Pension Fund Committee
Meeting to be held on Friday, 23 March 2018

Electoral Division affected: None;

Lancashire County Pension Fund
December 2017 Budget monitoring report
(Appendix 'A' refers)

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Executive Summary

This report sets out the income and expenditure of the Fund for the period 1st April to 31st December 2017 with comparison to the budget for the same period and includes a full year forecast with comparison for the full year budget to 31 March 2018.

Recommendations

1. The Committee is asked to consider and note the analysis of variances between actual results and the budgeted income and expenditure for the period 1st April to 31st December 2017.

2. The Committee is also asked to consider and note the forecast full year financial performance against budget.

Background and Advice

The 2017/18 budget is a key tool for monitoring the financial performance of the Fund, and in particular the achievement of planned savings through LPP.

The one year budget for the year ending 31 March 2018 was approved by the Pension Fund Committee at its meeting on 17 March 2017.

It was noted in the report to Committee in March that it is difficult to estimate income due to the Fund and costs associated with the investment activities of the Fund with any degree of accuracy but it was agreed that a quarterly review of variances against the budget would provide useful management information for the monitoring of the financial position of the Fund.

Referring to the key income and expenditure items outlined in the budget, a comparison of actual results to budget is set out below. As the budget has been phased evenly throughout the year, the budget for the first nine months of the year is 75% of the full year budget. For some budget headings (for example property expenditure) this is a simple approach which will result in variances attributable to timing / phasing of spend.

INCOME

Contribution income

- YTD budget £184.9m, YTD actual £175.4m

Contribution income includes pension strain income which is running at £9m below budget for the first 9 months of the year. This income is difficult to predict and also subject to fluctuations throughout the year.

Favourable variances on ordinary employer contributions are offset by a shortfall against budget in respect of deficit recovery contributions which are in line with current expectations and reflect the discount offered for prepayment by major employers.

Employee contributions are in line with budget for the 9 months to 31 December 2017.

- Full year budget £246.5m, forecast £240.8m

The adverse variance on pension strain income is forecast to increase to approximately £12m for the full year.

A full year shortfall of £2.0m is forecast for deficit recovery income which is more than offset by an anticipated over-recovery of income from regular employer contributions of £8.5m.

The forecast for employee contributions for the full year is £56.6m against a budget of £56.7m.

Transfers in

- YTD budget £5.0m, YTD actual £9.1m

As noted in previous budget monitoring reports, the budget for transfers in is based upon average income over the previous two years and an assumption that the income will begin to reduce in line with the number of employees within the member organisations.

- Full year budget £6.7m, forecast £12.1m

Actual transfers in for the 9 months to 31 December are in excess of the full year budget and extrapolating to the year end indicates a budget surplus of approximately £5.4m. This assumes the current rate of transfers in remains constant during the final quarter of the year.

Investment income

- YTD budget £81.9m, YTD actual £114.4m

A favourable variance of £41.2m has been recognised on income from pooled investments. This is principally dividends received within the global equities pool.

This income is reported in the budget monitoring report but the overall impact on the bottom line is nil as the Fund's policy is to reinvestment dividend income.

Offsetting this favourable variance is £8.7m under-recovery of income from other investments, most notably a £5.7m shortfall in income due from property rent. This is likely due to timing differences but a review of property voids will be undertaken before the year end.

- Full year budget £109.2m, forecast £141.3m

The full year forecast assumes a reduction in the pooled investment income run rate. Realised gains on the transition of investments are recognised here in addition to dividend income. As the rate of transition of investments slows then we expect to see a reduction in these realised profits.

Property income for the full year is assumed to be in line with the rent due from tenants as noted in the latest external valuation report for both county and national portfolios.

EXPENDITURE

Benefits payable

- YTD budget £191.0m, YTD actual £189.3m

The £1.7m favourable variance on benefits payable when compared to the budget for 9 months is the net of £3.3m additional retirement pensions paid and £5.0m underspend against budget on lump sum payment of retirement and death grants.

- Full year budget £254.6m, forecast £252.3m

Benefits payable for the full year are forecast to continue at the current rate, resulting in a budget saving of £2.3m.

Transfers out

- YTD budget £10.3m, YTD actual £13.1m

As for a number of pension fund budget items, expenditure on transfers out is difficult to predict.

- Full year budget £13.8m, forecast £17.5m

On the assumption that the rate of transfers out in respect of leavers continues at the current rate the forecast is for an 'overspend' of £3.7m.

Administrative expenses

- YTD budget £2.8m, YTD actual £2.5m

The budget for administrative expenses includes amounts payable to LPP for the pension administration service, together with a recharge from LCC in respect of the time and resource dedicated by the treasury management team to the Fund.

- Full year budget £3.7m, forecast £3.2m

Based on the 9 months to 31 December a saving of £0.5m on administrative expenses is forecast, arising on the charges paid to LPP.

At the time of setting the current year budget , an estimate of £0.4m was included in respect of support services in addition to pension fund administration, liability modelling and employer risk services. To date no invoices have been received against this budget and we are now reflecting this as a true saving for the current year.

An additional £0.1m saving is forecast based upon the current rate of invoicing at a unit cost of £17.03 per member.

Investment management expenses

- YTD budget £25.5m, YTD actual £20.0m

The current year budget for investment management expenses comprises direct charges from LPP in respect of non-pooled assets (£3.9m), transition expenses (£1.7m) and investment management charges absorbed into the net asset value of pooled investments by LPP and other investment managers (£27.9m). A budget allowance of £0.5m for other commission and agents charges is also included.

- Full year budget £34.0m, forecast £30.3m

The quarterly direct charge from LPP has reduced during the year as investments have been transitioned into LPP pools. The full year forecast assumes a continuing reduction in the quarterly fee.

The corresponding charge for pooled investments, which is not billed directly but is instead netted off the value of the investment, has increased as assets have been transitioned.

LPP have adopted the transparency code and this will have an impact on future budget setting.

Direct costs of transition are initially charged to LPP by 3rd party legal and other professional advisors and are then recharged to the Fund. The forecast for the full year has been provided by LPP and indicates that £1.2m will be recharged in the final quarter of the year. This is a saving of £0.5m compared to budget and reflects the lower cost of transitioning non-equity investments.

Oversight and governance costs

- YTD budget £6.3m, YTD actual £5.6m

Oversight and governance expenses include the cost of the investment panel, actuarial, audit and other professional advisory fees, custody charges and LCC recharges in respect of financial resources.

£0.7m savings have been recognised in the first 9 months of the year, most notably on legal and professional advisory fees. These expenses are partly dependent on the level of investment activity and would include any abortive fees on transactions not completed.

- Full year budget £8.3m, forecast £7.3m

£1.1m of savings have been forecast for legal and professional advisory fees for the full year.

Other, less significant, net variances of £0.1m have been forecast across the remaining oversight and governance lines, including custody, property expenses and LCC recharges, based on current rates of expenditure.

Net surplus before realised and unrealised profits on investments

- YTD budget £35.5m, YTD actual £68.0m
- Full year budget £47.4m, forecast £83.1m

The net surplus of £32.5m for the 9 months to 31 December 2017 and £35.7m for the full year to 31 March 2018 is a direct consequence of additional investment income from pooled investments. As noted above, where this is a consequence of dividend income, the policy is to reinvest the income with an overall net nil impact on the bottom line.

Consultations

Variances between actual results and budget, where relevant to LPP, have been discussed with the LPP finance team as appropriate.

Implications:

This item has the following implications, as indicated:

Risk management

Regular monitoring against the budget of the fund will provide an explanation of key variances and will also inform future budget setting and forecasting.

Monitoring will ensure that the Committee has oversight of the costs of LPP and that the planned savings are being realised as in the approved business plan.

An analysis of full year actual financial performance against budget will be presented to the June meeting of the Pension Fund Committee, together with a draft statement of accounts for the Fund for the year to 31 March 2018.

Local Government (Access to Information) Act 1985
List of Background Papers

Paper	Date	Contact/Tel

N/A

Reason for inclusion in Part II, if appropriate

N/A