

## CLWYD PENSION FUND COMMITTEE

<b>Date of Meeting</b>	Wednesday, 7 October 2020
<b>Report Subject</b>	Investment and Funding Update
<b>Report Author</b>	Deputy Head, Clwyd Pension Fund

### EXECUTIVE SUMMARY

An investment and funding update is on each quarterly Committee agenda and includes a number of investment and funding items for information or discussion. The items for this report are:

- (a) The Business Plan 2020/21 update on progress. 3 of the tasks are complete or on target. 1 has commenced but is behind schedule and 1 has been moved into Q2 and 3 due to change of plan. Appendix 1.
- (b) Current Developments and News – News and development continues to be dominated by the Pooling across the LGPS which is covered in agenda item 8. In addition, there are several other areas which will impact on the section, including, the consultation on reforming Local Government exit pay, a review of employer contributions and flexibility on exit payments, the effect of the McCloud remedy on employer contributions and the un-pausing of the 2016 Cost Cap Mechanism.
- (c) Delegated responsibilities (Appendix 2). This details the responsibilities which have been delegated to officers since the last Committee meeting. These can include, cash management, short term tactical decisions, investments in new opportunities and monitoring of fund managers. There are no items of exception to report.
- (d) Within the risk register (Appendix 3) overall, a number of investment and funding risks have moved towards target.

### RECOMMENDATIONS

1	That the Committee consider and note the update for delegated responsibilities and provide any comments.
2	That the Committee approve the extension of the timescales in relation to a number of actions within the Business Plan as outlined in paragraph 1.01.

## REPORT DETAILS

1.00	INVESTMENT AND FUNDING RELATED MATTERS
1.01	<p><b>Business Plan Update</b></p> <p>Appendix 1 provides a summary of progress against the Investment and Funding section of the Business Plans for 2020/21.</p> <p>Cash-flow has been reviewed in light of the impact of COVID-19 and has been assessed as sufficient at this stage. The new cash flow management approach is in place to manage any potential shortfalls or large surpluses in the future and will be subject to on-going monitoring. All that is outstanding is the documentation of the new process which will be completed before the year end.</p> <p>The implementation of the new investment strategy has been completed and outlined in 1.08 below.</p> <p>Work on the implementation of our Responsible Investment Policy continues and it is planned for a more detailed update on the progress with Climate risk to be brought to the next Committee. Although it should be noted in 1.08 below that we have moved to a Passive Equity ESG fund in August and the Wales Pool will soon be implementing carbon reduction to our Global Equity exposure.</p> <p>Also within asset pooling, the timing of the Fixed Income transition slipped into Q2 and the timing of transition for Emerging Market equity and Private Markets will extend into 2021/22.</p> <p>For the RPI reform, the deadline for responding to the consultation was extended to late in August due to COVID-19, and therefore the results are not expected until at least October. This has therefore impacted on the timescales of reviewing the inflation hedging position but further details are included in the Funding &amp; Flightpath agenda item.</p> <p>Members are asked to approve these minor adjustments to the Business Plan.</p>
1.02	<p><b>Current Development and News</b></p> <p><b>Consultation on Reforming Local Government Exit Pay</b></p> <p>The new arrangements are currently planned to come into effect on 1 January 2021 so careful thought is needed in terms of any quotes or illustrations for cases on or after this date. The consultation sets out the following as the proposed approach for public sector employers within the LGPS:</p> <ul style="list-style-type: none"><li>• A general reform of redundancy payments, to involve a maximum of three weeks' pay per year of service, an overall ceiling of 15 months' pay and a maximum salary of £80,000 p.a., which can be used in the calculation.</li><li>• An overall cap on the exit pay amount of £95,000, including any</li></ul>

pension strain cost.

- A waiver process to allow for relaxation of the £95,000 cap in exceptional circumstances. For English councils it seems that this will need ratification of the full council and approval of the MHCLG. The arrangements for Welsh Councils are, we understand, being discussed separately but expected to sit with the Welsh Minister which could be applied unilaterally.
- Strain costs (and the related pension enhancements) for members over age 55 will be reduced by the value of any statutory redundancy payment which the employee will receive in cash.

Redundancy payments over and above the statutory redundancy payment will generally not be allowed in cases where a strain cost is paid when a member accesses their pension benefits.

The above will apply to different employers in different ways and some employers will not be affected at all depending on whether they are listed in the HMT exit cap regulations. However, if it proceeds then everybody over the age of 55 who works for a Council will be affected, whether they are subject to the £95k cap or not in Wales.

### **Review of Employer Contributions and Flexibility on Exit Payments**

Amending regulations have been published and come into force with effect from 23 September 2020.

1.03

### **Review of Employer Contributions between Valuations**

The Government has concluded that the power to review contributions between valuations should be available in respect of all employers. This would enable administering authorities to respond to the full range of circumstances which may occur between valuations, including potential impacts of COVID-19 and some other circumstances for example when local government reorganisation leads to a material change in liabilities.

The Government has amended the regulations to grant the following new flexibilities:

- Administering authorities may review the contributions of an employer where there has been a significant change to the liabilities of an employer.
- Administering authorities may review the contributions of an employer where there has been a significant change in the employer's covenant.
- An employer may request a review of contributions from the administering authority.

Where the funding position for an employer significantly changes solely due to a change in assets, the new Regulations will not allow employer contributions to be reviewed outside a full valuation.

### **Flexibility on Exit Payments**

The Government has amended the regulations so that there will now effectively be three options for an exiting employer:

1. As currently, calculate and recover an exit payment for employers ready and able to leave and make a clean break.
2. Agree a repayment schedule for an exit payment with employers who wish to leave the scheme but need to be able to spread the payment.
3. Agree a Deferred Debt Agreement (DDA) with an employer to enable them to continue paying deficit contributions without any active members where the administering authority is confident that the employer would fully meet its obligations.

The introduction of Option 3 and the DDA could have a profound shift in the way exiting employers are treated. Under a DDA, the exiting employer's responsibilities will be the same as for employers of active members but excluding the requirement to pay primary contributions (the future service rate).

The Fund will need to set its policy for reviewing employer contributions between valuations and also the new flexibility on exit payments. The number of employers potentially affected in the Fund by this change in the flexibility on exit payments is relatively small but it will need to be considered in more detail. This will be included in the Funding Strategy Statement and will be an extension of the Employer Risk Management framework already in place which monitors funding positions and covenant for all employers.

Guidance is being developed by both MHLCG and the SAB to ensure as far as possible there is consistency of treatment between employers in different LGPS Funds. Once the guidance is available the policy will be developed and brought back to Committee for agreement.

1.04

#### **The McCloud Remedy and Employer Contributions**

On 16 July MHCLG released the much anticipated consultation on the McCloud remedy for the LGPS in England and Wales and this consultation has been covered in other update reports. The consultation ends on 7<sup>th</sup> October.

From a funding perspective, an allowance for the McCloud remedy was calculated at the 2019 valuation for Funds in England and Wales. The calculations were generally carried out in line with the proposed underpin in the consultation and where employers have made a provision in their contribution rates, we would not expect to revisit this until the next valuation. For other employers, the Funding Strategy Statement allows us to revisit this where appropriate. It was made clear to employers at the meetings over 2019/20, that where they did not make an allowance for McCloud in their contributions, additional contributions would be payable once the remedy was confirmed. The affected employers will

	<p>be notified of the increase in their contributions once consultation has ended and the final remedy is set out in Regulation. The Fund will then discuss with these employers the precise timing of when the increase will be effective (including any backdating to 1 April 2020).</p>
1.05	<p><b>2016 Cost Cap Mechanism Un-Paused</b></p> <p>Separately the Government has announced that the 2016 Cost Cap HMT assessment for all public sector schemes will be un-paused and critically that the McCloud remedy is to be included in the assessment of the impact on member benefits. The Scheme Advisory Board will need to consider the implications of this in relation to their separate assessment of the LGPS cost cap and its interaction with the HMT assessment but fundamentally this could mean that the overall cost of McCloud will be offset in part or entirely when the outcome of the Cost Cap assessment is known.</p>
1.06	<p><b>Policy and Strategy Implementation and Monitoring</b></p> <p>The Advisory Panel receive a detailed investment report from the Fund's Investment Consultants, Mercer, which shows compliance with the approved Investment Strategy Statement and reports on fund manager performance. A summary of this performance is shown in the Mercer report included in agenda item 7.</p> <p>The Advisory Panel also receive reports from the following groups:</p> <ul style="list-style-type: none"> <li>• Tactical Asset Allocation Group (TAAG)</li> <li>• Cash and Risk Management Group (CRMG)</li> <li>• Private Equity and Real Assets Group (PERAG)</li> </ul> <p>Any delegations arising from these meetings are detailed in Appendix 2.</p>
1.07	<p><b>Implementation of Investment Strategy Review and Transition of Assets</b></p> <p>The Committee approved the revised Investment Strategy in 2019/20 which included the following changes:</p> <ul style="list-style-type: none"> <li>• Increase Global Equity from 8% to 10%</li> <li>• Within Global Equity, switch from Passive to ESG Passive</li> <li>• Increase Emerging Market Equity from 6% to 10%</li> <li>• The additional 4% of Emerging Market Equity to be allocated to the BlackRock Passive Fund until allocate to WPP.</li> <li>• Redeem the 10% total invested with Diversified Growth Managers</li> <li>• Decrease Hedge Funds from 9% - 7%</li> <li>• Increase Cash and Risk Management Framework from 19% - 23%</li> <li>• Restructure the Private Markets Portfolio to include Impact/ Local and increase the overall allocation from 25% - 27%</li> </ul>
1.08	<p><b>Transition of Assets to WPP</b></p> <p>The Committee previously approved the transition of the Stone Harbor Multi Asset Credit (MAC) Fund to the WPP MAC sub fund portfolio managed by Russell Investments. This sub fund was one of five being</p>

implemented across Wales and BlackRock were appointed by Link Fund Solutions, the WPP operator to transition all the assets between July and September 2020.

As such, the Fund made the decision to carry out the transition of assets as a result of the revised strategy during the same period as it involved additional subscriptions to both WPP and BlackRock as the WPP Passive manager.

Due to the size of the transition and the complexity, this was completed in several tranches and to facilitate timing differences of transition dates for some of the managers, it was agreed to use some of the Pension Fund cash to alleviate some of the out of market exposure.

A summary of the transition is shown below.

Month	Manager	Redemption	Subscription
		£m	£m
July	Clwyd Cash	9.3	
	WPP Global Equity		9.3
	Pyrford DGF	86.4	
	Investec DGF	84.2	
	Stone Harbor MAC	64.8	
	WPP MAC Fund		101.5
	BlackRock Passive	64.0	
	BlackRock ESG Passive		86.7
	BlackRock Emerging Market Passive		71.4
	Insight Cash and Risk Management		39.8
August	BlackRock Passive	11.9	
	BlackRock ESG Passive		11.9
	Stone Harbor MAC	65.0	
	WPP MAC Fund		65.0
September	Stone Harbor MAC	35.0	
	WPP MAC Fund		33.5
	Clwyd Cash		1.5
	Total Transition	420.6	420.6

1.09

As a result of the transition, all asset classes except Private Markets were now in line with their strategic allocation.

The revised allocations for Private Markets were agreed as:

- Opportunistic            Reduce from 2% to 0%
- Impact / Local        Increase from 0% to 4%
- Private Equity        No change            8%
- Infrastructure        No change            8%

	<ul style="list-style-type: none"> <li>• Property                      No change                      4%</li> <li>• Private Debt                      No change                      3%</li> </ul> <p>Much of this restructure will be achieved by re categorising the investments into the relevant strategies and will be implemented in October 2020.</p>
1.10	<p><b>Delegated Responsibilities</b></p> <p>The Pension Fund Committee has delegated a number of responsibilities to officers or individuals. Appendix 2 updates the Committee on the areas of delegation used since the last meeting.</p> <p>To summarise:</p> <ul style="list-style-type: none"> <li>• Cash-flow forecasting continues to be monitored through the Cash and Risk Management Strategy going forward.</li> <li>• Shorter term tactical decisions continue to be made by the Tactical Asset Allocation Group (TAAG)</li> </ul>

<b>2.00</b>	<b>RESOURCE IMPLICATIONS</b>
2.01	None directly as a result of this report.

<b>3.00</b>	<b>CONSULTATIONS REQUIRED / CARRIED OUT</b>
3.01	None directly as a result of this report.

<b>4.00</b>	<b>RISK MANAGEMENT</b>
4.01	Appendix 3 provides the dashboard and risk register highlighting the current risks relating to Investments and Funding matters.
4.02	<p>There have been no additional risks added to the register since the last Committee but additional processes have been included in F3, 4 and 7 to include issues associated with the Covid pandemic.</p> <p>Of the 9 risks, 6 have remained the same as reported to the February 2020 Committee. Of the 6, F3 and 5 remain on target and F2, 3, 8 and 9 remain one step away from the target impact or likelihood.</p> <p>The remaining three risks have changed since the last Committee. F1 and F7 have increased their likelihood or impact by 1 which reflects the financial risks to some employers relating to COVID 19, although no issues have materialised to date. F6 has decreased the impact by 1 given some additional work on the covenant of our employers but some work remains outstanding.</p>

<b>5.00</b>	<b>APPENDICES</b>
5.01	Appendix 1 - 2020/21 Business plan update Appendix 2 – Delegated Responsibilities Appendix 3 – Risk dashboard and register – Investments and Funding

<b>6.00</b>	<b>LIST OF ACCESSIBLE BACKGROUND DOCUMENTS</b>
6.01	None.  <b>Contact Officer:</b> Debbie Fielder, Deputy Head, Clwyd Pension Fund <b>Telephone:</b> 01352 702259 <b>E-mail:</b> Debbie.a.fielder@flintshire.gov.uk

<b>7.00</b>	<b>GLOSSARY OF TERMS</b>
7.01	<p>(a) <b>The Fund - Clwyd Pension Fund</b> – The Pension Fund managed by Flintshire County Council for local authority employees in the region and employees of other employers with links to local government in the region</p> <p>(b) <b>Administering authority or scheme manager</b> – Flintshire County Council is the administering authority and scheme manager for the Clwyd Pension Fund, which means it is responsible for the management and stewardship of the Fund.</p> <p>(c) <b>The Committee - Clwyd Pension Fund Committee</b> - the Flintshire County Council committee responsible for the majority of decisions relating to the management of the Clwyd Pension Fund</p> <p>(d) <b>TAAG – Tactical Asset Allocation Group</b> – a group consisting of The Clwyd Pension Fund Manager, Pensions Finance Manager and consultants from JLT Employee Benefits, the Fund Consultant.</p> <p>(e) <b>AP – Advisory Panel</b> – a group consisting of Flintshire County Council Chief Executive and Corporate Finance Manager, the Clwyd Pension Fund Manager, Fund Consultant, Fund Actuary and Fund Independent Advisor.</p> <p>(f) <b>PERAG – Private Equity and Real Asset Group</b> – a group chaired by the Clwyd Pension Fund Manager with members being the Pensions Finance Managers, who take specialist advice when required. Recommendations are agreed with the Fund’s Investment Consultant and monitored by AP.</p> <p>(g) <b>In House Investments</b> – Commitments to Private Equity / Debt, Property, Infrastructure, Timber, Agriculture and other Opportunistic Investments. The due diligence, selection and monitoring of these investments is undertaken by the PERAG.</p>

- (h) **LGPS – Local Government Pension Scheme** – the national scheme, which Clwyd Pension Fund is part of
- (i) **ISS – Investment Strategy Statement** – the main document that outlines our strategy in relation to the investment of assets in the Clwyd Pension Fund.
- (j) **FSS – Funding Strategy Statement** – the main document that outlines how we will manage employers contributions to the Fund
- (k) **Funding & Risk Management Group (FRMG)** - A subgroup of Pension Fund officers and advisers set up to discuss and implement any changes to the Risk Management framework as delegated by the Committee. It is made up of the Clwyd Pension Fund Manager, Pension Finance Manager, Fund Actuary, Strategic Risk Adviser and Investment Advisor.
- (l) **Actuarial Valuation** - The formal valuation assessment of the Fund detailing the solvency position and determine the contribution rates payable by the employers to fund the cost of benefits and make good any existing shortfalls as set out in the separate Funding Strategy Statement.
- (m) **Actuary** - A professional advisor, specialising in financial risk, who is appointed by pension Funds to provide advice on financial related matters. In the LGPS, one of the Actuary's primary responsibilities is the setting of contribution rates payable by all participating employers as part of the actuarial valuation exercise.
- (n) A full glossary of Investments terms can be accessed via the following link.  
<https://www.schroders.com/en/uk/adviser/tools/glossary/>