

HAMPSHIRE COUNTY COUNCIL

Decision Report

Decision Maker:	Pension Fund Panel and Board
Date:	28 September 2018
Title:	Governance: Pension Fund Costs 2017/18
Report From:	Director of Corporate Resources – Corporate Services

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1. Recommendation

1.1. That the total cost of managing the Pension Fund for 2017/18 be noted.

2. Executive Summary

2.1. This report provides an overview of the costs of managing the Pension Fund in 2017/18.

3. Background

3.1. There are a variety of costs that are incurred in the management of the Pension Fund, which are disclosed in the Pension Fund's annual report and accounts under the following three categories:

- Investment management costs – the cost of managing the Fund's assets, which includes fees paid to the Fund's investment managers and its custodian. This includes the fees that are not paid directly for pooled and other investments, such as alternative investments like Hedge Funds and Private Equity that are netted off against investment income.
- Administration expenses – all activities the Administering Authority must perform to administer entitlements and provide members with scheme and benefit entitlement information.
- Oversight and governance – includes the costs of accounting for and monitoring the Pension Fund, plus the additional professional advice and support that is required by the Fund.

4. Total Pension Fund Management Costs

4.1. The total costs of managing the Pension Fund are shown in Table 1 below and also as a percentage of the average value of the Pension Fund in 2017/18 (2016/17 and 2015/16 costs are shown as a comparison):

Table 1: Total Pension Fund Management Costs

	2017/18		2016/17		2015/16	
	£000	%	£000	%	£000	%
Investment management	38,186	0.58	28,496	0.49	17,855	0.35
Administration	2,000	0.03	1,920	0.03	1,800	0.03
Oversight and governance	546	0.01	628	0.01	775	0.01
Total	40,732	0.63	31,044	0.53	20,430	0.39

4.2. Table 2 breaks down the investment management costs for 2017/18 by passive management, active management, and alternative investments (including property).

Table 2: Investment Management Costs for 2017/18

	£000	%
Passive investments	847	0.01
Active investments	10,419	0.16
Alternative investments (including Property)	26,513	0.41
Other (including custody and cash)	406	0.01
Total	38,186	0.58

4.3. The remainder of this report provides further detail on the three elements of the Pension Fund's management costs.

5. Investment management expenses

5.1. The Fund's business plan states that, as part of the Panel and Board's role it will make sure that its investment managers are providing value for money, it should review each year:

- the level of management fees paid to its investment managers in the previous financial year; and
- the level of transaction costs, in particular brokerage and stamp duty, incurred in the previous financial year.

5.2. Fees paid to the investment managers in 2017/18 are summarised in the confidential appendix. Fees are split into three categories:

- Direct – fees paid to investment managers as a percentage of the portfolio they manage according to their investment management agreement. Higher fees are payable to the 'active' managers who are aiming for high performance returns, with portfolios run on a passive basis attracting the lowest fees.
- Indirect – the cost of broker commissions and any stamp duty (taxes) incurred in the purchase and sale of equities and bonds by the Fund's

active managers, plus the costs incurred in the management of the Fund's direct property portfolio, such as legal and professional fees for managing tenants' leases, surveyors costs and the cost of any property repairs and maintenance that fall on the Fund, as well as any expenses incurred by investing via pooled funds.

- Pooled funds – fees applied to investments that the Fund holds, such as pooled and alternative investments. These fees will be the funds recovering their own management costs, plus performance fees in some instances. These costs are netted off against the investment income that these investments return to the Fund, so no costs are directly paid by the Fund. These costs are typically quite high due to the nature of Hedge Fund, Private Equity and Infrastructure investments, but are considered as part of the overall investment decision for every investment.

5.3. As shown in Table 1 of the confidential appendix, the cost of investment management increased as a percentage of asset value in 2017/18 in comparison to 2016/17; this was due to the following factors:

Private equity investments

5.4. A standard fee structure for a private equity/infrastructure/hedge fund investment is “2 and 20”. This means a 2% management fee, charged on commitments, and a 20% performance fee, or share of any profits. During 2017/18, the investment manager who manages the private equity portfolio made a significant number of new commitments to increase the size of the portfolio to nearer the Pension Fund's target allocation. This resulted in an overall increase in commitment of £126m and consequently the fees charged has increased, as fees are charged on the full amount committed as soon as the commitment is made, even if funds are yet to be drawn-down.

5.5. In addition the majority of the indirect costs of this portfolio during 2017/18 incurred were a one off expense due to equalisation payments. When the Pension Fund invests in a limited partnership later than the initial limited partners, the Fund is required to pay an equalisation payment in order to compensate existing investors for the Fund taking a share in assets which have gone up in value since they were originally purchased.

Direct property expenses

5.6. The direct property portfolio has associated indirect costs which vary greatly each year dependent upon the volume and value of purchases and sales, and changes in tenancy. These expenses include land registry charges, surveyors' fees, insurance revaluations, advertising, utilities charges, maintenance fees, service charge, insurance, the annual valuation, internal legal services fees, and pooled fund expenses. Included within the costs for 2017/18 were a number of refurbishments of properties which are carried out between tenancy periods.

6. Administration

6.1. The cost of administration represents the cost of the staff and systems required to record the pension benefits accrued by active and deferred

scheme members, and pay pensioners once they retire. The cost of pension administration is often described as a cost per member. For Hampshire's 167,176 scheme members this figure is £11.96. This figure is one of the lowest for an LGPS fund, which is in line with Hampshire being in the top ten largest funds.

The performance of the administration of the Pension Fund is regularly reported to the Panel and Board giving more detail on the administration of the Fund. Administration costs per member have reduced from £12.00 per member in 2016/17 to £11.96 per member in 2017/18 as the increase in administration costs for 2017/18 were slightly less than the increase in the number of members.

7. Governance and oversight

- 7.1. Governance costs include the costs of staff that produce the Fund's accounts, monitor the Fund's investment managers and support the Panel and Board. In addition it includes the various professional services, such as actuaries, lawyers, consultants and advisors, which are required in supporting the Fund's activities and the Pension Fund's share to the external costs of the creating the ACCESS pool.
- 7.2. Governance costs reduced in 2017/18 in comparison to 2016/17 due to the fact that 2016/17 was the year where the actuaries worked on the triennial valuation as at 31 March 2016, and in addition the Fund worked with the actuary on de-grouping on the Fund's employers which added additional one-off costs.

CORPORATE OR LEGAL INFORMATION:**Links to the Strategic Plan**

Hampshire maintains strong and sustainable economic growth and prosperity:	yes/no
People in Hampshire live safe, healthy and independent lives:	yes/no
People in Hampshire enjoy a rich and diverse environment:	yes/no
People in Hampshire enjoy being part of strong, inclusive communities:	yes/no
OR	
This proposal does not link to the Strategic Plan but, nevertheless, requires a decision because: For the ongoing management of the Hampshire Pension Fund.	

Other Significant Links

Links to previous Member decisions:	
<u>Title</u>	<u>Date</u>
Direct links to specific legislation or Government Directives	
<u>Title</u>	<u>Date</u>

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

DocumentLocation

None

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Due regard in this context involves having due regard in particular to:

- a) The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;
- b) Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;
- c) Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionately low.

1.2. Equalities Impact Assessment:

Equality objectives are not considered to be adversely affected by the proposals in this report.

2. Impact on Crime and Disorder:

2.1. The proposals in this report are not considered to have any direct impact on the prevention of crime.

3. Climate Change:

a) How does what is being proposed impact on our carbon footprint / energy consumption?

No specific impact.

b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

No specific impact.