



BEDFORD BOROUGH COUNCIL



Borough Charter granted in 1166

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Dear Ms Edwards

Call for Evidence on the Future Structure of the Local Government Pension Scheme

Bedfordshire Pension Fund (BPF) welcomes the opportunity to comment on the Call for evidence on the future structure of the Local Government Pension Scheme (LGPS).

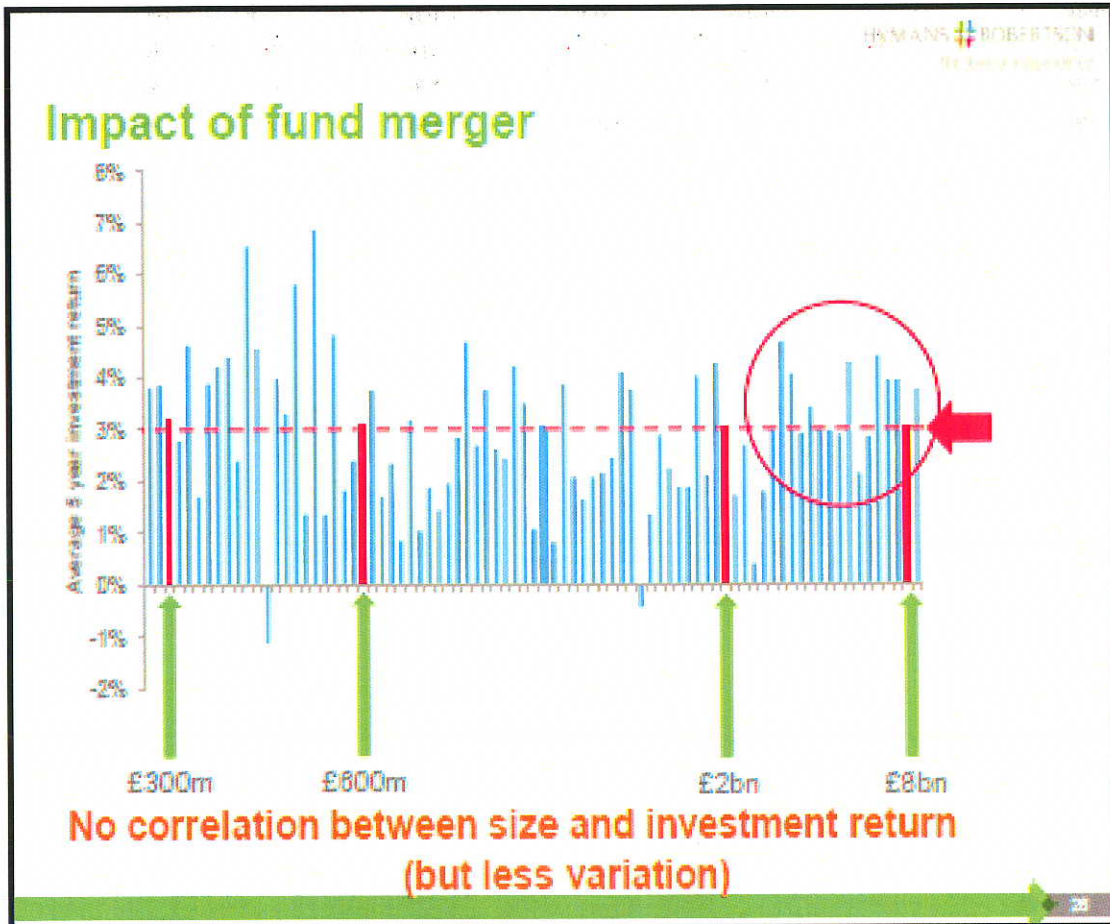
There are a number of specific questions asked and these are addressed below:

Question 1 – How can the Local Government Pension Scheme best achieve a high level of accountability to local taxpayers and other interested parties – including through the availability of transparent and comparable data on costs and income - while adapting to become more efficient and to promote stronger investment performance.

There is more than one way of achieving benefits of scale in LGPS fund investments. There are pros and cons in all of the potential approaches. Fund merger would clearly result in fewer, larger funds. However, it would require a legislative change to achieve this and considerable time and effort to implement the integration.

There is evidence that larger Funds have produced better returns; however, there is also evidence within the LGPS that the median Average 5 year return was achieved by 4 funds of differing sizes ranging from virtually the biggest to smallest. This fails to show any correlation between Fund Size and Investment performance. See chart overleaf, Source: Hymans Robertson Analysis Celtic Manor.

This Fund believes that working together with other LGPS funds is important and thus formed part of the LGPS CEM Benchmark exercise. It finds these results encouraging that the LGPS is already achieving good results on fee levels but shows that there is further work to be done in reducing costs. (Source: CEM Benchmarking press release 30 August 2013).



To achieve this goal the option, pooling of assets in common investment funds, could achieve scale benefits without fund merger. It is felt that this option could be implemented faster and without regulatory change. This approach might also realise significant scale benefits more quickly and with less disruption, while still retaining local accountability and decision making on key matters such as deficit recovery plans and asset allocation.

This Fund believes that if local council taxpayers are to play a significant part in meeting the cost of the scheme then their representatives, the Council members, need to play a significant part in running the scheme. The Fund feels that the merger of LGPS Funds would diminish the local influence to unacceptable levels.

In relation to transparency, there is a lot of information already available. There is an issue on consistency of data though between LGPS funds. A recent Financial Times article tried to compare two Funds which appeared consistent but were not. There are different auditors and approaches as to what an investment management fee is for example. To achieve fully comparable data there will need to be a greater level of definition and enforcement than currently exists and it is felt that this should be resolved prior to any major structural changes, to ensure that any cost and benefits can be appropriately identified. This was reinforced by the CEM Benchmarking exercise which required a significant amount of work, in order to produce the data to enable the benchmarking work to be completed.

BPF believes that savings can be achieved through improved investment options such as pooling investments. Information publicly available about BPF has shown an increase in investment management fees (See Annex). The more complicated the investment structure the higher the investment management costs have been. The current BPF Committee has therefore made costs a particular priority and has already seen some positive results.

Many of our investment managers recognise the size of the mandate in setting their fees. Given the synergy that 89 LGPS funds could offer for investment mandates there needs to be a simple way this synergy is captured and utilised to produce lower investment fees.

There has been much discussion in relation to merging pension fund administration sections, however, for the reasons mentioned above, poor comparative data and the marginal savings that could be achieved through administration changes in comparison to the scope to reduce investment manager fees, BPF believes investment manager fees should be the immediate focus for change.

Question 2 – Are the high level objectives listed above those we should be focussing on and why? If not, what objectives should be the focus of reform and why? How should success against these objectives be measured?

As a Fund a different investment objective has been identified:

- Optimising the return on investment consistent with a prudent level of risk over the long term.

The high level objectives should include recognition of risk and ensuring there is money to pay the right benefits when they are due.

There appears a requirement for an over-arching objective (defined by CLG/LGA) for structural reform to increase the ability of the scheme to become sustainable and affordable over the long term.

Question 3 – What options for reform would best meet the high level objectives and why?

The opportunity to better coordinate the investments, for example, through the ability to pool investments on behalf of other LGPS funds to facilitate lower fees.

In relation to Infrastructure specifically, this is something that the BPF would consider as an asset class if it can deliver the right profile of return and risk and is delivered with a satisfactory fee.

Both the high level objectives would be met by improving the net return generated to LGPS funds. Lower investment management fees would improve the net investment returns and improved net investment returns would go some way in reducing the deficit. Hymans Robertson highlighted the effect of compounding such an improvement over the 20 year time horizon many funds seek to recover their deficit.

	Assets	Liabilities	Funding Level
Today	£75	£100	75%
In 20 years ...			
7.0% pa asset growth	£290	£321*	90%
7.25% pa asset growth	£304	£321*	95%

A small improvement in net of fees performance can make a big difference

*6% per annum discount rate, ignoring future accruals & payments

Source: Hymans Robertson

The question of dealing with deficits is complicated. A deficit is caused by the financial valuation put on the liabilities of the Fund. Those valuations can change with different assumptions on discount rates, longevity, salary and inflation. The need to hedge inflation is interesting as the Fund only needs to have hedged the inflation experienced when the liabilities become due (which can be a very long time in the future) and that can be achieved by an appropriate investment asset mix without paying for any specific financial market hedge.

The best way to deal with deficits is to have a consistent measure and credible funding plans in place for the LGPS funds.

Question 4 – To what extent would the options you have proposed under question 3 meet any or all of the secondary objectives? Are there any other secondary objectives that should be included and why?

The option meets the secondary objective of lower investment fees.

Depending on how the option is implemented it may be able to meet other secondary objectives about flexibility of structures and more internal resources being available.

Question 5 – What data is required in order to better assess the current position of the Local Government Pension Scheme, the individual Scheme fund authorities and the options proposed under this call for evidence? How could such data be best produced, collated and analysed?

As referred to in the answer to question 1, the information is already available but it needs a greater level of definition and enforcement to ensure consistency. It is understood that the National Shadow Board and its sub-committees are considering the issue.

At overall scheme level, it is noted the only information being publicly correlated by Department of Communities and Local Government are the SF3 returns. There are only a small number of organisations that could collate and analyse the overall scheme data and their willingness (and cost implications) will be key in determining the appropriate organisation.

Yours sincerely



Fund Administrator