

FALKIRK COUNCIL

Subject: GENERAL GOVERNANCE MATTERS
Meeting: JOINT MEETING OF THE PENSION BOARD AND PENSIONS COMMITTEE
Date: 26 JUNE 2015
Author: CHIEF FINANCE OFFICER

1. INTRODUCTION

- 1.1 This report updates the Board and Committee on miscellaneous matters associated with the business of Falkirk Council Pension Fund.

2. LGPS 2015

- 2.1 The new version of the Local Government Pension Scheme came into effect on 1st April, 2015.

- 2.2 Key changes are as follows:

- Career average accrual
- Final salary rights protected
- Scheme normal retirement age now equivalent to each member's own State Pension Age
- Accrual rate of 49ths rather than 60ths
- Member contribution rate for part time members based on actual rather than full time pay
- Overtime hours pensionable for part time members
- 50/50 option
- No detriment underpin for older members
- Employer discretions policy due by 30th June, 2015
- New governance arrangements

- 2.3 The new pensions administration system which went live in March, 2015 has allowed the Fund to continue operating an administration system that is compliant with scheme rules. The system is maintained by external software providers and therefore reduces reliance on a key individual for systems development. Since the go live date, although it has been "business as usual" for the Pensions Section in calculating and paying benefits, some further development work requires to be undertaken, in particular, the migration of the pensioner payroll to the Altair platform.

3. RISK REGISTER

- 3.1 The Committee has asked officers to provide a regular update on any areas of heightened risk.

Identified Risk per Risk Register	Reason for Change in Risk Rating
Funding Position affected by falling asset values	<p>The outcome of the UK General Election guarantees that a referendum on EU membership will take place by 2017. Financial markets may be unnerved by the surrounding uncertainty. This may have an adverse effect on asset values.</p> <p><i>Mitigation – The Fund is a long term investor that can afford to withstand the volatility that may be triggered by political uncertainties. In addition, the Fund's assets are also invested in a wide range of asset classes, not all of which are likely to be impacted (e.g. infrastructure, overseas equities, etc).</i></p>

4. SOCIAL HOUSING

- 4.1 The Committee has agreed to make a £30m commitment to Hearthstone Investments to fund Social and Affordable Housing via their Housing Fund for Scotland. The Fund objective is to deliver returns of RPI + 2%. In order to deliver the new units in Scotland, Hearthstone is working in partnership with Castle Rock Edinvar, the Edinburgh based Housing Association.
- 4.2 An initial drawdown of £15m has been invested in a short term debt instrument to support the Social Housing element. A further £1.8 million has been drawn down to support the first phase of investment in Affordable Housing.
- 4.3 The Social Housing element involves the construction of 191 units across the pension fund area as follows:

Area	Site	Number of Units
Clackmannanshire	Sauchie	35
Falkirk	Bellsdyke	62
	Overton	34
Stirling	Durieshill	60
TOTAL		191

- 4.4 Due to its innovative nature, the Social and Affordable Housing project is being supported financially by the Scottish Government. A visit to the Bellsdyke site has been made by the Scottish Government's Housing Minister on 8th June.
- 4.5 The project was also part of a general discussion on pension fund investment in local infrastructure at the Scottish Parliament's Local Government and Regeneration Committee at which the Chief Finance Officer was invited to give evidence. The Committee has subsequently written to all Scottish Local Authority Pension Funds to obtain information about each Fund's Environmental, Social and Governance policy and approach to infrastructure investment. A copy of the Committee request letter and the Falkirk Council reply is attached as an Appendix to this report.
- 4.6 With regards to the affordable housing part of the Hearthstone mandate, the £1.8m drawdown has been used to buy 17 units in Bo'ness which will operate as affordable lets via Castle Rock Edinvar. Hearthstone is also holding discussions with several builders to assess whether any recently constructed stock can be used to meet the remainder of the mandate.
- 4.7 Hearthstone will give a formal update on progress to a future meeting of the Committee.

5. UK INFRASTRUCTURE

- 5.1 The Pensions Committee at its meeting of 5 June 2014 agreed to invest £30m in UK infrastructure projects in collaboration with the Lothian Pension Fund.
- 5.2 An initial investment has been made with Ancala Partners to support the purchase of Green Highland Renewables, the owner and developer of various small scale hydro projects in the UK, including the Scottish Highlands. Other investors include the Lothian Pension Fund and Towers Watson. Ancala specialise in infrastructure deals and have identified the vendor as having both a strong asset platform and pipeline of new projects.
- 5.3 The Fund's commitment is £2.75m (12.5%) towards a total purchase price of £22m. A draw down of £1.5m has already been made. The expected return is an average of 9% p.a. over 10 years, although it is possible that the asset could be held for up to 25 years.
- 5.4 Other investment opportunities for the UK Infrastructure commitment are currently being evaluated.

6. SCHEME ADVISORY BOARD

- 6.1 Under the new governance arrangements, a national Scheme Advisory Board has been established to provide advice to the Scottish Ministers on the desirability of changes to the LGPS. The Board is also empowered to provide advice to scheme managers or pension boards in relation to the effective and efficient administration and management of the Scheme.

- 6.2 An initial meeting of the Board has taken place and a proposed workplan includes the following:
- Funding the Scheme Advisory Board
 - Collection of consistent Fund data
 - Structural review of Funds
 - Review the results of the 2015 national valuation
 - Improve transparency of investment decisions
- 6.3 The Chair of the Scheme Advisory Board for 2015/16 is Councillor Stewart Cree with Harry Frew of UCATT as Vice-Chair. The Chief Finance Officer is one of a range of professional advisers to the new Board.

7. THE PENSIONS REGULATOR

- 7.1 The Public Sector Pensions Act 2013 gives the Pensions Regulator oversight over administration and governance standards in the Local Government Pension Scheme.
- 7.2 The Regulator has published Code of Practice No. 14 – Governance and Administration in Public Service Pension Schemes. Amongst the topics covered are:
- Knowledge and Understanding Required by Pension Board Members
 - Managing Risks and Internal Controls
 - Scheme Record Keeping
 - Contribution Monitoring and Reporting of Breaches
- 7.3 A fuller consideration of the Code of Practice will be provided at the next Committee/ Board meeting.

8. LOCAL AUTHORITY PENSION FUND FORUM (LAPFF)

- 8.1 The LAPFF represents the interests of over 60 local authority pension funds with combined assets of around £120 billion. Its mission is to promote the highest standards of corporate responsibility amongst the companies in which member funds invest.
- 8.2 The LAPFF is supported by PIRC Ltd, who are the Forum's company research and engagement partner. PIRC are also the Falkirk Fund's proxy voting agents and advisers on ESG matters.
- 8.3 As part of its lobbying activities, LAPFF is a leading participant in the "Aiming for A" campaign – a coalition of asset owners with shared concerns over the environmental dangers of climate change and the long term profitability of carbon intensive energy companies.
- 8.4 The campaign has prompted successful votes at recent AGMs by the shareholders of BP, Shell and Statoil for more disclosure around the management of carbon emissions and the level of research and development into lower carbon energy solutions. The campaign recognises that many long term institutional investors want energy producers to demonstrate that climate based risks are being accounted for in business strategies.

8.5 Other LAPFF activity during the last quarter included:

- Raising the lack of investor rights at the **Roche** AGM
- Writing to **Tesco** regarding linkage between executive remuneration and good governance
- Meeting with **Centrica's** chair to discuss executive pay, succession planning and carbon management
- Meeting with **Astra Zeneca** regarding remuneration policy, mergers and governance

8.6 Councillor Kieran Quinn, chairman of LAPFF, has agreed to attend the September meeting of the Pensions Committee / Board to talk about the work of LAPFF.

8.7 Following discussions at the last Committee meeting, Councillors Blackwood and Coleman have agreed to attend the LAPFF Annual Conference in Bournemouth on 2nd – 4th December, 2015.

9. RECOMMENDATION

9.1 The Pensions Committee and Pension Board are asked to note the contents of this report and invited to comment as appropriate.

Chief Finance Officer

Date: 8 June 2015

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

NIL

Enquiries to: Bryan Smail
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Date: 12 June, 2015
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Claire Menzies-Smith
Senior Assistant Clerk
Local Government and Regeneration Committee
Room T3.40
The Scottish parliament
Edinburgh
EH99 1SP

Sent by email only

Dear Ms Menzies-Smith,

Budget Strategy Phase 2016-17 - Local Government Pension Funds

I refer to your letter of 15th May 2015.

You requested a copy of the Pension Fund Statement of Investment Principles and I have sent this as an attachment to this letter. It can also be found on the Fund website www.falkirkpensionfund.org in the Forms and Publications section.

Responses to your other questions are as follows:

1. *When your Statement is next due for review;*
The Statement of Investment Principles will be updated following a review of Fund investment strategy that is currently being undertaken. This is expected to be Autumn, 2015.
2. *Details of your social, environmental or ethical policy, and how it is implemented having regard to fiduciary duties*
This information is contained in the Fund's Statement of Investment Principles. Although fiduciary duty remains the Fund's primary focus, the Fund is aware of its responsibilities as an asset owner and gives serious recognition to environmental, social and governance (ESG) issues. ESG considerations are therefore embedded within the investment processes of the Fund and its investment managers. As evidence of this, the Fund has engaged the Pensions and Investment Research Consultants (PIRC) to provide advice on corporate governance matters. The Fund is also a member of the Local Authority Pension Funds Forum (LAPFF) which acts for over 60 UK local authority pension funds and seeks to promote high corporate standards. Recent LAPFF campaigns have targeted Executive Remuneration, Phone Hacking, Gender Equality in Boardrooms and Fossil Fuel emissions.
3. *If you have no such policy, details of how your fund deals with social, environmental or ethical considerations.*
See Response to Question 2 overleaf

In/

In relation to the questions on infrastructure,

1. *Details of any investment you have made in Scottish or UK infrastructure projects;*
 - The Fund has made a £30m commitment to invest in Social and Affordable Housing. This is expected to result in 190 additional housing units being constructed in Forth Valley.
 - The Fund has made a £30m commitment to invest in UK Infrastructure projects with a preference for projects in Scotland. An initial £2.75m commitment has been made in support of a Scottish hydro project.
 - The Fund has made an \$80m commitment to Global infrastructure with Grosvenor Capital. This investment is in a mixture of infrastructure projects and infrastructure funds some of which are invested across geographies including the UK.
2. *Whether your Fund has considered investing in the Pensions Infrastructure Platform when it opens to non-founder members*

The Fund is aware of the PIP but has not formally considered investing in it. The Fund will continue to monitor the PIP's progress, however, in view of the length of time taken for the PIP to establish itself and uncertainty as to when it may be rolled out to non-founder members, the Pension Committee's preference has been to pursue infrastructure investments through its Global and UK mandates.
3. *Whether your Fund has worked in partnership with other Scottish Local Government Pension Funds to invest in Scottish or UK infrastructure projects*

Yes. Falkirk is formally collaborating with the Lothian Pension Fund in a shared service arrangement whereby the Falkirk Fund relies on the in house expertise of the Lothian team to source investments of mutual interest. The Lothian team undertake due diligence and legal oversight of each investment opportunity, although ultimately Falkirk can elect not to participate in a particular deal.
4. *Details of the current barriers to investing in infrastructure projects.*

Perceived barriers to greater investment in infrastructure projects are as follows:

 - Breadth of specialist expertise (and "presence" in the market) that is needed to be able to source and evaluate deals, to negotiate terms, to conclude legal formalities and to record and monitor performance.
 - Pension funds have a fiduciary duty to invest fund monies for the benefit of fund stakeholders. This means that any investment with spin off social or economic benefits must be at least as favourable in terms of risk/return characteristics as an investment without these collateral benefits. Many infrastructure projects do not meet this test, having, for example, too much construction risk, regulatory uncertainty, inadequate returns, etc. In essence, funds will generally be looking for low risk opportunities that yield a minimum of RPI plus 3%.
 - The Local Government Pension Scheme (Management and Investment of Funds) regulations contain restrictions on the level of investment that can be made in partnerships (the investment vehicle normally adopted for infrastructure investments), albeit that this has not proved to be a barrier to date for this Fund.

I hope you find these comments helpful.

Yours sincerely

Chief Finance Officer



The Scottish Parliament
Pàrlamaid na h-Alba

Local Government and Regeneration Committee

To the Director of—

Dumfries and Galloway Pension Fund
Falkirk Pension Fund
Fife Pension Fund
Highland Pension Fund
Lothian Pension Fund
North East Scotland Pension Fund
Orkney Pension Fund
Scottish Borders Pension Fund
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Sent via email only

15 May 2015

Dear Sir/Madam

Budget Strategy Phase 2016-17 – Local Government Pension Funds

I am writing on behalf of the Scottish Parliament's Local Government and Regeneration Committee. Following a recommendation in the Committee's Report on Draft Budget 2015-16 (see paragraphs 61 to 66), the Committee agreed to take evidence from two panels of witnesses on the use of local authority pension funds to invest in infrastructure. The Official Report of this evidence session, which took place on 29 April 2015, is available here.

A number of points arose during the session where Members of the Committee wished to seek further background information from all Local Government Pension Funds in Scotland to inform their further consideration of the subject area. These questions are attached below.

It would be helpful if those Funds which gave oral evidence to the Committee on 29 April could also answer the questions below for ease of comparison of the information provided.

The Committee would find it helpful if you could provide **a copy of your Statement of Investment Principles**, and a note of the following:

1. When your Statement is next due for review;

2. Details of your social, environmental or ethical policy, and how it is implemented having regard to fiduciary duties;
3. If you have no such policy, details of how your fund deals with social, environmental or ethical considerations.

The Committee is also interested in your **investment in infrastructure**, in particular:

1. Details of any investment you have made in Scottish or UK infrastructure projects;
2. Whether your Fund has considered investing in the Pensions Infrastructure Platform when it opens to non-founder members;
3. Whether your Fund has worked in partnership with other Scottish Local Government Pension Funds to invest in Scottish or UK infrastructure projects;
4. Details of the current barriers to investing in infrastructure projects.

In order for the Committee to progress its considerations I would be grateful if you could **respond by close of business on Friday 12 June**. Responses should be sent, via email, to lgr.committee@scottish.parliament.uk

If you have any questions or comments about the suitability of these arrangements, please do not hesitate to contact me.

Kind regards

Claire Menzies-Smith
Senior Assistant Clerk
Local Government and Regeneration Committee

For the attention of: Paul Garrett, Dumfries and Galloway Pension Fund; Bryan Smail, Falkirk Pension Fund; Brian Livingston, Fife Pension Fund; Derek Yule, Highland Pension Fund; Alastair Maclean, Lothian Pension Fund; Steven Whyte, North East Scotland Pension Fund & Shetland Pension Fund; Gareth Waterson, Orkney Pension Fund; David Robertson, Scottish Borders Pension Fund; Richard McIndoe, Strathclyde Pension Fund; Marjory Stewart, Tayside Pension Fund.