

# Pensions Committee

21 March 2018

<b>Report title</b>	Budget 2018/19 and Financial Plan to 2022/23	
<b>Originating service</b>	Pension Services	
<b>Accountable employee(s)</b>	George Hill Tel Email	Interim Head of Finance 01902 555244 <a href="mailto:george.hill@wolverhampton.gov.uk">george.hill@wolverhampton.gov.uk</a>
<b>Report to be/has been considered by</b>	Rachel Brothwood Tel Email	Director of Pensions 01902 551715 <a href="mailto:rachel.brothwood@wolverhampton.gov.uk">rachel.brothwood@wolverhampton.gov.uk</a>

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## Recommendations for action or decision:

The Committee is recommended to approve:

- a. The operating budget for 2018/19;
- b. The medium term financial plan for the period to 2022/23.

## **1.0 Purpose**

- 1.1 The purpose of this report is to seek the Committee's approval of the operating budget for 2018/19, and medium term financial plan for the five years up to and including 2022/23.

## **2.0 Background**

- 2.1 The operating budget for 2018/19 has been developed to reflect the objectives and priorities set out in the Fund's Service Plan, the impact of the transfer of investment assets, responsibilities and employees to LGPS Central, 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 his valuation process for such costs.
- 2.3 Being able to demonstrate value for money is crucial for the Fund, and a key measure of this is cost per scheme member. To reflect this, the budget and forecast figures quoted in this report are also expressed in terms of cost per scheme member.
- 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 2018/19**

- 3.1 The recommended operating budget for 2018/19 is £78.5 million. It should be noted that this budget includes the full value of investment management costs including fees from external managers that are deducted at source.
- 3.2 Of this total budget of £78.5 million, £77.8 million will be charged to West Midlands Pension Fund, with the remaining £750,000 charged to the ITA Fund.
- 3.3 Table 1 sets out the recommended budget by expenditure type, compared with the 2017/18 budget.

**Table 1 – Operating Budget 2018/19**

<b>Description</b>	<b>2017/18 Budget £'000</b>	<b>2018/19 Budget £'000</b>	<b>Net Growth/ Saving(-) £'000</b>
Employees	6,270	5,527	-743
Premises	300	221	-79
Transport	83	65	-18
Other Supplies and Services	640	1,177	537
Professional Fees	1,045	1,171	126
Communications and Computing	639	534	-105
Support Services	558	544	-15
Income	-5	-180	-175
<b>Sub Total</b>	<b>9,530</b>	<b>9,059</b>	<b>-471</b>
External Investment Management Costs	70,565	65,201	-5,364
LGPS Central Charges	0	4,425	4,425
<b>Total</b>	<b>80,095</b>	<b>78,685</b>	<b>-1,410</b>
<b>Funded by:</b>			
West Midlands Pension Fund	79,345	77,935	-1,410
West Midlands ITA Pension Fund	750	750	0
<b>Total</b>	<b>80,095</b>	<b>78,685</b>	<b>-1,410</b>

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

- Savings on investment management fees resulting from portfolio restructuring and reduced external management costs reflecting pressure to reduce fees (£5.4 million);
- Addition of a recharge of costs from LGPS Central of £4.4 million. This is balanced, in part, by savings from: TUPE transfer of staff; reductions in staff related budgets such as Premises, Transport and Communications; and transfer of responsibility for some Professional Fees, all totalling £1 million
- A net increase in Supplies and Services for 2018/19 (£537,000) reflecting a number of one off costs for the year, because of an increase in service development for Digital Transformation (which will deliver increased efficiency over time), Guaranteed Minimum Pensions (GMP) reconciliation work, and further data work to improve scheme member records.
- A change in presentation of Actuarial Fees which are now shown gross, within Professional Fees, including costs to be borne by employers, primarily year end accounting reports (FRS17, IAS19). This is reflected in the income increase of (£175,000);
- The overall impact of these changes is a reduction in costs funded by the WMPF of £1.4 million

- 3.5 The Fund's staffing establishment stands at 116 permanent full-time-equivalent employees. This is a reduction of 12 from 2017/18. The reduction is the net change following TUPE to LGPS Central, agreed restructure proposals, and includes 3 new graduate trainee posts.

#### **4.0 Medium Term Financial Plan**

- 4.1 Table 2 sets out the Funds' 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 shows 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 essentially assume that the Funds will continue to have growth in investments and costs as associated with the current structure throughout the medium-term. Initially, the introduction of LGPS Central adds to the overall operational Fund budget and there will be some overlap in service and provider costs in the early years as transition takes place. Additional governance and operator costs (40% of the LGPS Central charge in 2018/19), reflecting the ongoing cost of the FCA-regulated asset management company, are expected to be partially offset a by reduction in Fund service and fee costs from 2019/20. Future investment management costs (through external managers and LGPS Central) will evolve as investment strategy changes, further work is undertaken to increase cost transparency and as transition and product development plans are refined with Partner Funds and LGPS Central. The benefits from pooling, in terms of cost savings, are not anticipated to emerge within the period of this MTFP.
- 4.4 Tables 5 and 6 provide forecasts for all Fund activities from 2017/18 to 2022/23. There are some important caveats concerning these forecasts which are discussed at paragraph 5.6.

**Table 2 – Forecast Operating Budgets 2017/18 to 2022/23**

	<b>2017/18 Budget £'000</b>	<b>2018/19 Budget £'000</b>	<b>2019/20 Forecast £'000</b>	<b>2020/21 Forecast £'000</b>	<b>2021/22 Forecast £'000</b>	<b>2022/23 Forecast £'000</b>
Employees	6,270	5,527	5,310	5,454	5,565	5,673
Premises	300	221	201	205	209	213
Transport	83	65	67	68	69	71
Other Supplies and Services	640	1,177	887	904	920	937
Professional Fees	1,045	1,171	1,097	1,119	1,142	1,164
Communications and Computing	639	534	545	556	567	578
Support Services	558	544	554	566	577	588
Income	-5	-180	-184	-187	-191	-195
<b>Sub Total</b>	<b>9,530</b>	<b>9,059</b>	<b>8,478</b>	<b>8,684</b>	<b>8,857</b>	<b>9,030</b>
External Investment Management Costs	70,565	65,201	69,109	73,252	77,643	82,297
LGPS Central Charges	0	4,425	4,691	4,972	5,270	5,586
<b>Total</b>	<b>80,095</b>	<b>78,685</b>	<b>82,278</b>	<b>86,907</b>	<b>91,770</b>	<b>96,913</b>
<b>Funded by:</b>						
West Midlands Pension Fund	79,345	77,935	81,528	86,157	91,020	96,163
West Midlands ITA Pension Fund	750	750	750	750	750	750
<b>Net Budget</b>	<b>80,095</b>	<b>78,685</b>	<b>82,278</b>	<b>86,907</b>	<b>91,770</b>	<b>96,913</b>

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

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Budget	Budget	Forecast	Forecast	Forecast	Forecast
Total Administration, Oversight and Governance Costs (£000)	8,238	8,071	7,574	7,742	7,901	8,059
<b>Cost of Administration, Oversight and Governance per Member (£)</b>	<b>27.05</b>	<b>25.76</b>	<b>23.53</b>	<b>23.43</b>	<b>23.30</b>	<b>23.19</b>
Total Investment Management Costs (£000)	79,345	77,935	81,528	86,157	91,020	96,163
<b>As Percentage of Total Net Assets</b>	<b>0.52%</b>	<b>0.49%</b>	<b>0.50%</b>	<b>0.50%</b>	<b>0.50%</b>	<b>0.50%</b>

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

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Budget	Budget	Forecast	Forecast	Forecast	Forecast
Total Administration, Oversight and Governance Costs (£000)	120	120	120	120	120	120
<b>Cost of Administration, Oversight and Governance per Member (£)</b>	<b>23.34</b>	<b>23.58</b>	<b>23.58</b>	<b>23.58</b>	<b>23.58</b>	<b>23.58</b>
Total Investment Management Costs (£000)	630	630	630	630	630	630
<b>As Percentage of Total Net Assets</b>	<b>0.13%</b>	<b>0.13%</b>	<b>0.12%</b>	<b>0.12%</b>	<b>0.12%</b>	<b>0.12%</b>

**Table 5 – Medium Term Forecasts (WMPF)**

	<b>2017/18 Forecast £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Forecast £m</b>	<b>2020/21 Forecast £m</b>	<b>2021/22 Forecast £m</b>	<b>2022/23 Forecast £m</b>
Contributions Receivable**	-1,089.2	-334.5	-349.9	-659.7	-674.2	-694.4
Other Income	-15.7	-16.0	-16.3	-16.6	-16.9	17.1
Benefits Payable	555.2	582.3	610.3	639.2	669.0	697.8
Other Payments	0.3	0.3	0.3	0.3	0.3	0.3
<b>Net Cost of Pensions</b>	<b>-549.4</b>	<b>232.1</b>	<b>244.4</b>	<b>-36.8</b>	<b>-21.8</b>	<b>20.8</b>
Investment Income	-198.0	-211.0	-219.1	-229.5	-242.3	-256.8
(Gains)/Losses in Value of Investments*	-650.6	-693.2	-719.9	-754.1	-796.3	-844.1
<b>Return on Investments</b>	<b>-848.6</b>	<b>-904.2</b>	<b>-939.0</b>	<b>-983.6</b>	<b>-1,038.6</b>	<b>-1,100.9</b>
<b>Management Expenses</b>	<b>79.3</b>	<b>77.7</b>	<b>81.5</b>	<b>86.2</b>	<b>91.0</b>	<b>96.2</b>
<b>Net (Increase)/Decrease in the Fund</b>	<b>-1,318.7</b>	<b>-594.4</b>	<b>-613.1</b>	<b>-934.2</b>	<b>-969.4</b>	<b>-983.9</b>
Opening Fund Balance	13,908.5	15,227.2	15,815.6	16,421.8	17,348.9	18,310.8
<b>Closing Fund Balance</b>	<b>15,227.2</b>	<b>15,815.6</b>	<b>16,421.8</b>	<b>17,348.9</b>	<b>18,310.8</b>	<b>19,387.4</b>

\* Note: for 2018/19 to 2022/23, investment assets are forecast to grow by 6% per year. The figure for 2017/18 is an estimate based on investment performance for the year to date.

\*\* Note: the contributions receivable figures for 2017/18 to 2019/20 reflect agreements with some individual employers to pay contributions in advance.

**Table 6 – Medium Term Forecasts (WMITAPF)**

	<b>2017/18 Forecast £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Forecast £m</b>	<b>2020/21 Forecast £m</b>	<b>2021/22 Forecast £m</b>	<b>2022/23 Forecast £m</b>
Contributions Receivable	-11.8	-11.8	-11.9	-11.9	-11.9	-11.9
Other Income	-2.8	-2.9	-2.9	-3.0	-3.1	-3.2
Benefits Payable	29.7	30.6	31.5	32.5	33.5	34.6
<b>Net Cost of Pensions</b>	<b>15.1</b>	<b>15.9</b>	<b>16.7</b>	<b>17.6</b>	<b>18.5</b>	<b>19.5</b>
Investment Income	-18.8	-19.3	-19.8	-20.3	-20.8	-21.3
(Gains)/Losses in Value of Investments*	-10.7	-11.0	-11.3	-11.6	-11.9	-12.2
<b>Return on Investments</b>	<b>-29.5</b>	<b>-30.3</b>	<b>-31.1</b>	<b>-31.9</b>	<b>-32.7</b>	<b>-33.5</b>
<b>Management Expenses</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>
<b>Net (Increase)/Decrease in the Fund</b>	<b>-13.6</b>	<b>-13.6</b>	<b>-13.6</b>	<b>-13.5</b>	<b>-13.4</b>	<b>-13.2</b>
Opening Fund Balance	490.5	504.1	517.7	531.3	544.8	558.2
<b>Closing Fund Balance</b>	<b>504.1</b>	<b>517.7</b>	<b>531.3</b>	<b>544.8</b>	<b>558.2</b>	<b>571.0</b>

\* Note: for 2018/19 to 2022/23, investment assets are forecast to grow by 6% per year. The figure for 2017/18 is an estimate based on investment performance for the year to date.



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

**Table 7 – Key Assumptions**

	17/18	18/19	19/20	20/21	21/22	22/23
Pay Award	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
Consumer Price Inflation (September of preceding year)	3.00%	2.00%	2.00%	2.00%	2.00%	2.00%
Increase in Total Number of Members *	2.90%	2.80%	2.70%	2.70%	2.60%	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.

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

- a) Contributions for 2020/21 to 2021/22 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 investment portfolios and the development of asset pooling with Partner Funds and LGPS Central, both in terms of investment growth and costs.

## **6.0 Financial implications**

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

## **7.0 Legal implications**

7.1 This report has no legal implications.

## **8.0 Equalities implications**

8.1 This report has no equalities implications.

## **9.0 Environmental implications**

9.1 This report has no environmental implications.

## **10.0 Human resources implications**

10.1 The report has no human resources implications.

## **11.0 Corporate landlord implications**

11.1 This report has no corporate landlord implications.

## **12.0 Schedule of appendices**

- None

## **13.0 Schedule of background papers**

13.1 Service Plan 2018-2023, Report to Pensions Committee, 21 March 2018