

Pension Fund Committee

Meeting to be held on Friday, 6 March 2020

Electoral Division affected: None;

Lancashire County Pension Fund - Budget for year ending 31 March 2021

(Appendix 'A' refers)

Contact for further information: Abigail Leech, Head of Fund, Lancashire County Pension Fund Abigail.leech@lancashire.gov.uk 01772 530808

Executive Summary

A one year budget has been set for the Lancashire County Pension Fund for the year ending 31 March 2021. This budget forecasts that the net income available for investment (before accounting for changes in the market value of investments during the year) will be £219.1m.

Recommendation

That the Committee approve the Lancashire County Pension Fund budget for the year ending 31st March 2021, as set out in Appendix 'A' to this report.

Background and Advice

It is not a constitutional requirement for a pension fund to set an annual financial budget but it is considered a useful monitoring tool for the assessment of the overall financial position and performance.

The proposed one year budget for Lancashire County Pension Fund is set out in Appendix 'A' to this report.

The following have been taking into account in setting the one year budget:

- The latest (unaudited) forecast for the year ending 31 March 2020.
- Information received from the Local Pensions Partnership in terms of investment income, administration and investment management expenditure.
- The 2019 actuarial valuation in respect of contribution income receivable – pending confirmation of amounts to be paid in advance.
- The current investment strategy.
- Contractual agreements in respect of oversight, governance and investment management fees.

Previous budget assumptions have also been reviewed and adjusted where appropriate.

A summary of the budget is outlined below, by key budget heading.

INCOME

Contribution income budget £373.1m

Contribution income for the year ending 31 March 2021 includes £219.2m paid in advance by employers taking up the 2019 actuarial valuation option of prepaying future service rate (£206.8m prepayment) and deficit recovery contributions (£12.4m prepayment) for up to three years in advance.

Individual employers have been asked to confirm whether the option to prepay will be taken, by 9 March. The figures included in the budget are the expected outcomes based on confirmations received to date and the options taken following the 2016 valuation.

Our agreed accounting policy for these receipts in advance is to recognise them as income in the year of receipt. This will have a significant and favourable impact on the fund account in the year ending 31 March 2021 but will be offset by reduced contribution income in the following two financial years.

A 5% increase in pension strain and other pension augmentations has been budgeted against the forecast for the year ending 31 March 2019.

A 2% pay award has been recognised in budgeting for employee contributions.

Transfers in budget £12.5m

Transfers in have been budgeted at the same level as the forecast for the year ending 31 March 2020 in the absence of any identifiable trend in this area of income.

Investment income budget £214.5m

Budgeted investment income includes dividend income, net rental income from pooled properties and other direct income streams ('pure income') but also capital returns and distributions from the Fund's investments in private equity and infrastructure for example (capital income).

The Fund's pure income is relatively stable year on year however capital income can fluctuate significantly. The Local Pensions Partnership have forecast an average 5% increase per annum in the market value of the portfolio over a multi-year time horizon. The budget assumes that the pure income will increase at the same rate. Capital income is dependent on a number of market factors and the timing of distributions and liquidations of investments and as a result can vary over time. Any capital income budget is likely to require variance analysis and the forecast will be updated each quarter and for budgeting purposes a 5% increase in this income has also been recognised.

EXPENDITURE

Pensions payable budget £245.7m

Pensions payable are budgeted to increase by 2.6% CPI on the basis of the November 2019 pensioner payroll.

Lump sum benefits £43.8m

Lump sum benefits payable are budgeted in line with the forecast for the year ending 31 March 2020 since this expenditure fluctuates each year and cannot be forecast with accuracy.

Transfers out and other payments in respect of leavers budget £16.4m

Consistent with lump sum benefits payable, this expenditure is budgeted in line with forecasts for the year ending 31 March 2020.

Pension administration costs £4.1m

The budget for pension administration costs is to cover amounts payable to the Local Pensions Partnership for the administration of the scheme. The costs comprise £3.7m for core administration services, at a cost of £21.27 per member (£17.08 per member in 2019/20) and based on membership at 31 March 2019, together with £0.2m for employer risk and a further £0.2m for employer asset and liability modelling, both of which have been increased by an inflation factor of 2.7% on the previous year.

Investment management expenses £70m

The budget for investment management expenses is subject to fluctuations in the market value of the Fund's investment portfolio.

The Fund collects fee data from investment managers and works with the Local Pensions Partnership to ensure reporting complies with guidance on transparency.

Industry practice is to disclose fees in arrears – usually quarterly but sometimes with more delay, and this requires the Fund to estimate fees on best available information. The budget assumes charges embedded in the net asset value of investments held on behalf of the Fund will be in line with the forecast for the year ended 31 March 2020 with an additional £1m in respect of expenses previously incurred on directly held real estate assets which have now been pooled.

The forecast level of direct charges from Local Pensions Partnership Investments Limited for non-pooled assets is £2.1m for the year ending 31 March 2021 and reflects the transition of assets into pools throughout the current year. Charges raised by Local Pensions Partnership Investments Limited for management of the pooled funds held on behalf of the Fund are estimated at £9.4m.

The increase in total investment management fees payable to Local Pensions Partnership is due to the increase in the market value of assets under management. The fees are subject to fluctuations in market value. If the value of the portfolio increases by less than the budgeted rate then the fees payable by the Fund will be lower. The budgeted fees are in line with the Local Pensions Partnership budget which considers average growth of the portfolio value over a multi-year time horizon.

The budget for investment management expenses also includes £1.5m in respect of withholding tax which will ultimately be recovered and treated as investment income, £2.0m expenses for real estate investments directly held by the Fund and an allowance of £0.1m for each of custody and transition fees.

There is a £3.5m reduction in the property expenses from the forecasted expenditure in 2019/20. This reflects the impact of the pooling of property which took place part way through 2019/20 which is referred to above as the expenses will now be incurred by the pool and some non-recurring costs which were recognised in 2019/20.

A proportion of the Lancashire County Council staff recharges (£0.1m) is included within investment management to account for work done by the treasury management team on behalf of the Fund.

Oversight and governance expenditure £1.0m

The budget for oversight and governance of the Fund is broadly in line with the forecast for the year ended 31 March 2020.

The cost of actuarial work is forecast to decrease as much of the work for the 2019 valuation will have been completed. The budget for professional fees has been reduced to reflect the decrease in costs over the last few years as expenditure on potential investment decisions has dropped.

No change to the audit fee has been made and the budget reflects proposed fees as per the Public Sector Audit Appointments published rates. A nationwide consultation on 2020/21 audit fees will close on 6 March 2020.

Staff and other resource costs recharged by Lancashire County Council to the Fund have been budgeted at existing levels.

NET POSITION

The net income available for investment (before accounting for changes in the market value of investments during the year) is budgeted at £219.1m.

This compares very favourably to the latest forecast for the current year (£8.5m net income) due in part to increased investment income (budgeted to increase by 5% per annum) but mainly as a result of contribution income received in advance (£219.2m) which benefits the fund account in the year of receipt but will be offset by corresponding reduced income in the next two financial years.

Consultations

The Local Pensions Partnership have been consulted in respect of investment management and administration expenses.

Implications:

This item has the following implications, as indicated:

Risk management

Financial Risk

Regular monitoring against the budget will provide a useful tool for reviewing the financial position and performance of the Lancashire County Pension Fund, providing an analysis of significant variances from expectations.

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

Paper	Date	Contact/Tel
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N/A

Reason for inclusion in Part II, if appropriate

N/A