP Hedged	Passive	01/11/12	13bps base fees	+/- 0.5
Baillie Gifford	Global Equity	25.0	MSCI AC World Index	+2.0 p.a. (net of fess)	18/03/14	40bps base fee	
Longview	Global Equity		MSCI World (GBP) Index	To outperform the benchmark over a market cycle	15/01/15	75bps base fees minus a rebate dependent on fund size	
Insight	Fixed Interest Gilts	-	FTSE GILTS up to 15 Yrs Index	Passive	31/05/06	10bps base fees	
	Non-Gilts	20.0	iBoxx £ Non-Gilt 1-15 Yrs Index	+ 0.90 p.a. (gross fees)	31/05/06	c.24bps base fee	0 - 3.0
Hermes	Property	5.0	IPD UK PPFI Balanced PUT Index	+0.5 p.a. (net of fess)	26/10/10	40bps base fee	
Standard Life	Property	5.0	FTSE Gilts All Stocks Index +2% p.a.	+0.5 p.a. (net of fess)	14/06/13	50bps base fee	
To be determined	Property / Infrastructure	5.0					
	Total	**100.0**					

For the purposes of our performance calculations we have assumed the 5% awaiting allocation to property / infrastructure is split evenly between Majedie and LGIM.

Appendix 2 – Manager Ratings

Based on our manager research process, we assign ratings to the investment managers for specific products or services. The ratings are based on a combination of quantitative and qualitative factors, where the inputs for the qualitative factors come from a series of focused meetings with the investment managers. The ratings reflect our expectations of the future performance of the particular product or service, based on an assessment of:

- The manager's business management;
- The sources of ideas that go to form the portfolio ("alpha generation");
- The process for including the ideas into the portfolio ("alpha harnessing"); and
- How the performance is delivered to the clients.

On the basis of the research and analysis, managers are rated from 1 (most positive) to 4 (most negative), where managers rated 1 are considered most likely to deliver outperformance, net of fees, on a reasonably consistent basis. Managers rated 1 will typically form the basis of any manager selection short-lists.

Where there are developments with an investment manager that cause an element of uncertainty we will make the rating provisional for a short period of time, while we carry out further assessment of the situation.

Appendix 3 – Style analysis

The Style Skylines are designed to answer the question "How significantly different is the portfolio from the benchmark?" in respect of Style factors which are important and relevant in equity markets.

In each Style Skyline, the first six bars from the left are Value factors (shown as blue bars in the output). The next six bars are the Growth factors (green bars) and include four current/historic measures as well as two forward-looking Growth factors (incorporating IBES consensus earnings estimates and earnings revisions). The remaining bars on the right cover Size, Beta, Momentum, Gearing/Leverage and Foreign Sales.

As a general rule of thumb, for any individual Style tilt (Standard or Adjusted):

- Style tilts less than -0.5 or more than +0.5 indicate a tilt is observable.
- Style tilts less than -1 or more than +1 are statistically significant.
- Style tilts less than -2 or more than +2 are statistically very significant.

There is a further interpretation when we compare across similar factors such as the Value factors (blue bars in the Style Skyline) or the Growth factors (green bars). If most of the Value factors are positive and, say, between 0.4 to 0.6 this suggests that there is a significant Value tilt even though no individual tilt is very significant i.e. multiple tilts in a similar direction within Value or within Growth can reinforce our interpretation of a Style orientation.

It is possible that more extreme tilts can be produced when portfolios and benchmarks are themselves narrowly defined against the market e.g. it is not unusual for Small Cap portfolios to show tilts of 3, 4 or even much larger in magnitude against a Small Cap benchmark. In these cases the significance of the tilts should not be overemphasized.

There is little purity of definition, but in general the various Value and Growth tilt possibilities can be initially interpreted as follows:

Value Factors	Growth Factors	Interpretation
Positive	Negative	Traditional Value
Positive	Positive	Growth at the Right Price
Negative	Positive	Traditional Growth
Negative	Negative	Popular Recovery Situations

Appendix 4 – Risk warnings & Disclosures

- Past performance is not necessarily a guide to the future.
- The value of investments may fall as well as rise and you may not get back the amount invested.
- Income from investments may fluctuate in value.
- Where charges are deducted from capital, the capital may be eroded or future growth constrained.
- Investors should be aware that changing investment strategy will incur some costs.
- Any recommendation in this report should not be viewed as a guarantee regarding the future performance of the products or strategy.

Our advice will be specific to your current circumstances and intentions and therefore will not be suitable for use at any other time, in different circumstances or to achieve other aims or for the use of others. Accordingly, you should only use the advice for the intended purpose.

Our advice must not be copied or recited to any other person than you and no other person is entitled to rely on our advice for any purpose. We do not owe or accept any responsibility, liability or duty towards any person other than you.

Deloitte Total Reward and Benefits Limited is authorised and regulated by the Financial Conduct Authority.

City of Westminster Pension Fund

Funding Update Report

as at 31 December 2015

Barnett Waddingham LLP

15 February 2016

Contents

Introduction

We have carried out a quarterly monitoring assessment of the City of Westminster Pension Fund (the Fund) as at 31 December 2015. The purpose of this assessment is to provide an update on the funding position.

We assess the funding position on a smoothed basis which is an estimate of the average position over a six month period spanning the reporting date. As the smoothing adjustment reflects average market conditions spanning a six month period straddling the reporting date, the smoothed figures are projected numbers and likely to change up until three months after the reporting date. The smoothed results are indicative of the underlying trend.

In addition, we assess the funding position on an unsmoothed basis where assets are taken at market value and discount rates are taken as the spot rates at the reporting date.

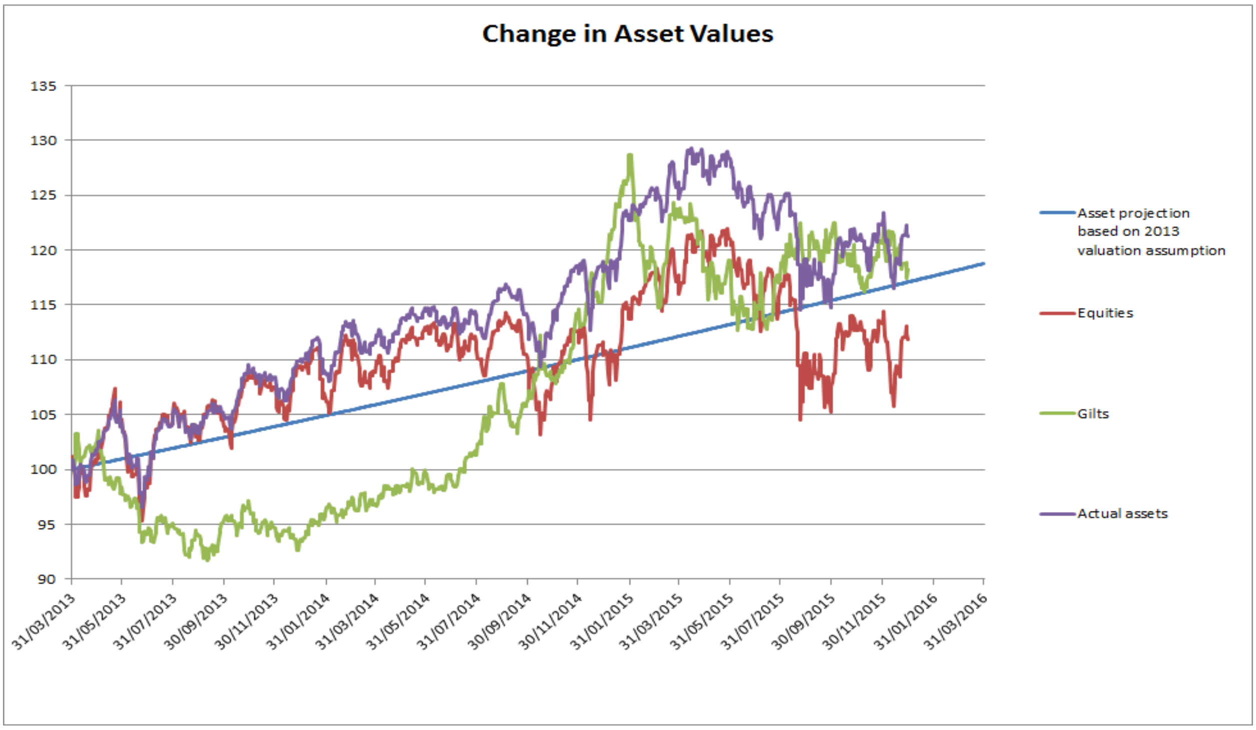
Assets

The estimated (unsmoothed) asset allocation of the City of Westminster Pension Fund as at 31 December 2015 is as follows:

Assets (Market Value)	31 December 2015		30 September 2015		31 March 2013	
	£000's	%	£000's	%	£000's	%
UK and Overseas Equities	769,808	72.7%	751,756	73.5%	643,179	73.6%
Bonds	137,443	13.0%	142,444	13.9%	111,092	12.7%
Property	104,783	9.9%	98,128	9.6%	35,787	4.1%
Gilts	26,706	2.5%	26,151	2.6%	49,821	5.7%
Cash and Accruals	20,868	2.0%	3,876	0.4%	34,303	3.9%
Total Assets	**1,059,608**	**100%**	**1,022,356**	**100%**	**874,182**	**100%**

The investment return achieved by the Fund's assets in market value terms for the quarter to 31 December 2015 is estimated to be 4.0%. The return achieved since the previous valuation is estimated to be 21.3% (which is equivalent to 7.3% p.a).

The following chart shows the changes in equity and bond markets since the previous actuarial valuation and compares them with the estimated actual fund returns and the expected fund returns assumed at the previous valuation:



As we can see the asset value as at 31 December 2015 in market value terms is slightly more than where it was projected to be at the previous valuation.

Changes in market conditions – market yields and discount rates

The actual investment returns earned by the Fund will affect the value of the Fund's assets. The value of the Fund's liabilities, however, is dependent on the assumptions used to value the future benefits payable. The following table show how these assumptions have changed since the last triennial valuation:

Assumptions (Smoothed)	31 December 2015		30 September 2015		31 March 2013	
	Nominal	Real	Nominal	Real	Nominal	Real
	%p.a.		%p.a.		%p.a.	
Pension Increases	2.64%	-	2.69%	-	2.74%	-
Salary Increases	4.44%	1.80%	4.49%	1.80%	4.54%	1.80%
Discount Rate						
Scheduled Bodies	6.12%	3.48%	6.06%	3.38%	5.90%	3.16%
Admission Bodies (in service)	4.81%	2.18%	4.79%	2.10%	4.90%	2.16%
Admission Bodies (left service)	2.99%	0.35%	3.00%	0.31%	3.50%	0.76%

Assumptions (Unsmoothed)	31 December 2015		30 September 2015		31 March 2013	
	Nominal	Real	Nominal	Real	Nominal	Real
	%p.a.		%p.a.		%p.a.	
Pension Increases	2.64%	-	2.59%	-	2.80%	-
Salary Increases	4.44%	1.80%	4.39%	1.80%	4.60%	1.80%
Discount Rate						
Scheduled Bodies	6.10%	3.47%	6.10%	3.51%	5.91%	3.11%
Admission Bodies (in service)	4.85%	2.21%	4.77%	2.18%	4.86%	2.06%
Admission Bodies (left service)	3.09%	0.46%	2.92%	0.33%	3.40%	0.59%

The key assumption which has the greatest impact on the valuation of liabilities is the real discount rate – the higher the real discount rate the lower the value of liabilities. As we see the real discount rates are broadly similar as at the 2013 valuation, maintaining the value of liabilities used for funding purposes.

Summary of results

The results of our assessment indicate that:

- the current projection of the smoothed funding level as at 31 December 2015 is 73% and the average required employer contribution would be 36.2% of payroll assuming the deficit is to be paid by 2038;
- the current projection of the unsmoothed funding level as at 31 December 2015 is 75% and the average required employer contribution would be 35.2% of payroll assuming the deficit is to be paid by 2038;
- this compares with the reported (smoothed) funding level of 74% and average required employer contribution of 29.8% of payroll at the 2013 funding valuation.

The discount rate underlying the smoothed funding level as at 31 December 2015 is 6.1% p.a. The investment return required to restore the funding level to 100% by 2038, without the employers paying deficit contributions, would be 7.5% p.a.

The funding position for each month since the formal valuation is shown in Appendix 1. It should be borne in mind that the nature of the calculations is approximate and so the results are only indicative of the underlying position.

We would be pleased to answer any questions arising from this report.

Graeme D Muir FFA

Partner

Appendix 1 Financial position since previous valuation

Below we show the financial position on both a smoothed and an unsmoothed basis for each month since the previous full valuation. As the smoothing adjustment reflects average market conditions spanning a six month period straddling the reporting date, the smoothed figures for the previous three months are projected numbers and likely to change up until three months after the reporting date.

Smoothed Valuation Date	Assets £000's	Liabilities £000's	Surplus/ Deficit £000's	Funding Level %	Final Salary Ongoing (% of Payroll)	CARE Ongoing Cost	Past Service Ctbn	Total Ctbn (% of payroll)	Main Discount Rate	Return required to restore funding level (pa)
March 2013	866,938	1,164,198	(297,260)	74%	14.3%	13.3%	16.5%	29.8%	5.9%	7.1%
April 2013	878,910	1,165,568	(286,658)	75%	14.3%	13.8%	13.1%	26.8%	5.9%	7.1%
May 2013	888,642	1,169,568	(280,926)	76%	14.2%	13.7%	12.9%	26.6%	5.9%	7.1%
June 2013	895,688	1,170,718	(275,030)	77%	14.1%	13.5%	12.7%	26.2%	6.0%	7.1%
July 2013	904,339	1,173,403	(269,063)	77%	14.0%	13.4%	12.5%	25.9%	6.0%	7.0%
August 2013	909,690	1,175,518	(265,828)	77%	13.9%	13.3%	12.4%	25.7%	6.0%	7.1%
September 2013	918,777	1,183,051	(264,274)	78%	13.9%	13.3%	12.3%	25.7%	6.0%	7.1%
October 2013	929,362	1,191,805	(262,443)	78%	13.9%	13.4%	12.3%	25.7%	6.0%	7.0%
November 2013	938,213	1,201,055	(262,842)	78%	13.9%	13.4%	12.3%	25.7%	6.0%	7.0%
December 2013	946,872	1,211,047	(264,176)	78%	14.0%	13.4%	12.4%	25.8%	6.0%	7.0%
January 2014	954,969	1,220,108	(265,139)	78%	13.9%	13.4%	14.1%	27.5%	6.0%	7.0%
February 2014	962,658	1,228,794	(266,137)	78%	13.9%	13.4%	14.3%	27.7%	6.0%	7.0%
March 2014	1,004,578	1,236,829	(232,251)	81%	13.9%	13.4%	14.4%	27.8%	6.0%	6.9%
April 2014	1,005,726	1,247,749	(242,023)	81%	-	13.4%	15.8%	29.2%	6.0%	6.9%
May 2014	1,007,188	1,258,014	(250,825)	80%	-	13.4%	16.3%	29.7%	5.9%	6.9%
June 2014	1,009,896	1,238,977	(229,081)	82%	-	12.8%	15.5%	28.3%	6.1%	7.0%
July 2014	1,009,337	1,256,980	(247,642)	80%	-	13.0%	15.2%	28.2%	6.1%	7.0%
August 2014	1,009,990	1,267,542	(257,552)	80%	-	13.0%	15.8%	28.8%	6.0%	7.0%
September 2014	1,009,471	1,277,558	(268,087)	79%	-	13.0%	16.4%	29.4%	6.0%	7.0%
October 2014	1,023,980	1,302,309	(278,329)	79%	-	13.2%	17.1%	30.4%	5.9%	7.0%
November 2014	1,034,712	1,316,533	(281,820)	79%	-	13.3%	17.7%	31.0%	5.9%	6.9%
December 2014	1,040,341	1,330,754	(290,413)	78%	-	13.4%	18.4%	31.8%	5.9%	6.9%
January 2015	1,078,282	1,357,915	(279,633)	79%	-	13.7%	17.5%	31.2%	5.8%	6.8%
February 2015	1,091,181	1,371,376	(280,195)	80%	-	13.8%	17.9%	31.7%	5.8%	6.7%
March 2015	1,104,985	1,374,723	(269,739)	80%	-	13.7%	17.6%	31.3%	5.8%	6.8%
April 2015	1,106,355	1,376,996	(270,640)	80%	-	13.6%	17.4%	31.0%	5.9%	6.9%
May 2015	1,105,768	1,385,201	(279,433)	80%	-	13.5%	17.8%	31.4%	6.0%	7.0%
June 2015	1,103,539	1,409,858	(306,319)	78%	-	13.9%	19.0%	32.8%	5.9%	7.0%
July 2015	1,075,885	1,399,015	(323,130)	77%	-	13.4%	19.9%	33.3%	6.0%	7.2%
August 2015	1,064,979	1,403,042	(338,062)	76%	-	13.3%	20.5%	33.8%	6.1%	7.3%
September 2015	1,052,607	1,415,081	(362,474)	74%	-	13.3%	21.6%	34.9%	6.1%	7.4%
October 2015	1,044,851	1,406,704	(361,853)	74%	-	13.0%	22.0%	34.9%	6.1%	7.5%
November 2015	1,038,650	1,407,484	(368,834)	74%	-	12.8%	22.6%	35.4%	6.2%	7.5%
December 2015	1,043,284	1,423,387	(380,103)	73%	-	12.9%	23.3%	36.2%	6.1%	7.5%

Unsmoothed Valuation Date	Assets £000's	Liabilities £000's	Surplus/ Deficit £000's	Funding Level %	Final Salary Ongoing (% of Payroll)	CARE Ongoing Cost	Past Service Ctbn	Total Ctbn (% of payroll)	Main Discount Rate	Return required to restore funding level (pa)
March 2013	874,182	1,175,148	(300,966)	74%	14.7%	13.6%	13.4%	27.0%	5.9%	7.1%
April 2013	886,487	1,186,870	(300,384)	75%	14.9%	13.8%	13.5%	27.3%	5.8%	7.0%
May 2013	901,919	1,182,756	(280,837)	76%	14.6%	13.5%	12.8%	26.2%	5.9%	7.0%
June 2013	862,959	1,138,024	(275,065)	76%	13.2%	13.5%	12.9%	26.4%	6.1%	7.2%
July 2013	911,592	1,173,707	(262,116)	78%	14.1%	13.5%	12.1%	25.6%	5.9%	6.9%
August 2013	897,984	1,162,093	(264,109)	77%	13.5%	13.3%	12.4%	25.7%	6.1%	7.2%
September 2013	910,261	1,176,348	(266,087)	77%	13.7%	13.3%	12.5%	25.8%	6.0%	7.0%
October 2013	944,904	1,208,939	(264,035)	78%	14.4%	13.2%	12.3%	25.5%	5.9%	6.9%
November 2013	939,772	1,206,750	(266,978)	78%	14.0%	13.4%	12.5%	25.9%	6.1%	7.1%
December 2013	953,407	1,212,836	(259,429)	79%	14.1%	13.4%	12.2%	25.6%	6.0%	7.0%
January 2014	940,435	1,213,328	(272,893)	78%	13.8%	13.4%	12.9%	26.3%	6.0%	7.0%
February 2014	979,617	1,231,045	(251,428)	80%	14.1%	13.4%	11.9%	25.3%	5.9%	6.9%
March 2014	994,420	1,226,711	(232,291)	81%	13.6%	13.2%	11.2%	24.5%	6.1%	7.0%
April 2014	1,009,341	1,247,964	(238,623)	81%	-	13.4%	15.7%	29.1%	6.0%	6.9%
May 2014	1,018,430	1,265,089	(246,660)	81%	-	13.6%	16.0%	29.5%	6.0%	6.9%
June 2014	1,005,898	1,245,649	(239,751)	81%	-	12.9%	15.8%	28.7%	6.1%	7.0%
July 2014	1,006,083	1,253,133	(247,050)	80%	-	12.9%	15.2%	28.1%	6.0%	7.0%
August 2014	1,032,413	1,288,597	(256,185)	80%	-	13.4%	15.7%	29.0%	5.9%	6.8%
September 2014	1,009,675	1,281,513	(271,838)	79%	-	13.0%	16.6%	29.6%	6.0%	7.0%
October 2014	1,013,601	1,293,450	(279,849)	78%	-	13.1%	17.2%	30.3%	6.0%	7.1%
November 2014	1,048,970	1,329,207	(280,237)	79%	-	13.6%	17.5%	31.1%	5.9%	6.9%
December 2014	1,047,254	1,339,010	(291,756)	78%	-	13.5%	18.5%	32.0%	5.8%	6.9%
January 2015	1,083,087	1,375,272	(292,185)	79%	-	14.0%	18.0%	32.0%	5.5%	6.5%
February 2015	1,107,211	1,377,004	(269,793)	80%	-	14.0%	17.1%	31.1%	5.7%	6.6%
March 2015	1,098,972	1,372,946	(273,974)	80%	-	13.6%	17.5%	31.1%	5.8%	6.8%
April 2015	1,118,105	1,391,869	(273,764)	80%	-	13.9%	17.5%	31.4%	5.9%	6.9%
May 2015	1,129,075	1,399,817	(270,742)	81%	-	13.8%	17.4%	31.2%	5.9%	6.9%
June 2015	1,071,652	1,383,734	(312,083)	77%	-	13.3%	19.4%	32.7%	6.1%	7.2%
July 2015	1,092,998	1,412,427	(319,429)	77%	-	13.7%	19.6%	33.3%	6.0%	7.1%
August 2015	1,045,267	1,390,462	(345,195)	75%	-	13.0%	21.0%	34.0%	6.1%	7.4%
September 2015	1,022,356	1,391,477	(369,121)	73%	-	12.8%	22.1%	35.0%	6.1%	7.5%
October 2015	1,058,388	1,416,073	(357,685)	75%	-	13.2%	21.7%	34.9%	6.1%	7.4%
November 2015	1,069,435	1,424,526	(355,091)	75%	-	13.1%	21.8%	35.0%	6.1%	7.4%
December 2015	1,059,608	1,418,732	(359,124)	75%	-	12.9%	22.3%	35.2%	6.1%	7.4%

City of Westminster

Pension Fund Committee

Date:	**22 March 2016**
Classification:	**General Release**
Title:	**Pension Fund Benchmarking Costs**
Report of:	**Steven Mair** ***City Treasurer***
Wards Involved:	**All**
Policy Context:	**Effective Control over Council Activities**
Financial Summary:	**There are no financial implications arising from this report**

1. Executive Summary

1.1 This report advises the Pension Fund Committee of the current position with regard to performance benchmarking of the Fund and in particular the Scheme Advisory Board Key Performance Indicator (KPI) Benchmarking exercise.

2. Key Matters for the Committee

2.1 The Committee note the contents of this paper

3. Background

3.1 At the 19 October 2015 meeting of the Westminster Local Pension Board members asked for more information on the benchmarking arrangements for the Funds' investments and costs.

3.2 This report covers:

- the response to the Scheme Advisory Board KPI Benchmarking exercise;
- Investment performance benchmarking; and
- A comparative review of the fund's management costs.

4. Scheme Advisory Board KPIs

4.1 As part of its work over the last two years the LGPS Scheme Advisory Board (in shadow prior to April 2015) has sought to improve the quality and comparability of data associated with the LGPS following criticism from the Hutton Commission Final Report in 2012.

4.2 There has also been considerable discussion around the ability to identify and compare the financial health of individual LGPS Funds. This led to the establishment of a working party which was tasked with creating a range of meaningful performance indicators to show those funds who were in a stronger or weaker position. This assessment is not necessarily a reflection of the current governance and administration arrangements but will highlight where improvements are required following decisions made over a number of years.

4.3 The Guidance issued by Scheme Advisory Board which sets out the rationale for the exercise and explains the range of KPIs was reported to the last meeting in September 2015. The KPIs are split into 4 core and 14 supplementary indicators where the core KPIs are classed as “alarm bells” to identify under-performing funds. It should be noted that no one single indicator is pre-eminent – the assessment is one which is “taken in the round” using the whole basket of KPIs to form an overall picture of each fund’s relative performance compared to its peers.

4.4 Officers have completed the KPI Proforma attached at Appendix 1 which was reported to the Pension Fund Committee meeting in November 2015.

4.5 A summary of all responses is expected in early 2016 and those funds identified with significant issues are likely to be contacted directly regarding establishing an action plan to make the necessary improvements.

5. Investment Performance Benchmarking

5.1 The Pension Fund Committee receive reports every quarter which analyse the investment performance between asset classes, fund managers and various time periods all against pre-determined benchmarks. These benchmarks are largely market related i.e. FTSE indices and give an indication of the success of the investment strategy and individual mandates/fund managers.

5.2 Due to the long term nature of the Fund’s liabilities the Pension Fund Committee is able to take a long term approach in its investment strategy and will make strategic allocations to different asset classes such as equities and bonds based upon the expected returns and risk appetite and will have less regard for short-term market fluctuations.

5.3 Table 1 below shows the Fund's investment returns at March 2015 over one and three year periods and compares them to the benchmark target. Overall the fund has out-performed the benchmark target and individual managers have either out-performed or met their benchmark targets.

Fund Manager	Asset Type	Value at 31/03/15	Asset allocation 31/03/15	One Year Net Return	One Year Benchmark	Three Year Annualised Net Return	Three Year Annualised Benchmark
		£m	**%**	**%**	**%**	**%**	**%**
Majedie	UK Equity	£256.5	23.5	6.9	6.6	16.0	10.6
Legal & General	Passive Global Equity	£277.3	25.4	13.7	13.9	n/a	n/a
Baillie Gifford	Global Equity	£179.2	16.4	18.9	19.0	n/a	n/a
Longview	Global Equity	£109.6	10.0	n/a	n/a	n/a	n/a
Insight	Index Linked Gilts	£17.9	1.7	6.6	6.8	2.6	2.7
Insight	Bonds	£156.6	14.4	9.8	9.8	8.1	7.5
Hermes	Property	£45.7	4.2	19.1	16.9	12.1	9.5
Standard Life	Property	£47.9	4.4	9.4	16.2	n/a	n/a
TOTAL		**£1,090.7**	**100.0**	**12.5**	**12.9**	**13.3**	**12.0**

Table 1: Westminster Pension Fund Investment Returns

5.4 In order to better understand the performance of the fund relative to other LGPS funds, officers have recently subscribed to the WM Local Authority Performance League tables. These tables are produced annually and provide comparisons on the level of returns across asset classes as well as overall returns achieved by individual funds. The results from the 2014/15 Local Authority Universe are shown at Appendix 2. These show that whilst the one year performance of the fund was slightly below the LGPS average of 13.2%, it slightly exceeded the three year annualised average of 12.9%.

5.5 Whilst there may well be particular circumstances which determine individual fund returns, such as level of risk taken, this remains a helpful indication of where an individual fund's returns sit when compared to their peers and the overall range of results achieved. It also provides an insight into the drivers for success such as the investment strategy adopted and the success or otherwise of particular fund managers.

5.6 Compiling data from almost all LGPS Funds also provides the opportunity to carry out wider analysis and hence the ability to draw out specific conclusions. Each year an Annual Review of Local Authority Funds is produced which discusses a range of topical issues in relation to LGPS investments such as asset allocation, individual asset classes and comparisons to corporate funds.

5.7 Data has now been submitted to WM Company in respect of investment returns in 2015/16 and further updates will be reported to the Pension Fund Committee in due course.

6. Fund Management Costs

6.1 The focus on the costs of operating the LGPS has increased significantly over recent years with a number of commentators offering views on the comparability and potential savings that could be achieved through greater collaboration. In particular Michael Jonson at the Centre for Policy Studies (CPS) has recently published a report titled LGPS: Unsustainable : http://www.cps.org.uk/files/reports/original/151215155124-LGPSUnsustainable.pdf

6.2 The management costs for the Westminster Pension Fund have been analysed over the last 5 years and this is included at Appendix 3 (exempt). It is important to note there have been a number of changes during the period which limit the comparability of the figures such as changes in investment strategy and fund managers.

6.3 For the first time in 2014/15 CIPFA introduced guidance on accounting for the costs of running pension funds. This included reporting transaction costs in the accounts for the first time (transaction costs are costs associated with the purchase and sale of assets such as stamp duty and Broker commissions). As these costs exceed £1M pa the annual reported costs have increased significantly from 2013/14 onwards.

6.4 In order to provide some perspective to these figures and to consider how the Fund compares to other LGPS Funds an independent consultant has carried out a review of management costs. This highlights the degree of compliance with the CIPFA Guidance and shows how Westminster Pension Fund compares across a number of categories. This analysis is included at Appendix 4.

6.5 The analysis has been prepared in the context of the CPS report mentioned above and seeks to clarify some of the points raised and challenges a number of the conclusions drawn. In particular, the new CIPFA guidance and the inclusion of transaction costs is an attempt to improve the transparency around costs but has been interpreted as an increase in costs which is simply not the case.

6.6 Clearly the size of the Pension Fund will have a major influence on the costs as a percentage of assets and as Westminster is a smaller Fund this will result in a higher figure. In addition, the choice and number of fund managers will have a significant impact and needs to be considered alongside the investment returns achieved.

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

David Hodgkinson, Assistant City Treasurer

Email: dhodgkinson@westminster.gov.uk

Telephone: 020 7641 8162

BACKGROUND PAPERS:

None

APPENDIX 1:

Westminster Response to the Scheme Advisory Board KPI Exercise

APPENDIX 2:
WM UK Local Authority Universe Results 2014/15

LOCAL AUTHORITY

ANNUAL 2014/2015

The following summary is based on 85 funds with a total Market Value of £199,896m.

FINAL RESULTS

CATEGORY	ASSET MIX (%)		RETURNS (%)					
	Latest Year		Last 12 Months		3 Year Annualised		5 Year Annualised	
	31/03/2014	31/03/2015	Average	Index	Average	Index	Average	Index
TOTAL EQUITIES	63.1	61.5	13.7	19.2	13.2	14.2	9.6	10.0
GLOBAL POOLED INC UK	5.9	7.0	18.3	19.2	14.3	14.2	-	10.0
UK EQUITIES	24.3	21.2	6.3	6.6	11.7	10.6	9.4	8.3
OVERSEAS EQUITIES	32.9	33.3	18.1	20.7	13.8	14.8	9.5	10.3
North America	11.7	8.2	24.8	25.1	18.4	18.1	14.0	14.0
Europe	8.6	6.3	8.8	7.7	14.6	14.2	8.2	7.2
Japan	3.1	2.9	27.3	27.1	13.9	12.7	8.4	6.7
Pacific (ex Japan)	3.2	2.8	16.0	10.6	8.7	7.2	7.1	6.1
Emerging Markets	5.4	3.8	13.5	16.3	6.0	3.7	4.1	2.7
Global ex UK	1.0	9.3	19.2	20.7	16.0	14.8	11.3	10.3
TOTAL BONDS	16.4	17.1	13.0	-	7.1	-	7.9	-
U.K. BONDS	9.3	9.2	11.8	13.9	7.5	5.3	7.9	7.0
OVERSEAS BONDS	2.4	2.3	8.7	8.4	3.9	4.9	4.3	4.8
INDEX LINKED	3.7	4.2	20.2	18.5	8.5	7.9	10.3	9.6
POOLED BONDS	0.9	1.3	7.6	-	5.5	-	5.8	-
TOTAL CASH	2.9	2.7	1.8	0.3	2.0	0.4	1.8	0.4
ALTERNATIVES	7.0	7.9	12.5	-	8.6	-	7.0	-
Total Private Equity	3.8	4.3	15.7	-	10.9	-	9.6	-
Total Hedge Funds	2.0	2.2	8.6	-	6.5	-	4.9	-
Other Alternatives	1.2	1.4	9.5	-	4.8	-	3.3	-
POOLED MULTI ASSET	3.1	2.8	10.2	-	-	-	-	-
TOTAL EX-PROPERTY	92.6	91.9	13.0	12.5	11.2	10.6	8.8	8.1
TOTAL PROPERTY	7.4	8.1	15.8	18.3	9.7	11.4	8.9	10.3
TOTAL ASSETS	100.0	100.0	13.2	12.9	11.0	10.6	8.7	8.2

APPENDIX 4:

External Analysis of LGPS Management Costs 2014/15

Worth Technical Accounting Solutions Response to CPS Report *LGPS: Unsustainable*

1. The analysis prepared by Michael Johnson is based on the DCLG's data rather than the published accounts for 2014/15. During 2014/15 CIPFA issued new guidance on accounting for the costs of running pension funds. The guidance required:

    a. All transaction costs to be reported gross (hitherto these have tended to be netted off purchases and sales)
    b. Report all management fees (i.e. *ad valorem* fees, performance fees and custody fees) gross rather than net these off purchases and sales
    c. Disclose costs over three categories of expense:
        i. Administration
        ii. Investment management
        iii. Oversight and governance (new category for 2014/15)

2. The guidance was not fully implemented by all pension funds. Nationally only about half the pension fund across England, Scotland and Wales complied with the guidance and within London, less than half of all pension funds fully implemented the guidance. Therefore any inter-fund comparison is probably flawed. Michael Johnson's analysis does not reflect this.

	London pension funds			National position	
	No.	%		No.	%
Fully complied	14	43%		51	52%
Partly complied	6	19%		16	16%
Did not comply	12	38%		31	32%
	32	100%		98	100%

3. Westminster Pension Fund fully implemented the CIPFA guidance in 2014/15.

Restating 2013/14

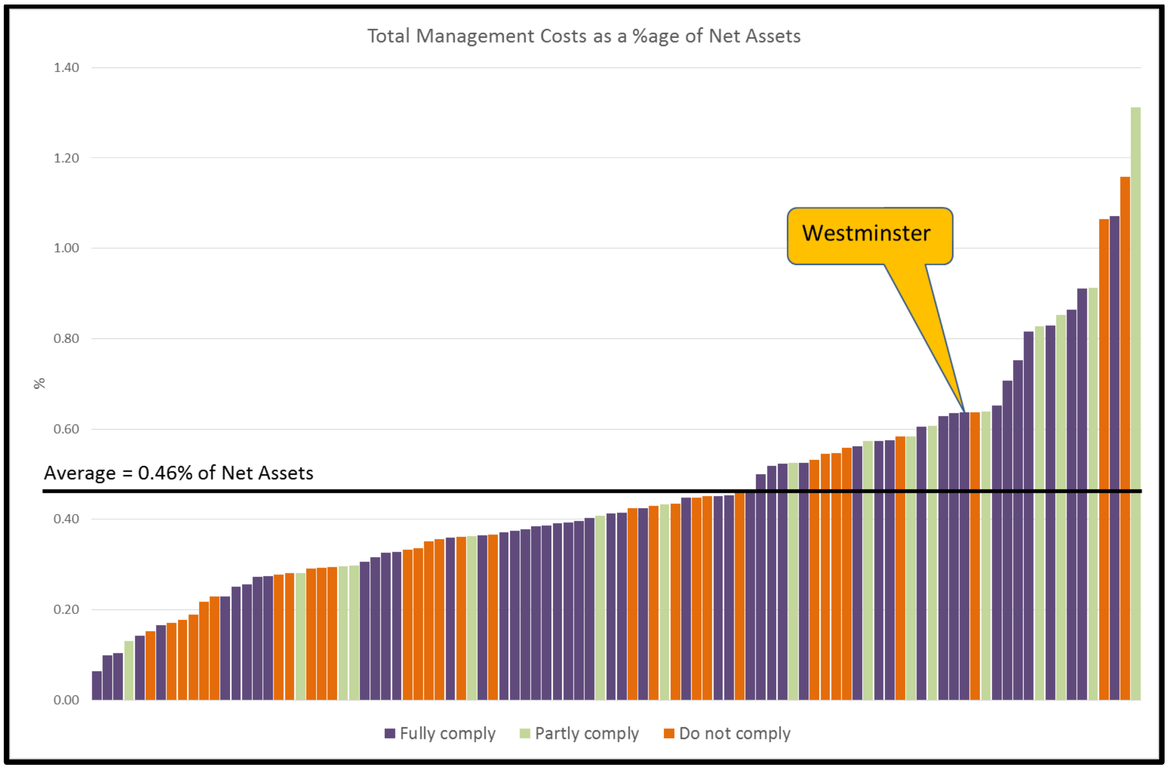
4. Michael Johnson states that the cost of running LG pension funds has risen by 40%. His analysis is based on the data reported on the DCLG website. The pension funds which fully implemented the CIPFA guidance also restated the comparator financial information for 2013/14 to ensure consistency of reporting – the DCLG data for 2013/14 has not been restated.

5. Just looking at the authorities who fully implemented the CIPFA guidance, total management costs rose by 29% rather than 40%.

6. Additionally a significant number of LG pension funds have active pension fund management mandates with some fund managers. These are designed to out-perform the market. The reward for fund managers under active mandates is a performance fee on top of the basic *ad valorem* fee. Performance fees are inherently volatile between years. Overall 2014/15 was a good year compared with 2013/14 so part of the 29% increase is due to performance fees.

Total management costs

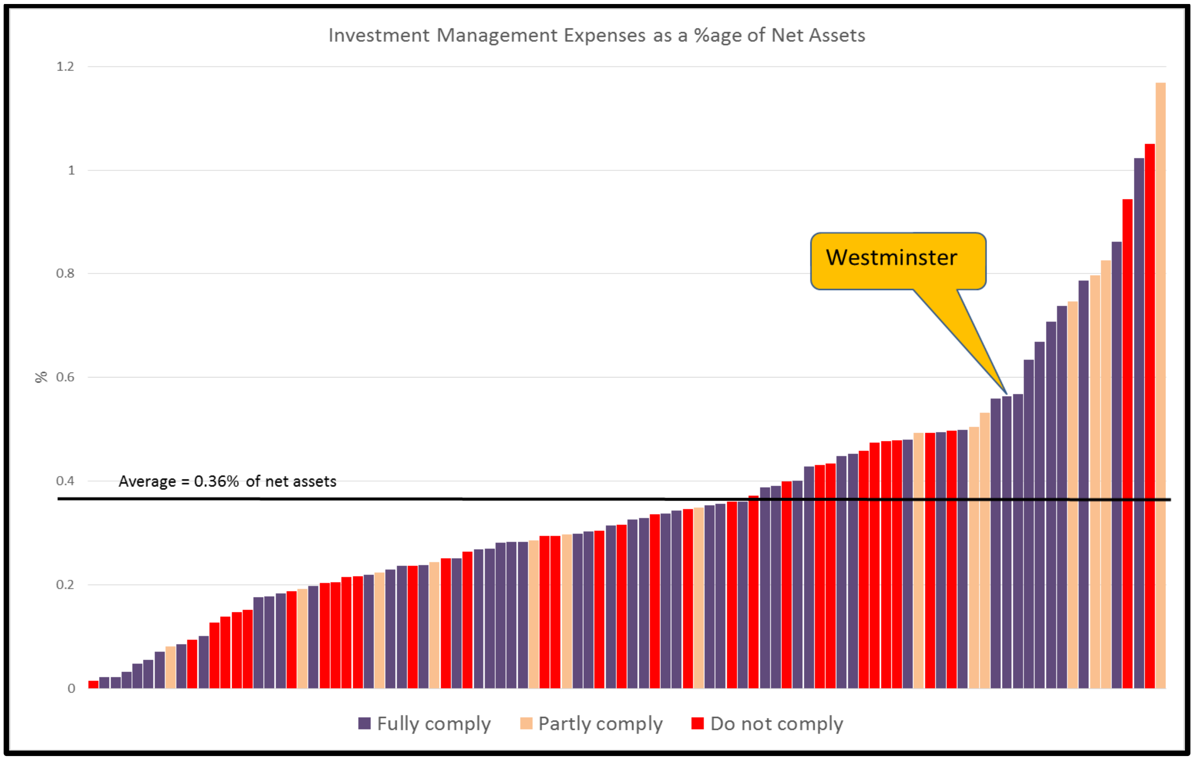
7. The average total management costs for a LG pension fund were 0.46% of net assets. Westminster pension fund was above average at 0.64% of total net assets – see graph below. The difference of 0.18% is around £1.9m. To a large extent this reflects that investment management expenses are higher than the average- see next section.



Investment management expenses

8. The average total investment management costs for a LG pension fund were 0.36% of net assets. Westminster pension fund was above average at 0.56% of total net assets –see graph below. However this compares favourably against pension funds in the private sector where investment management fees are in the range 0.75 to 1.25%.

9. The difference of 0.20% equates to around £2.2m of net assets.



10. Westminster's Pension Fund's above average costs reflect that the pension fund paid around £2.2m in performance fees to one fund manager to reward out-performance.

11. Given that overall management costs are 0.18% above average, but investment management expenses are 0.2% above average, this means that the pension fund's administration and oversight and governance costs are below average.

No.	Key Indicator	Examples of level for concern	Examples of good practice for high performing fund	Fund score	Evidence and comments	Links
1	Risk management	No or only a partial and/or an unclear risk register with no or poorly specified or un-implemented mitigation actions over time leading to increased fund risk.	Comprehensive risk register covering the key risks (in accordance with current CIPFA guidelines) with prioritisation, robust mitigation actions, defined deadlines, with action tracking to completion.			
		No evidence of a risk register being	Evidence and e-links to demonstrate			
		a) prioritised	a) risks prioritised on a RAG red, amber, green or by a scoring methodology	1	Risk Register in place - implemented May 2015	http://committees.westminster.gov.uk/documents/s13403/Pension%20Risk%20Register%20WCC%20draft%20150416.pdf
		b) annually reviewed by Pensions Committee	b) completed actions signed off by Pensions Committee after at least annual update,	0	Reviewed quarterly by Committee, not yet been in place for a year.	
		c) annually reviewed by internal audit or external audit	c) annual review by internal audit and external audit	-1	Not yet been reviewed by Internal Audit	
		d) used to reduce high risks	d) <3 priority/"red" risks	1	No red risks to date	
		e) available for public scrutiny.	e) public disclosure of a summary version published on fund website or in fund annual report.	0	As per links above, register is available as part of public Committee papers on Council's website. Most recent version published for September Meeting. Not included in 2014/15 Annual Report.	http://committees.westminster.gov.uk/documents/s15237/Fund%20Financial%20Management%20Apx%202.pdf
		Self score -1 point for each one	Self score +1 point for each one			
2	Funding level and contributions	a) Decreasing funding level (calculated on a standardised and consistent basis) and/or in bottom decile of LGPS, over the last three triennial valuations on a standardised like for like basis.	Evidence and e-links to demonstrate			
	(see explanatory notes)	b) No or minimal employer funding risk assessment and monitoring and not reported to Pensions Committee	a) Funding level rising and getting closer to 100% funded (or above) over last three triennial valuations on a standardised like for like basis. Funding %		Funding level 78% on standardised basis at 2013. 74% as reported to Fund in TV, 74% in 2010 and 79% in 2007	http://transact.westminster.gov.uk/Newdocstores/publications_store/Pensions/westminster-valuation-report-2013.pdf
		c) Total actual contributions and actual received in last 6 years less than that assumed and certified in last 2 triennial valuations.	91 to >100 =score +5			
		d) Net inward cash flow less than benefit outgoings so need for any unplanned or forced sale of assets.	80-90 =+4			
		Self score -1 for each one	70-79 =+3	3		
			60-69 = +2			
			<59 = +1			
			b) Employer funding risk assessment and monitoring reports to Pension Committee. Net inward cashflow forecasts meeting planned income or significantly exceeding benefot outgoings.	-1		
			c) Total actual contributions received in last 6 years equate to (or exceed) that assumed and certified in the last 2 triennial valuations.	1	two lump sum deficit payments received totalling £97m over the period	
			d) Net inward cash flow significantly exceeds benefit out-goings	-1	Cash flow monitored by officers and reported quarterly to Committee	http://committees.westminster.gov.uk/documents/s15236/Fund%20Financial%20Management%20Apx%201.pdf
			Self score a) as above and rest +1 for each one			
3	Deficit recovery	a) No or opaque deficit recovery plan.	Evidence and e-links to demonstrate :			
	(see explanatory notes)	b) Lengthening implied deficit recovery period (for contributions)	a)Transparent deficit recovery plan for tax raising and non-tax raising bodies.	1	See Funding Strategy Statement	http://transact.westminster.gov.uk/Newdocstores/publications_store/Finance/pension_funding_strategy.pdf
		c) Implied deficit recovery periods >25 years for last 3 valuations.	b) Implied deficit recovery reducing each triennial valuation.	1	30 years at 2010 reduced to 25 years in 2013	http://transact.westminster.gov.uk/Newdocstores/publications_store/Pensions/westminster-valuation-report-2013.pdf
		Self score -1 point for each	c) Implied deficit recovery period in line <15 years for last 3 valuations	-1	30 years at 2007	
			Self score +1 point for each one			
4	Investment returns	a) Required future investment return (calculated on standardised and prudently consistent basis) not aligned to the investment strategy target return, so lower likelihood of the fund achieving its funding strategy.	Evidence and e-links to demonstrate :			
	(see explanatory notes)	b) Actual investment returns consistently undershoot actuarially required returns	a) Required future fund investment return (calc by actuary) are consistent with and aligned to investment strategy (asset mix expected target returns) so higher likelihood of the fund meeting its funding strategy.	1	Rate of return expected from Investment Strategy in line with Actuarial assumptions - see Statement of Investment Principles	http://transact.westminster.gov.uk/docstores/publications_store/pensions/westminster_sip_2015.pdf
		Self score -1 point for each one	b) Actual investment returns consistently exceed actuarially required returns	1	Returns at 2013 Valaution of 7.9% exceeded expected figure of 7.5%. Three year annualsied returns to March 2015 of 13.3% in excess of actuarial required rate of return of 7.1%	http://committees.westminster.gov.uk/documents/s13398/2015%20Q1%20Performance%20Rpt%20-%20Deloittes%20vf.pdf
			Self score +1 point for each one			

No.	Key Indicator	Examples of level for concern	Examples of good practice for high performing funds	Fund score	Evidence and comments	Links
5	Pensions Committee and Pensions Board members competence	Appointees unclear of statutory role and unable to clearly articulate the funds funding and investment objectives. No evidence of a) different scheme employer types and no or minimal scheme member representation. b) No training needs analysis, or training strategy, or training log or use of CIPFA LGPS training framework. c) No training record disclosures d) Self assessment Self score core -1 point for each	Appointees understand their statutory role and are able to clearly articulate the funds funding and investment objectives Evidence and e-links to demonstrate a) representation from different scheme employer types (scheduled and admitted) and member types (actives, deferred and pensioners). b) annual training plan recorded against the CIPFA knowledge and understanding framework. c) annual training records disclosed in Annual Report d) annual self-assessment of training undertaken and identification of future needs. Self score +1 point for each one	0 0 -1 -1	Only one scheduled body on Board and two active/one pensioner representative. No other employer representation on Committee Knowledge & Skills Policy agreed in September 2015 None in place by 31 March 2015 None in place by 31 March 2015	http://committees.westminster.gov.uk/documents/s15232/Governance%20Arrangements%20Apx%201.pdf
6	Administering authority staff accountability, leadership, experience, and training	a) No or only part time Head of Fund and or only part time officers b) No or little induction or on- going training provision or experience recorded on the adoption of CIPFA LGPS knowledge and understanding framework. Self score -1 for each one	Evidence and e-links to demonstrate a) Experienced Head of Fund with full time dedicated officers with at least 3+ years' experience. b) staff undertake regular CIPFA LGPS TKU or other CPD training recorded across all LGPS skills (governance, benefits administration, funding, investments, and comms) Self score +1 point for each one	0 0	Shared Head of Fund across three tri-borough funds Training undertaken through attendance at various seminars - no formal records due to lack of formal appraisal process	
7	Statutory governance standards and principles (as per DCLG guidance and TPR codes)	Several key areas of non- compliance with a) DCLG LGPS statutory guidance b) TPR guidance and codes and reasons why not explained. c) No, little or poor key decision taking records and no or poor self, or scheme employers, or scheme members assessment of overall fund effectiveness. Self core -1 for each one	Evidence and e-links to demonstrate a) Full compliance with DCLG LGPS statutory guidance b) Full compliance with TPR guidance and codes for public sector pension schemes c) Meet or exceed other LGPS best practice on recording all key decision taking and annual self, scheme employers, scheme member assessment of overall effectiveness. Self score +1 for each one	0 0 0	Representation only area of non-compliance. Link: Partially compliant - Board papers show conflict of interest, training and code of conduct policies in place Link: Committee Decisions clearly recorded - no assessments of effectiveness Link to Committee minutes:	http://committees.westminster.gov.uk/documents/s15233/Governance%20Arrangements%20Apx%202.pdf https://www.westminster.gov.uk/council-pension-fund http://committees.westminster.gov.uk/mgCommitteeDetails.aspx?ID=321
8	Quality and accessibility of information and statutory statements, strategies, policies (governance, FSS, SIP, comms, admin authority and employer discretions policies)	a) Statutory publications not all in place or published on fund website or updated in accordance with regulatory requirements and due timelines. b) Fund and employers discretions not published c) Do not seek to meet any recognised 'Plain English' or e-publishing standards Self score -1 for each one	Evidence and e-links to demonstrate a) Statutory publications all in place and published on fund website and updated in accordance with regulatory requirements and due timelines. b) Fund and employer discretions pubished c) Meet 'Plain English' and or other recognised e-publishing standards. Self score +1 for each one	1 1 -1	Statutory publications published. Link to website: Contained within the WCC pensions poilcies found on the internal WCC knowledge base Do not seek to meet plain english standards	https://www.westminster.gov.uk/council-pension-fund https://btlg.service-now.com/LFSharedServices/pft_wcc.do
9	a) Adoption and report compliance with Investment Governance Principles (IGP) (was Myners Principles) and voluntary adoption/signatory to FRC Stewardship Code and UNPRI	No or un-explained non- compliance and/or non-support of a) IGP b) UK Stewardship Code c) UN PRI Self score -1 for each	Evidence and e-links to demonstrate a) 100% compliance with IGP b) adoption and public reporting of compliance against the FRC UK Stewardship Code c) external managers or fund are PRI signatories Self score +1 for each	0 0 0	Compliant with all except assessment of own effectiveness Stewardship Policy approved in September 2015 and included in 2014/15 Annual Report All except one fund managers are signatories	http://transact.westminster.gov.uk/docstores/publications_store/pensions/westminster_sip_2015.pdf https://www.westminster.gov.uk/council-pension-fund http://www.unpri.org/signatories/signatories/#investment_managers
10	a) Historic investment returns (last 1, 3, 5, and 10 years) and b) total investment costs compared to other LGPS funds. (See explanatory notes)	a) overall fund investment returns (net of fees) for last 1, 3, 5 years bottom two quintiles Score -3 and -5 points b) Retain fund managers under- performing their mandates for 2 triennial valuation cycles. Score -1 point c) Fund does not benchmark its fund manager and total investment costs relative to other LGPS funds. Score -1 point	Evidence and e-links to a) overall fund investment return (net of fees) for last 1, 3, 5 years a) Top quintile score +5 points b) Next two quintiles score +3 and 0 points respectively b) >75% of fund mandates deliver over rolling 3 year performance periods. Score +1 point c) Fund benchmarks its fund manager and total investment costs Score +1	-3 0 -1	only 1 year data available. Position 66 All managers with 3 year record ahead of targets but only covers 40% of assets. Other managers replaced in 2015 Do not benchmark against other LGPS funds	http://committees.westminster.gov.uk/documents/s13398/2015%20Q1%20Performance%20Rpt%20-%20Deloittes%20vf.pdf
11	Annual report and audited financial statements	a) Do not fully meet some regulatory requirements or CIPFA LGPS guidance b) Not published in Admin Authority Accounts by 1st October. c) Published on SAB website after 1st November Self score -1 for each one	Evidence and e-links to demonstrate a) Meet all regulatory and CIPFA best practice guidance b) Publish in Administering Authority accounts by 1st October c) Publish fund report and accounts of SAB website before 1st November. Self score +1 for each one	1 1 1	Meet all regulatory requirements and CIPFA best practice Pension Fund Accounts published in Administering Authority accounts within timescale On website	http://transact.westminster.gov.uk/docstores/publications_store/accounts/6.51_wcc_pensions_fund_report_2014_interactive_v2.pdf
12	Scheme membership data	a) Common data does not meet TPR standards b) Conditional data do not meet the TPR standards. No plans in place to rectify this. Self score -1 for each	Evidence and e-links to demonstrate a) >99% common data meets TPR quality and due date standards b) >95% of conditional data meets TPR quality and due date standards. Plans in place to improve this. Self score +1 for each one	0 0	Awaiting for the data to be updated via the new payroll/pensions interface Awaiting for the data to be updated via the new payroll/pensions interface	
13	Pension queries, pension payments, and Annual Benefit Statements	a) No or poor website with no scheme member or employer access. b) ABS do not meet regulatory requirements or due timelines for issuance. Self score -1 for each	Evidence and e-links to demonstrate a) Good website with interactive scheme member and employer access. b) ABS meet or exceed regulatory standards and due timelines for issuance. Self score +1 for each	1 1	Website in place ABS meet standards	http://www.wccpensionfund.co.uk/
14	Cost efficient administration and overall VFM fund management	a) In bottom quartile with high total admin cost pa per member (based CIPFA or other benchmark tool). b) Not in any national or regional frameworks for any externally procured services or collective investments. Self score -1 for each	Evidence and e-links to demonstrate a) In top quartile with low total admin cost pa per fund member (based CIPFA or other benchmark tool calculated on a consistent and transparent basis). b) Lead and/or actively participates in collaborative working and collective LGPS procurement, shared services or CIVs Self score +1 for each	0 1	Needs to be remeasured in 15/16 Council is a CIV shareholder. Actuarial national LGPS framework used in 2015, custody in 2014.	
15	Handling of formal complaints and IDRPs	a) Any Pensions Ombudsman determinations (and any appeals) fines were against the actions of the fund (ie not employer). Score -1	Evidence and e-links to demonstrate a) No Stage 2 IDRPs and no Pensions Ombudsman findings <u>against the fund</u> actions in last 3 years. Score +1	1	Clear IDRP process in place and strong evidence of application	http://www.wccpensionfund.co.uk/
16	Fraud prevention	No or minimal systems/programme or plan or mechanisms in place to a) Prevent fraud b) Detect fraud c) detect pension over-payments due to unreported deaths Self score -1 for each one	Evidence and e-links to demonstrate a) Fraud prevention programme in place. b) Use external monthly, quarterly/annual mortality screening services, and c) participate in bi-annual National Fraud Initiative. Self score +1 for each one	0 0 1	Currently obtaining costings and reviewing options Currently obtaining costings and reviewing options Participation confirmed	
17	Internal and external audit	a) No annual internal audit or qualified internal and external audit opinions b) Urgent management action recommended on high/serious risks. c) Only moderate or low level of assurance and a number of high priority action recommended Self score -1 for each	Evidence and e-links to demonstrate a) Unqualified annual internal reports with no or only low priority management actions b) Unqualified and annual external audit with no or only low priority management recommendations. c) Full or substantial assurance against all key audit areas with no high risk recommendations. Self score +1 for each	0 1 1	One medium priority action in last internal audit report Unqualified external audit report with no recommendations. Page 40 of Annual Report Unqualified external audit report with no recommendations.	http://transact.westminster.gov.uk/docstores/publications_store/accounts/6.51_wcc_pensions_fund_report_2014_interactive_v2.pdf
18	Quality assurance	No evidence of a) quality management system b) external reviewed publications c) externally approved website accessibility d) any awards. Self score -1 for each one	Evidence and e-links to demonstrate a) Fund has formal quality management external certification b) Crystal Mark for plain English for publications/forms c) externally approved website accessibility d) pensions & investment recognition award(s) Self score +1 for each one	0 -1 -1 -1	Surrey County Council have internal QA system in place No crystal mark for plain english No external approval for website No awards received	

City of Westminster

Pension Fund Committee

Date:	**22nd March 2016**
Classification:	**General Release**
Title:	**Analysis of the 2014/15 pension administration costs**
Report of:	**Director of Human Resources**
Financial Summary:	**The costs of the out-sourced pensions administration service were higher than expected in 2014/15, because of one-off costs migrating data from the LPFA to Surrey CC and because the start of the new arrangement was postponed by five months to 1 September 2015.**
Report Author and Contact Details:	**Trevor Webster 0207 641 2803**

1. Executive Summary

1.1 At the 16th November 2015 meeting, the Pension Fund Committee requested a breakdown of the 14/15 pension administration costs.

1.2 This report summarises the costs for each type of expenditure in the context that 14/15 was the financial year that the pensions administration contract was awarded to Surrey County Council from the LPFA and there were expected migration and start-up costs to absorb.

2. Recommendation

2.1 That the Committee notes the content of the report.

3. Background

3.1 Westminster City Council (WCC) first outsourced its pension administration service to the London Pensions Fund Authority (LPFA) in April 1992. The service remained with LPFA through various procurement exercises until 2014.

3.2 The contract was re-tendered but as a s.101 agreement and Surrey CC were successful

3.3 The initial cost of the Surrey s.101 agreement was £227k for 2014/15 representing a £17k (7%) annual saving on the previous contract with LPFA which cost £245k in 2013/14.

3.4 It should be noted that the difference between a contract and a s.101 agreement is that a section 101 agreement provides greater control over the costs of pension administration, because the costs of the services are transparent to both parties and the fee agreed is on a *not for profit* basis.

4. Analysis

4.1 The costs incurred in 2014/15 were £373k compared with the s.101 agreement sum of £227k and explained in Table 1 below.

4.2 The additional cost was due to:

- One-off start-up costs arising from the data migration of £73k;
- Licence fees payable to Heywards for the administration system which straddled two financial years;
- Offset by the saving in fees payable to LPFA and Surrey CC of £27k. The saving would have been £80k for a full year, but the start of the s.101 agreement was delayed from 1 April 2014 to 1 September 2014 to avoid clashing with the start date for the MSP project which was originally due to go live also on 1 April 2014.

Table 1

		£000s	**£000s**
	Original s.101 agreement sum		227
LESS	Saving in fees payable to Surrey CC due to delayed start		(130)
ADD	Additional fees payable to LPFA to extend the contract to 31 August 2014		103
ADD	One-off start-up costs:		
	Data migration	17	
	Fee payable to Heywards to transfer licence from LPFA to Surrey CC	50	
	Miscellaneous	6	
			73
ADD	Heyward licence fee payable for 2014/15		47
	True cost for 2014/15		**320**
	Heyward licence fee prepaid for 2015/16 to 30 November 2015		53
	Total cost		**373**

5 Financial Implications

5.1 It is expected that the cost of administration will reduce as there should be no further one-off costs.

6. Legal Implications

6.1 None

.
If you have any questions about this report, or wish to inspect one of the background papers, please contact:
Trevor Webster Tel: 0207 641 2803

This page is intentionally left blank