

Pensions Committee

27 March 2019

Report title	Budget 2019/2020 and Financial Plan to 2023/2024	
Originating service	Pension Services	
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Recommendations for decision:

The Committee is recommended to approve:

- a. The Operating Budget for 2019/2020.
- b. The Medium-Term financial plan for the period to 2023/2024.

1.0 Purpose

- 1.1 The purpose of this report is to seek the Committee's approval of the Operating Budget for 2019/2020 and the Medium-Term financial plan for the five years up to and including 2023/2024.

2.0 Background

- 2.1 The operating budget for 2019/2020 has been developed to reflect the objectives and priorities set out in the Fund's Service Plan, the impact of the continuing transfer of investment assets and responsibilities to LGPS Central Limited, agreed restructure proposals and action to mitigate risks highlighted in the risk register. All existing budgets have been subject to thorough review for on-going relevance and adequacy and adjusted where appropriate.
- 2.2 LGPS regulations allow for the costs of administering the Funds to be charged to the Funds themselves and not directly to employers. The actuary makes provision in the Actuarial Valuation for such costs.
- 2.3 The budget and forecast figures quoted in this report whilst expressed in terms of cost per scheme member it is recognised that this is often a blunt but widely used measure of pension schemes cost-effectiveness.
- 2.4 Regular monitoring of the budget, including the preparation of a forecast outturn, will be undertaken throughout the year and reported to Pensions Committee at quarterly intervals.

3.0 Operating Budget 2019/2020

- 3.1 The recommended Operating Budget for 2019/2020 is £82.2 million. It should be noted that this budget includes the full value of investment management costs i.e. in addition to invoiced management fees, estimates have been made for fees being deducted at source by external managers.
- 3.2 Of the total budget of £82.2 million, £81.5 million will be charged to West Midlands Pension Fund and £750,000 charged to the ITA Fund. However, recognising that the ITA Fund is making significant changes to investment strategy, it is likely that the costs to this Fund will see increases in future years, although at this stage this is not built into forecasts.
- 3.3 Table 1 sets out the proposed budget analysed by expenditure type with comparison to the 2018/19 budget.

Table 1 – Operating Budget 2019/2020

	2018/2019 Budget £'000	2019/2020 Budget £'000	Net Growth/ saving (-) Budget £'000
Employees	5,527	7,358	1,831
Premises	221	302	81
Transport	65	37	(28)
Other Supplies and Services	412	430	18
Service Development	765	949	184
Professional Fees	1,171	1,483	312
Communications and Computing	534	585	51
Support Services	544	634	90
Miscellaneous Income	(180)	(584)	(404)
Net Expenditure	9,059	11,195	2,136
External Investment Management Costs	65,201	65,936	735
LGPS Central Charges	4,425	4,669	244
Total	78,685	82,200	3,515
		-	
Funded by:		-	
West Midlands Pension Fund	77,935	81,450	3,515
West Midlands ITA Pension Fund	750	750	-
Net Budget	78,685	82,200	3,515

3.4 The main reasons for the net increase in the operating budget are:

- a) Increased staffing structure reflecting growing employer base, additional complexity of administering the Fund and new reporting requirements and ensuring that the Fund is in a position to deliver a high-quality service to scheme members, employers and broader stakeholders. This combined with a higher level of retained investment functions than had been anticipated at the outset of pooling along with ensuring proper oversight and governance of the pooling arrangements in accordance with government guidance. A fundamental review of staffing requirements to meet growing demands and building resilience means this element of the budget for staffing will see an increase of £1.8m (including an allowance for national pay awards) and has been foreshadowed at previous Committee meetings. This includes an estimate for interim resource for project work for 2019/2020 and is not carried forward to future years, representing around 15% of the additional cost in the staffing budget.
- b) A net increase in professional fees for 2019/2020 (£312,000) largely reflecting the triennial valuation year i.e. actuarial costs, along with additional risk and investment work associated with the valuation process.
- c) Higher costs relating to a mix of service development, service recharges and other ancillary costs reflecting some deferred spending from the 2018/2019 financial year as well as a requirement to develop systems to meet both growing demand on the Fund's resources and enhance capabilities.

d) Investment management costs can be difficult to forecast with a high level of accuracy given dependency on the underlying value of assets under management and also changes to asset allocation e.g. moving to more expensive asset classes for risk management and investment return purposes. At this stage Increased investment management fees resulting from assumed growth in assets under management of (£735,000). Following approval by Shareholders of LGPS Central Ltd budget an increase in the Fund's share of the Company's operational budget. It should be noted that the forecast does not include allowances for potential fee reductions which are expected to arise from investment pooling, but likewise does not include in changes to asset allocation which could see a move to more expensive asset classes for diversification and risk management purposes.

3.5 The Fund's staffing establishment stands at 140 permanent full-time-equivalent employees, including the Fund's graduate and industrial placement programme.

4.0 Medium Term Financial Plan

4.1 Table 2 sets out the Fund's forecast operating budgets for the next five years. These generally assume a continuation of existing activities, plus service development initiatives, adjusted for inflation, pay awards and other anticipated changes.

Tables 3 and 4 show the forecast cost of administration, oversight and governance per member and the cost of investment management as a percentage of net assets which are key measures of the Funds' cost efficiency over the medium term.

4.2 The forecasts reflect assumed growth of 6% per year in the value of the Funds' investment assets (inclusive of income), which links through to growth in investment management costs, being based largely on assets under management.

4.3 It is important to note that these operating budget forecasts assume that the Fund will continue to have growth in investments and costs as associated with the current structure throughout the medium-term, although it should be recognised that whilst savings in fees are expected to flow through from the roll out of LGPS Central Ltd as the Fund transitions assets, some of this may be offset by wider asset allocation changes. The forecasts for the later years can be considered as an indication of the level of costs based on the current service model, including the latest estimate of the cost of pooling. Further savings to reduce costs will be required to offset the costs of pooling. Any benefits from pooling are not anticipated within the period of this MTFP.

4.4 Tables 5 and 6 provide forecasts for all Fund activities from 2019/2020 to 2023/2024. There are some important caveats concerning these forecasts which are discussed at paragraph 4.5.

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Table 2 – Forecast Operating Budgets 2018/2019 to 2023/2024

	2018/2019 Budget £'000	2019/2020 Budget £'000	2020/2021 Forecast £'000	2021/2022 Forecast £'000	2022/2023 Forecast £'000	2023/2024 Forecast £'000
Employees	5,527	7,358	7,230	7,375	7,523	7,673
Premises	221	302	308	314	320	326
Transport	65	37	38	39	40	41
Other Supplies and Services	412	430	439	448	457	466
Service Development	765	949	450	450	450	450
Professional Fees	1,171	1,483	1,363	1,390	1,418	1,446
Communications and Computing	534	585	597	609	621	633
Support Services (CWC recharges)	544	634	647	660	673	686
Miscellaneous Income	(180)	(584)	(595)	(607)	(619)	(631)
Net Expenditure	9,059	11,195	10,477	10,678	10,883	11,090
External Investment Management Costs	65,201	65,936	69,892	74,086	78,531	83,243
LGPS Central Charges	4,425	4,669	4,949	5,246	5,561	5,895
Total	78,685	82,200	85,318	90,010	94,975	100,228
Funded by:						
West Midlands Pension Fund	77,935	81,450	84,568	89,260	94,225	99,478
West Midlands ITA Pension Fund	750	750	750	750	750	750
Net Budget	78,685	82,200	85,318	90,010	94,975	100,228

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Table 3 – Cost per Scheme Member and Investment Costs as a Percentage of Net Assets (WMPF)

	2018/2019 Budget £000	2019/2020 Budget £000	2020/2021 Forecast £000	2021/2022 Forecast £000	2022/2023 Forecast £000	2023/2024 Forecast £000
Number of Members	313,399	329,746	338,649	347,454	356,835	366,470
Total Administration, Oversight and Governance Costs (£000)	8,071	10,402	9,727	9,928	10,133	10,340
Total Administration, Oversight and Governance cost per Member (£)	25.75	31.55	28.72	28.57	28.40	28.22
Total Investment Management Costs (£000)	69,626	70,606	74,842	79,332	84,092	89,138
Investment Management Cost per Member (£)	222.16	214.12	221.00	228.32	235.66	243.23
Investment Management Costs as a Percentage of Forecast Net Assets	0.44%	0.47%	0.47%	0.47%	0.47%	0.47%

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Table 4 – Cost per Scheme Member and Investment Costs as a Percentage of Net Assets (WMITAPF)

	2018/2019	2019/2020	2020/2021	2021/2022	2022/2023	2023/2024
	Budget	Budget	Forecast	Forecast	Forecast	Forecast
Total Administration, Oversight and Governance Costs (£000)	120	120	120	120	120	120
Cost of Administration, Oversight and Governance per Member (£)	23.58	23.58	23.58	23.58	23.58	23.58
Total Investment Management Costs (£000)	630	630	630	630	630	630
As Percentage of Total Net Assets	0.13%	0.12%	0.12%	0.12%	0.12%	0.12%

Table 5 – Medium Term Forecasts (WMPF)

	2017/2018 Forecast £m	2018/2019 Forecast £m	2019/2020 Forecast £m	2020/2021 Forecast £m	2021/2022 Forecast £m	2022/2023 Forecast £m	2023/2024 Forecast £m
Contributions Receivable**	(1,089)	(335)	(350)	(660)	(674)	(694)	(715)
Other Income	(16)	(16)	(16)	(17)	(17)	(17)	(17)
Benefits Payable	555	582	610	639	669	698	728
Other Payments	0	0	0	0	0	0	0
Net Cost of Pensions	(549)	232	244	(37)	(22)	(13)	(4)
Investment Income	(198)	(211)	(219)	(230)	(242)	(257)	(272)
(Gains)/Losses in Value of Investments*	(651)	(693)	(720)	(754)	(796)	(844)	(895)
Return on Investments	(849)	(904)	(939)	(984)	(1,039)	(1,101)	(1,167)
Management Expenses	79	78	82	85	90	95	100
Net (Increase)/Decrease in the Fund	(1,319)	(594)	(613)	(934)	(969)	(1,019)	(1,071)
Opening Fund Balance	13,909	15,420	15,816	16,422	17,349	18,311	19,330
Closing Fund Balance	15,227	15,816	16,422	17,349	18,311	19,330	20,401

* Note: for 2018/2019 to 2022/2023, investment assets are forecast to grow by 6% per year.

** Note: the contributions receivable figures for 2018/2019 to 2019/2020 reflect agreements with some individual employers to pay contributions in advance in 2017/2018. Contributions 2020/2021 reflect estimate of annual contributions post the 2019 actuarial valuation

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Table 6 – Medium Term Forecasts (WMITAPF)

	2017/2018 Forecast £m	2018/2019 Forecast £m	2019/2020 Forecast £m	2020/2021 Forecast £m	2021/2022 Forecast £m	2022/2023 Forecast £m	2023/2024 Forecast £m
Contributions Receivable	(12)	(12)	(12)	(12)	(12)	(12)	(12)
Other Income	(3)	(3)	(3)	(3)	(3)	(3)	(3)
Benefits Payable	30	31	32	33	34	35	36
Net Cost of Pensions	15	16	17	18	19	20	20
Investment Income	(19)	(19)	(20)	(20)	(21)	(21)	(22)
(Gains)/Losses in Value of Investments*	(11)	(11)	(11)	(12)	(12)	(12)	(13)
Return on Investments	(30)	(30)	(31)	(32)	(33)	(34)	(34)
Management Expenses	1						
Net (Increase)/Decrease in the Fund	(14)	(14)	(14)	(14)	(13)	(13)	(13)
Opening Fund Balance	491	492	518	531	545	558	571
Closing Fund Balance	504	518	531	545	558	571	585

* Note: for 2018/2019 to 2022/2023, investment assets are forecast to grow by 6% per year, however recognising the increasing maturity of this Fund and negative cashflow position, the forecasting will be subject to review as part of the actuarial valuation.

4.5 Table 7 provides the key assumptions used in preparing the medium-term forecasts.

Table 7 – Key Assumptions

	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Pay Award	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
Consumer Price Inflation (December of preceding year)	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
Increase in Total Number of Members *	2.80%	2.70%	2.70%	2.70%	2.70%	2.70%
Gross Growth in Investment Assets	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%

* Note: this projection is based on changes in membership numbers over the last five years.

4.6 The medium-term forecasts shown in Tables 5 and 6, are subject to change, in particular because:

- a) Contributions for 2020/2021 to 2021/2022 will be influenced by the 2019 actuarial valuation, and could be significantly different from the figures shown here;
- b) The local government sector has experienced, and will continue to experience for the foreseeable future, a combination of cost pressures and funding reductions, and it is not yet possible to quantify the extent to which this will translate into a long-term reduction in the number of active scheme members;
- c) Investment income and growth in asset value are very difficult to forecast and are likely to demonstrate much greater year-on-year volatility than shown here.
- d) The impact of the transfer of funds to the LGPS Central, both in terms of growth and costs

5.0 Financial implications

5.1 The financial implications are discussed in the body of the report.

6.0 Legal implications

6.1 This report has no legal implications.

7.0 Equalities implications

7.1 This report has no equalities implications.

8.0 Environmental implications

8.1 This report has no environmental implications.

9.0 Human resources implications

9.1 The report has no human resources implications.

10.0 Corporate landlord implications

10.1 This report has no corporate landlord implications.

11.0 Schedule of background papers

11.1 Service Plan 2018-2024, Report to Pensions Committee, 27 March 2019