PENSIONS COMMITTEE
29-06-09

Present: Councillor John G. Jones (Chairman)

Councillors Trefor Edwards, J.R.Jones, W. Tudor Owen, Gwilym E. Roberts and Councillors Goronwy O. Parry (Isle of Anglesey Council) and Margaret Lyon (Conwy County Borough Council)

Also present: Dilwyn Williams (Corporate Director),
Dafydd Edwards (Head of Finance), Gareth Jones (Pensions Operations Manager) and Gwyn Parry Williams (Committee Officer).

Apologies: Councillors Keith Greenly-Jones and Linda W. Jones

1. CHAIRMAN

RESOLVED to re-elect John G. Jones as Chairman of the Committee for 2009/10.

2. VICE-CHAIRMAN

RESOLVED to re-elect Councillor Keith Greenly-Jones as Vice-chairman of the Committee for 2009/10.

3. DECLARATION OF PERSONAL INTEREST

No declarations of personal interest were received from any member present.

4. MINUTES

The Chairman signed the minutes of the previous meetings of this committee held on
12 December 2008 and 2 February 2009, as a true record.

5. GOVERNANCE ARRANGEMENTS FOR PENSION FUNDS

Submitted – the report of the Pensions and Investments Officer, noting that the Department for Communities and Local Government had published a consultation document in relation to governance arrangements for Local Government Pension Funds, the aim of which was to try and find the best way of extending representation and the standards of governance of these funds. The paper highlighted the results of the Department's scrutiny work regarding the Governance Policy Statements that Local Government Pension Funds were required to prepare. The purpose of the exercise was to assess the extent to which each fund's governance policies measured up to the best practice standards and to attempt to identify areas where further work was necessary.

Pension Funds now had to measure their compliance against the following best practice principles:
a) Structure

b) Committee membership and representation
c) Selection and role of lay members
ch) Voting
d) Training / Facility Time / Expenses
dd) Meetings (frequency / quorum)
e) Access
f) Scope
ff) Publicity

The initial review by the Department suggested that compliance against the best practice principles across the country was significantly high. Compliance was very good in some areas such as Structure, Representation and the Selection and Role of Lay Members. Approximately 96% of authorities had some level of representation in their formal governance arrangements. However, there were some areas where there was a lack of progress, e.g. training, facility time and expenses. Although there was evidence of some progress being made, it was believed that formal training was for elected members only, not for lay members. In addition, there was an absence of clear policies regarding facility time and the payment of expenses.

Consultees were asked to consider which steps that could be taken to achieve compliance with the principles, especially regarding the following -
i) Training and facility time for all those involved in the democratic and stewardship process.
ii) Extending the knowledge base of new councillors, as well as existing non-elected and committee participants.
iii) To provide an alternative method of communication and representation in those instances where scheme members were not represented on the committee.

Any observations on the consultation were invited by 30 September 2009. It was of the opinion that not much further that could be said on the matter as the committee already decided not to extend the committee's representation, but rather to experiment with informal committees for stakeholders. Therefore, it was suggested that there was a need to see how these worked before considering taking any further steps in this field.

RESOLVED
a) To inform the Department for Communities and Local Government that the Council has no further observations to submit on the consultation document as the Council has already decided to experiment with informal meetings for stakeholders, and there is a need to see how these work before taking any further steps.
b) That we hasten to hold the informal meetings of employers.

6. APPOINTMENT OF FIDELITY

Submitted – the report of the Corporate Director noting that the committee had appointed Fidelity to manage the global equity investment portfolio and by now, the legal arrangements had been completed and the assets had been transferred from Legal & General to them.

At a meeting of the Investment Panel in February 2009, the performance fee offered by Fidelity had been raised and it was noted that the Council was not entirely comfortable with the proposed fee and Hymans Robertson were asked to go back to them to renegotiate, as there was a feeling that the threshold at which the company would gain was too low. After discussing the issue with Hymans, a compromise was reached by changing the percentages payable at different performance levels and in order to be able to move forward with the transfer of assets, agreement was reached to that compromise. He noted that the committee would gain should the performance be less than 1% above the benchmark, but worse off should it be between 1 and 3% above the benchmark.

He also noted that the intention outlined during the interviews was for Fidelity to use their "Global Select" strategy on a pooled basis (rather than keeping Gwynedd's investments separately) to invest the Fund's resources and the benchmark used was the MSCI AC index. In this benchmark, 9.5% of the assets were meant to be in emerging markets. It had become apparent a short time before the transfer that Fidelity's Global Select Fund did not have any investment in emerging markets but they intended to start a Select Fund that invested in such markets in future, but it would not be available for some months.

He informed the committee that Fidelity had another fund that was available at the time which invested in emerging markets, but Hymans recommended that the "select" method of investment managed risks better within a portfolio and was likely to provide more constant outperformance in the long term. In order to address this problem, a number of options were suggested, namely -
a) Rather than transferring 20% of the value of the Fund to Fidelity, transfer 18% now and keep the 2% we had in emerging markets by keeping them in the funds of Legal & General (which included the investment in the UBS Emerging Market Fund of course) and then transfer the rest to Fidelity when they had an Emerging Market "Select Fund".
b) Transfer 20% of Fund assets to the Fidelity Global Select Fund and transferring out of that once Fidelity had a suitable fund.
c) Transfer 18% of the Fund assets to Fidelity's Global Select Fund and 2% to the other Fund Fidelity had for investments in emerging markets, and transferring out of that when Select Fund was available by Fidelity.

In order to move on with the transfer, he had agreed to the first option noted above, namely transferring 18% at present to Fidelity for their Global Select Fund and leaving the developing markets investment with Legal & General until Fidelity had a suitable Fund.

RESOLVED
a) To confirm the steps taken by the Corporate Director as noted above.
b) To express concern to Hymans Robertson that they had not drawn the Council's attention to the lack of ability to invest in emerging markets, earlier on.

7. APPOINTING A NEW INVESTMENT MANAGER FOR BONDS

Submitted – the report of the Corporate Director noting that the committee had resolved on 12 December 2008 to introduce a new active bond mandate into the Fund's investment structure. The new mandate would represent 15%

of the Fund's assets (approximately £100m) and it would be funded from the fixed income assets that were currently being held in BGI's passive mandate.

In order to appoint a new active bond manager, the Fund would have to carry out a new formal tender process within time constraints set out by law. The process would include four stages, namely -
a) Draft and agree a Fund specific Official Journal of the European Union (OJEU) notice and Pre Qualification Questionnaire.
b) Analyse PQQ responses using quantitative and qualitative screening to identify investment managers to be included on the long list
C) Issue detailed Requests for Proposal (RFP) to long-listed managers and analyse responses.
ch) Shortlist of managers to present to the committee.

He informed the committee that an OJEU notice had already been issued and the PQQs had been sent to each manager that had responded. He provided details of the timetable from now on. When appointing an equity manager recently, the committee had decided that the decision on the managers that should be given a Request for Proposal should be left to the Corporate Director himself, having received recommendations from Hymans Robertson and that the committee itself should draw up a shortlist of managers to be interviewed from the proposals received.

He reminded members of the discussion held at the previous Investment Panel meeting in relation to utilising an absolute return benchmark for this mandate. This meant that the manager would be measured against a cash benchmark. This allowed managers to have the freedom to act as they wished within the bond universe to try and achieve the stated return, as opposed to the traditional approach which would constrain them to pre-determined weightings within the bond universe.

RESOLVED
a) To agree, when the report of Hymans Robertson is received, to delegate powers to the Corporate Director to decide which managers to invite to present an RFP, and that the committee draws up a shortlist for interview from the proposals received.
b) To confirm the decision to run the new mandate on an absolute return basis with a benchmark relative to cash.

8. MAKING THE CONNECTIONS: THE LOCAL GOVERNMENT PENSION SCHEME IN WALES

Submitted – the report of the Corporate Director, noting that the Welsh Local Government Pension Funds currently operated within the National Local Government Pension Scheme and dealt with assets of approximately £7bn, with over 200,000 members and annual expenditure on administration in the region of £7m and fund management costs of approximately £22m. Staff numbers were in excess of 120. Within the context of the increasing cost of public sector pensions and the increasingly difficult financial environment for local councils, it was very likely that this field would come under further scrutiny in years to come. In order to achieve sufficient savings in the costs in order to stabilise or even reverse increasing employers' contributions, some further measure of national scheme reform would be necessary. However, there was a question as to whether it would be possible to reduce

the costs involved in administering and investing pensions, thus releasing some financial benefits to authorities, by changing the structure of Funds in Wales. Any reduction in costs would have to be set against any investment risks and other relevant factors. It was not clear whether closer working or the merger of funds would actually achieve these outcomes, and in order to come to a rational and informed decision, Pension Funds needed to consider the potential to achieve economies of scale and consider the scope for potential benefits.

Pension Fund Treasurers had begun to consider the merits or otherwise of this issue. However, no detailed work had been undertaken yet and any departure from existing arrangements would require detailed consideration and assessment. The Welsh Pension Funds already exchanged good practice, discussed the detail associated with regulatory changes and had worked jointly in producing a newsletter and annual benefits statements. This was very important work that deserved recognition, however, consideration should be given to the question of whether more fundamental change would yield benefits.

He informed the committee that it would be necessary to give careful consideration to a wide range of issues, in order to come to an informed decision on this, however, the ever increasing pressure on local government finance meant that this was a sensible opportunity to look at the issue. He provided details of some of the issues that would possibly need to be considered as part of any Outline Business Plan. He also referred to the initial decisions held by the Welsh Local Authority Pension Fund Treasurers and the views voiced by them.

In relation to the next steps, every Fund was asked to move the issue forward within their own administering council so that members could consider the principle of the Pension Fund joining in the commissioning of the work and then subsequently to meeting any cost of the Outline Business Case production. Only by commissioning and carrying out this work would it be possible to form a view on the merits or otherwise that would either prove or disprove any proposition for change. The Pension Fund Treasurers would act as a Project Board in commissioning this work and a suitable resource would be identified from one of the Councils to act in a project management role for this initial stage only. The scope and method statement of achieving this work would be agreed and then the Outline Business Case would be produced for consideration by all the individual funds. It would be premature to plan any subsequent stage since any judgements on whether or not to progress beyond the initial stage would be dependent on the outline business case conclusions and subsequent consultation with all stakeholders on that business case.

RESOLVED
a) To agree for the Pension Fund to participate in this joint exercise to commission work and then subsequently to meeting a share of the cost of the outline business case production jointly with the other eight funds.
b) To place trust in the Corporate Director and Head of Finance to decide whether the cost is reasonable, but to submit a further report to the committee should they be of the opinion that the cost is too high.

9. FUND POSITION

Submitted – the report of the Corporate Director, noting that the Pension Fund was formally valued every three years, and as a result of that valuation, the employer's contribution was established. The Fund was last valued on 31 March 2007 and the next valuation would be held in March 2010, with the new employers' contributions becoming operational in April 2011. In the meantime, in order to ensure that the Council was aware of the Fund's general position and what was likely to happen to the employer's contribution, it was customary for a report to be commissioned every year in order to assess the general position of the Fund.

It had been noted in the last valuation that there were assets in the Fund that were tantamount to 84% of the liabilities. Overall for the fund, this meant that the necessary employer contribution was 20.1% (15.8% to pay for future service and 4.3% to rectify the past service deficit). By now, substantial reductions had been seen in equity market values from the end of 2007 to March 2009 and this meant that the Fund's comparable position had deteriorated substantially. The Council was not unique in that every fund which invested in equities would have suffered a similar fate.

The commissioned report showed that due to the reduction in returns from gilts (which were used to value liabilities), the contribution that would be required for paying for future service had risen from 15.8% to 16.8%. Similarly, this factor, together with the fact that the value of assets had fallen since 2007, meant that the fund had assets to the value of 56% of the liabilities in the Fund and the employer contribution rate would need to increase from 4.3% to 13.4% to make up this deficit. This would mean, should the valuation happen on 31 March 2009, there would be a danger that the employer contribution would have to increase from 20.1% to 30.2%. This would not be acceptable, considering the objective of seeking to establish employer contributions and in the meantime, the actuary would be considering how to ameliorate this effect in the actual valuation in March 2010, unless the position would have improved by then. He noted that the position had already changed as the report was based on when the FTSE 100 index stood at 3926 on 31 March 2009, whilst it had currently stood at around the 4400 level.

It was noted that the actuary had already mentioned work that was taking place in other places which took a longer-term view than that of the three years of the valuation, and this idea would be discussed further with them so as to see whether it would suggest a solution to the problem.

RESOLVED
a) To contact the employers of the Fund now to give them prior notification and warning of the position.
b) To continue to discuss any alternative proposals available in order to establish the employer contributions and to report back once anything of substance is to be reported.

10. PRIVATE EQUITY

Submitted – the report of the Corporate Director, noting that the committee had agreed that approximately 5% of the Fund should be invested in private

equity due to the fact that it would give the fund greater divergence of investments in an asset class which was not directly correlated to equities and which offered the opportunity for greater returns. The committee had resolved to invest on a Fund of Funds approach, i.e. rather than investing in a single private equity manager (which would have greater risk implications in terms of deciding upon one manager and getting access to the better funds), the committee invested in a manager who allocated his funds amongst various private equity managers, thus spreading the risk. In March 2007, the Committee had appointed Partners Group as its private equity manager. Private equity was not an asset class that was easy to value at any time.

He noted that the investment cycle was one whereby you decided to commit a sum of money; the manager drew down those funds as and when the opportunities arose, and over a period of time, fees were paid to the Fund Manager. Whilst the Fund Manager would value the investment according to their own internal valuation process, unlike quoted equities which could be sold on any day at a quoted price; the true value of the private equity investment would only be known when the money would be returned to the Council. Whilst Hymans Robertson would report on the manager's estimate of current value of the investment, in truth, the true value would only be seen when the investment would be fully realised – and even that period was uncertain.

He informed the Committee that the Council had committed €85m (approximately £72m) into three different funds with the group. The largest allocation was the "2006 Global Value Fund" where €50m was committed. This was the main investment that invested in a range of Private Equity companies. It also invested in secondary investments, namely buying private equity stakes from those wishing to sell their holdings, and direct investments (where a Private Equity house was looking for a partner to co-finance a particular project and offered that opportunity to its investors). Also, direct investments had been made in the Secondary Fund (€15m) and their Direct Investment Fund (€20m).

A meeting had been held in April 2009 between the Council officers and representatives of Partners Group, to discuss the current position of the Fund. The "2006 Global Value Fund" had around 98 investment elements and the representative gave a summary of the current position. Through the use of secondaries, 9% of the capital contributed had already been distributed to investors.

He referred to the fact that the Direct Investment element was being invested in approximately 53 various elements and he gave details of the current assessment.

There had been two early wins in these investments, giving a 63% internal rate of return. However, they noted that this Fund also traded behind expectation at the moment. The Secondary Fund had not yet closed. Partners Group expected to be able to take advantage of a shift from a sellers market to a buyers market in 2009 to add value. It would be required to consider the best way to monitor the activity in this field in the future. The matter had been raised with Hymans Robertson and it was expected that the matter could be addressed at the next monitoring meeting.

RESOLVED to accept the report.

11. CONFERENCES

Submitted – the report of the Corporate Director, noting that details had been received of two conferences relevant to members of this committee, namely -
a) LGC Investment Summit, Newport 10-11 September 2009
b) LGPS Trustees' Conference, Cardiff, 22-23 October 2009

It was noted that it had been decided in 2008, in accordance with the usual arrangements, to send two members of the committee to the LGC Conference and the representatives were selected from the committee member list in alphabetical order. This was a conference which dealt with investment only. The members were currently circulated on an alphabetical basis, starting with the name which followed last year's attendees, to see who would be attending this year's conference.

In relation to the LGPS Conference, it had been decided last year, as the majority of members were new to the committee, to send four members to the conference, rather than two, as it was a conference that considered a broader programme of issues and the same arrangements had been established so as to select attendees, which involved giving the opportunity to members in alphabetical order. It was noted that the original arrangements were to book places for two members and one officer for both conferences and he asked
for the committee's views in relation to reverting to the usual arrangements for the LGPS conference from now on.

RESOLVED to agree to revert to the usual arrangements for the LGPS conference, namely to send two members (according to alphabetical order) and one officer.

The meeting commenced at 3.30am and concluded at 4.20pm