

Lancashire County Council

Pension Fund Committee

Minutes of the Meeting held on Friday, 15th July, 2011 at 10.00 am in Cabinet Room 'C' - County Hall, Preston

Present:

County Councillor David Westley (Chair)

County Councillors

T Aldridge	S Riches
M Devaney	G Roper
P Evans	M Welsh
M France	B Winlow
M Parkinson	K Young
T Pimblett	

Co-opted members

P Doyle	(Lancashire Leaders' Group representative)
B Harvey	(Trade Union representative)
P Hyett	(HE/FE Sector Establishments representative)
M Smith	(Blackpool Council representative)
R Whittle	(Trade Union representative)

Independent Advisers - Panel Members:

E Lambert

County Councillor B Winlow replaced County Councillor M Brindle for this meeting.

1. Apologies

Apologies for absence were received from County Councillor F De Molfetta and Mr N Mills, Independent Adviser.

2. Disclosure of Personal and Prejudicial Interests

County Councillors P Evans, M France, M Parkinson, T Pimblett, S Riches D Westley and B Winlow and Mr R Whittle and Mr R Harvey disclosed personal, non-prejudicial interests in the agenda as they were members of the Local Government Pension Scheme.

3. Minutes of the Meeting held on 15 April 2011

The minutes of the meeting held on 15 April 2011 were presented.

It was noted that County Councillor T Pimblett had been omitted from the list of members who had declared a personal interest in the agenda. Councillor Pimblett was a member of the Local Government Pension Scheme and it was agreed that the minutes should be amended to reflect his declaration.

Resolved: That, subject to the above amendment, the minutes of the meeting held on 15 April 2011 be confirmed and signed by the Chair.

4. Constitution and Membership

The Chair welcomed County Councillor M Devaney and Councillor M Smith as new members on the Committee.

Resolved:

- i. That the appointment of County Councillor D Westley and County Councillor M Welsh as Chair and Deputy Chair of the Pension Fund Committee for the remainder of the 2011/12 municipal year be noted.
- ii. That the appointment of County Councillor M Welsh and County Councillor G Roper as Chair and Deputy Chair of the Pension Fund Administration Sub-Committee for the remainder of the 2011/12 municipal year be noted.
- iii. That the membership of the Pension Fund Committee and the Pension Fund Administration Sub-Committee following the County Council's annual meeting be noted.
- iv. That the Terms of Reference of the Pension Fund Committee and the Pension Fund Administration Sub-Committee be noted.

5. Exclusion of Press and Public

Resolved: That the press and members of the public be excluded from the meeting during consideration of the following items of business on the grounds that there would be a likely disclosure of exempt information as defined in the paragraph of Part 1 of schedule 12A to the Local Government Act, 1972, indicated against the heading to the item. It was considered that in all the circumstances the public interest in maintaining the exemption outweighed the public interest in disclosing the information.

6. Fund Performance Report

(Exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act, 1972. It was considered that in all the circumstances of the case the public interest in maintaining the exemption outweighed the public interest in disclosing the information.)

The Committee considered a report on the performance of the Fund as at 30 April 2011, focussing on the funding position, the investment performance and allocation and risk management of the Fund.

There was a lengthy discussion on these issues and in particular the Committee welcomed the news that the Fund's deficit had recovered significantly in the last two years largely as a result of increased investment values.

In response to a question about risk management and in particular benchmarking with other Schemes, officers advised that such information was not available. The Fund's risk management processes were being formalised in conjunction with the new custodian and this would enable the Committee to see at a glance the Fund's level of exposure to risk. A further report on the Fund's risk profile would be presented to a future meeting.

A view was expressed that members had little opportunity to network with other Pension Funds. However, it was acknowledged that attendance at conferences and other pension fund related events had to represent value for money and officers agreed to prepare a further report on this matter.

The Committee was informed that the Treasury Management and Pension Team had won the Council's 2011 team of the year at the recent Pride Awards.

Resolved:

- (i) That the report be noted.
- (ii) That a report on the opportunities for members to attend conferences and other pension fund related events be presented to the next meeting of the Committee.
- (iii) That the Treasury Management and Pension Team be congratulated on winning the Council's 2011 team of the year award.

7. Report of the Investment Panel

(Exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act, 1972. It was considered that in all the circumstances of the case the public interest in maintaining the exemption outweighed the public interest in disclosing the information.)

The Committee considered a report on matters considered by the Pension Fund Investment Panel on 15 June 2011.

It was reported that the Panel had discussed a broad range of issues relating to:

- The Investment Context in which the Fund was operating;
- The current position of the Fund, including specific manager performance;
- Property annual strategy;
- Private Equity project;

- Alternative investment due diligence process;
- Future Strategy; and
- Other Business Plan Issues.

There was a general discussion on the Panel's report and in particular the Fund's property portfolio. In response to a question about the location of properties owned by the Fund, officers advised that the location of a property was not a determining factor. It was important to base decisions solely on the property achieving the best rate of return possible for the Fund. It was acknowledged that any decisions to purchase property in Lancashire would need to avoid a potential conflict of interest with the County Council.

Resolved: That the report be noted.

The Committee then returned to the remaining Part I agenda items.

8. Strategy for the procurement of tax agents

The Committee considered a strategy for the appointment of tax advisors to act on behalf of the Pension Fund.

The Pension Fund had previously used the assistance of KPMG to submit specific tax claims to the UK and European tax authorities. However, the current contract with KPMG did not enable them to review any other potential tax exposures of the Fund or provide advice on the implications of the Fund's Private Equity and other alternative investments.

The Committee noted that the investment strategy approved in December 2010 would increase the Fund's exposure to overseas investments and that this could lead to the Fund having tax payment and filing obligations in various local jurisdictions. In addition, certain countries (e.g. India) stipulated that investors had local tax agents before they invested.

It was good governance to appoint tax advisors to the fund who would provide ad hoc advice on the tax structure of new investments and any overseas tax filing obligations. The advisors would also be asked to review the current investments of the fund to ensure that any tax filing and payment obligations had been met.

They would also be asked to act as tax agents in jurisdictions where there was a local law requirement.

Given the likely scale of a contract of this sort and the relatively small number of firms with relevant global exposure, it was felt that procurement process should be run through a form of "mini competition", and a brief for this was presented at Appendix 'A'.

Resolved: That the running of a mini competition procurement exercise to appoint tax advisors to the Pension Fund, as set out at Appendix 'A', be approved.

9. Strategy for the Procurement of Governance and Proxy Voting

Services

The Committee considered a strategy for the appointment of corporate governance and proxy voting advisors to act on behalf of the Pension Fund.

PIRC had provided corporate governance services to the Fund since 2003. The current contract included the provision of voting advice and corporate governance company reports relating to the UK FTSE Allshare, the US S & P 500 and the Eurofirst 300 index. The service also included the provision of PIRC alerts, a weekly newsletter on current issues in corporate governance and socially responsible investment and also the County Council was entitled to two free places at any conferences PIRC organises on issues of corporate governance. The Fund's investment managers voted on the Fund's behalf based on PIRC recommendations.

A review of the service had shown that the Pension Fund only required reports for approximately 300 companies rather than the 1,000 that were currently being received and that current practice was to allow PIRC to vote on behalf of the Pension Fund. Initial research had indicated that the current arrangements were not in line with best practice and not arranged in the most cost effective way. A revised service could lead to approximately £17k cost saving to the Fund.

The Fund's current contract with PIRC was due to expire on 30 June 2011 and it was proposed that the contract be temporarily extended pending the completion of a procurement process to appoint corporate governance and proxy voting advisors to act on behalf of the Pension Fund. Details of the proposed procurement exercise were presented at Appendix 'A'.

Resolved: That the procurement procedure for the appointment of corporate governance and proxy voting advisors, and the short term extension of the current contract with PIRC, as set out in the report and at Appendix 'A', be approved.

10. Strategy for the Procurement of Global Equity Managers

The Committee considered a strategy for the procurement of the global equity manager framework on behalf of the Pension Fund

The investment strategy approved by the Committee in December 2010 included a switch to actively managed global equity mandates without a pre-determined geographical allocation. As a result the Investment Panel had considered the options for the global equity mandate and recommended the appointment of a framework of equity investment managers, comprising around 10 managers with a range of investment approaches and styles, from which 2 to 4 managers would be awarded funds to manage immediately.

The Investment Panel anticipated that some £1,500m would be placed with 2 to 4 equity managers with complementary investment styles. This would replace the mandates currently managed by Newton, JP Morgan and BNY Mellon. Having a framework of managers in place would mean that funds could be awarded to different managers quickly and easily when circumstances warranted and would

provide the Fund with greater flexibility to respond to both opportunities and the global economic context prevailing at the time.

A mini-competition had been run amongst the Manager Selection Consultant's Bench and subject to the Committee's approval of the framework approach, it was proposed that independent consultants, Bfinance, be appointed to run the selection and appointment process, including managing the tender and OJEU notices.

Bfinance had substantial experience in selecting equity managers for both private and public sector investors. Their bespoke approach, which incorporated the specific requirements of the client and did not rely on pre-approved buy lists, impressed the Investment Panel.

It was proposed to use the restricted tender process with a view to making a final decision on the appointment of the equity managers' bench and initial funding awards in December 2011. Further details about the restricted tender process were presented.

Resolved: That the procurement of the global equity manager framework, as set out in the report, be approved.

11. Strategy for the Procurement of a Direct Property Manager and Independent Valuers

The Committee considered a strategy for the tendering of contracts for the management and independent valuation of the Fund's UK property portfolio.

The Committee was informed that the existing UK property management and valuation contracts had been in place for many years without having been market tested. Recent renegotiation of aspects of the contracts and an internal audit recommendation highlighted the need for market testing.

At its meeting on 30 March 2011, the Investment Panel agreed it was appropriate to undertake appropriate due diligence regarding tendering of the management of the UK property portfolio and its annual independent valuation. As a result Officers had discussed the structure of the property mandate with a number of parties including professional surveyors and another Local Government Pension Scheme.

In common with other investment mandates, it was proposed that the property management mandate be tendered as a discretionary mandate. With a discretionary mandate, the property investment manager was responsible for the overall performance of the property portfolio, including both its strategic direction and its day to day management.

The Fund also had to revalue its properties annually for accounting and performance reporting purposes. A separate tender process would be run for the valuation service. It was proposed to run the tender processes in-house with the assistance of the One Connect Procurement Centre of Excellence and take appropriate specialist professional advice on the construction and scoring of the technical questions. The aim was to obtain technical advice from industry

specialists rather than general consultants in order to structure the contracts in the most commercially advantageous manner for the Fund and to reflect current best practice.

It was proposed to use the restricted tender process with a view to making a decision on an investment manager by the end of 2011 and an implementation with effect from 1 April 2012 (the start of the new financial year). Further details about the restricted tender process were presented.

In its assessment of fees, the Fund would seek an arrangement which linked the manager's remuneration to the performance of the property portfolio.

A similar restricted tender process would be used to appoint an independent valuer to the Fund at the same time.

Resolved: That the tendering of the UK property management and independent valuation contracts, as set out in the report, be approved.

12. Award of the Contract for Actuarial Services

The Committee considered a report on the outcome of the process for procuring actuarial services for the Fund.

The current arrangements for the provision of actuarial services to the Pension Fund were less formal than would be desirable and had been due for exposure to competition for some time. As a result the Committee approved a joint procurement with the Cumbria and Merseyside Funds.

While the Merseyside Fund had led the procurement process all three funds had participated in the evaluation and scoring of the formal proposals and presentations and had come to a common recommendation.

The conclusion of the evaluation panel was that Mercer should be appointed for a term of three years with the option to extend for a further three years. The County Treasurer, acting on behalf of the Lancashire County Pension Fund, approved this under the new arrangements for procurement on 15 June 2011.

The Committee was informed that the standstill period required under EU law had now expired and that the contract had commenced.

It was felt that there would be a significant advantage for all three funds in managing this contract collectively, both to reduce the overall effort involved but also to ensure that all three funds gained the benefit of new developments as they occurred.

Resolved: That the conclusion of the process for procuring actuarial services for the Fund and the appointment of Mercer as the Fund Actuary for a period of three years with the option to extend for a further three years be noted.

13. Delivery of Value for Money in the Management of the Fund

The Committee considered a report on some of the commercial initiatives undertaken in the last year to drive out both immediate one-off and on-going financial benefits to the Fund.

The following initiatives would produce a one-off benefit of £311,000 to the Fund and on-going savings of £751,000 per year plus efficiency savings:

	One Off Saving £000	Recurrent Saving £000 pa
Renegotiation of elements of the Property Management Contract resulting in a backdated rebate and ongoing savings	85	58
Negotiated cap to annual property revaluation fee, saving compared with previous percentage rate	36	
Cancellation of unnecessary IPD property report		18
Rebate from KPMG for poor service delivery	6	
Introduction of foreign currency accounts to hold Private Equity cash-flows saving on foreign exchange costs		10
Reduced costs arising from new Custody Contract	78	48
Reduced fund management costs from transferring L&G 2 Portfolio to the transition bench.		325
Transfer to transition bench out of pooled fund allows stock to enter stock lending programme		75
Renegotiation of L&G 1 portfolio fees. Refund of L&G fees for rebalancing not in accordance with instructions	106	50
Savings from new contract for actuarial services		102
Reduction in cost of administration from £22 per member to £21.50 per member following introduction of the new pensions payroll system, bringing the charge further below the lower quartile.		65
Total	311	751

Work to identify further savings would continue and reports would be presented to the Committee as appropriate.

Resolved: That the initiatives to deliver immediate one-off and on-going financial benefits to the Fund, as set out in the report, be welcomed.

14. Revised Statement of Investment Principles

The Committee considered a report on the revised Statement of Investment Principles.

The regulations governing the operation of the Pension Fund require that the Statement of Investment Principles must be reviewed and if necessary, revised, in case of any material change to the Principles within 6 months from the date of

change. The Committee was informed that the revised Investment Strategy and Governance arrangements approved by the Committee at its meetings in December 2010, January and April 2011 constituted a material change.

An updated Statement of Investment Principles was presented at Appendix 'A'.

Resolved: That the revised Statement of Investment Principles, as set out at Appendix 'A', be approved.

15. Annual Report and Accounts of the Fund 2010-11

The Committee considered the Annual Report and Accounts of the Pension Fund for 2010/11.

The Committee was informed that the Statement of Accounts was currently being audited by the Audit Commission. The Audit Commission's auditor's opinion would be included in the published Annual Report when the audit was complete. A copy of the Annual Report 2010/11 was presented at Appendix 'A'. The content of the Annual Report included the following sections:

- An overview of the management and financial performance of the fund;
- The Governance Compliance Statement;
- Administration of the Fund;
- Investments of the Fund;
- The accounts and financial statements;
- Actuarial Valuation;
- The Governance Policy Statement;
- The Communication Policy Statement;
- The Funding Strategy Statement;
- The Statement of Investment Principles

It was noted that the County Council's Constitution required the Pension Fund Annual Report to be approved by the Committee and submitted to the Full Council for information.

Members were informed that the Annual Report and a summary of the key points would be made available to employers and Fund members. Officers would welcome any suggestions to help promote the Annual Report.

Resolved: That the 2010/11 Lancashire County Pension Fund Annual Report, as now presented, be approved for submission to the Full Council.

16. Updated Governance Policy Statement

The Committee considered a report on revisions to the Fund's Governance Policy Statement.

Regulation 31 of the LGPS (Administration) Regulations required all Local Government Pension Scheme (LGPS) Funds in England and Wales to publish a Governance Policy Statement.

The Committee was informed that the Fund's Governance Policy Statement had been reviewed and updated following the approval of the Committee's revised constitution by the Full Council on 26 May 2011. The opportunity had also been taken to make a number of 'tidying up' amendments to the Statement. Other than the revised governance arrangements, the main change was the inclusion of the Fund's Governance Compliance Statement. The Governance Compliance Statement was previously omitted and the opportunity had now been taken to include the Statement at Appendix I of the Governance Policy Statement.

A copy of the revised Governance Policy Statement was presented at Appendix 'A'.

The Committee was informed that the Government's final response to the Hutton Report might require further amendments to be made to the Statement. A report would be presented to the Committee as necessary.

Resolved: That the updated Governance Policy Statement, as presented at Appendix 'A', be approved.

17. Internal Audit annual report 2010-11

The Committee considered the 2010/11 internal audit annual report for the Lancashire County Pension Fund.

The Committee was informed that based on the internal audit work undertaken during the year, the Audit Service was able to provide substantial assurance over the internal control environment for the Pension Fund and pension administration.

This was particularly pleasing as the Lancashire Pensions Service had been under considerable pressure during 2010/11 arising from the additional work involved both in processing the abnormal level of redundancies required this year across the scheme's employers and also from the implementation of the new pensions administration system.

It was confirmed that management responses to the report findings had been positive and action had or would be taken to address the recommendations for improvements to some control systems. It was noted that the recommendations did not represent significant areas of concern.

Officers promised to circulate further information about the level of fees paid to the internal audit service in 2010/11. This would include a comparison of fees paid across other Local Government Pension Schemes.

Resolved: That the 2010/11 internal audit annual report for the Lancashire County Pension Fund be noted.

18. Pension Fund External Audit Fees 2011-12

The Committee considered a report on the proposed fees for the external audit and inspection of the Lancashire County Pension Fund for 2011/12.

The Audit Commission's fees letter set out the main elements of the proposed audit and inspection work for 2011/12 and where appropriate, highlighted any specific risks which would be reviewed as part of this work.

Members were informed that the Audit Commission had set a scale fee for 2011/12 rather than providing a scale fee with fixed and variable elements. The Commission would keep the scale fee under review and analyse the costs of completed 2010/11 audits to determine whether it needed to make any changes to the fee. A further report would be presented to the Committee in February 2012.

Concerns were expressed about the annual audit fee being based on the size of the Fund rather than the work undertaken. It was felt that this should be taken up with the Audit Commission. Officers advised that given the possible abolition of the Audit Commission, they would be looking to undertake a procurement exercise for the provision of future audit services at some point. It was hoped that other authorities and Pension Funds would be willing to join the procurement exercise as this would help to secure the best possible terms and reduce the level of fees charged.

The Committee was also informed that Clive Portman, District Auditor would be retiring at the end of November 2011.

Resolved:

- (i) That the Audit Commission's fees letter for the audit and inspection of the Lancashire County Pension Fund for the year ending 31 March, 2012 be noted.
- (ii) That the Committee place on record its appreciation of the work undertaken by Clive Portman, District Auditor, on behalf of the Lancashire County Pension Fund, and that he be wished a long and happy retirement.

19. Administration Sub-Committee

The Committee received the minutes of the Pension Fund Administration Sub-Committee from its meeting on 5 July 2011.

The Sub-Committee had considered the Annual Administration Report for 2010/11. A copy of the report was available for inspection on the council's website at <http://council.lancashire.gov.uk/mgConvert2PDF.aspx?ID=3394>. The Sub-Committee resolved:

- (i) That the 2010/11 Administration report, as now presented, be approved.
- (ii) That the Sub-Committee's thanks and appreciation be extended to the Your Pension Service staff for the work undertaken during 2010/11.

The Committee endorsed the appreciation of the work undertaken by the Your Pension Service (formerly known as the Lancashire Pensions Service) staff in 2010/11. It was acknowledged that considerable additional pressure had been

put on the team in 2010/11 due to the abnormal level of redundancies and the implementation of the new pensions administration system.

The Sub-Committee also considered a report on the relatively low take up of the Local Government Pension Scheme by County Council employees and resolved:

- (i) That employee focus groups be established to explore the reasons for the relatively low take up of the Local Government Pension Scheme.
- (ii) That officers be requested to consider measures to improve communications with employees about the future operation of and changes to the Local Government Pension Scheme.

In endorsing these decisions, the Committee was mindful that the future of the Local Government Pension Scheme was uncertain and it was important to promote accurate information based on facts. The 'Your Pension Service' website was a key method of communication and officers agreed to review the website to see if improvements could be made to its content and the level of information provided.

Resolved: That the minutes of the Pension Fund Administration Sub-Committee from its meeting on 5 July 2011 be noted and that the decisions of the Sub-Committee be endorsed.

20. Urgent Business

None.

21. Date of Next Meeting

It was noted that the next meeting of the Lancashire Pension Fund Committee would be held on Friday 18 November 2011 at 10.00am at the County Hall, Preston.

I M Fisher
County Secretary and Solicitor

County Hall
Preston