

Report To: Pension Fund Management/Advisory Panel

Date: 11 March 2016

Reporting Officer: Peter Morris, Executive Director of Pensions

Subject: **MEDIUM TERM FINANCIAL PLANNING**

- Approval of GMPF investment and administration expenses budget 2016/17
- GMPF cost comparisons with other LGPS funds

Report Summary

This report will:

- (i) Review the medium term outlook for the pension fund;
- (ii) Review the medium term expenditure requirement;
- (iii) Seek approval for the 2016/17 expenditure budget;
- (iv) Show unit cost comparisons with other LGPS funds;
- (v) Set out the key assumptions on which the estimates are based.

Recommendations:

1. To approve the budget including development items for 2016/17 at £28.1 million.
2. To note the future year estimates, medium term planning and costs comparison.
3. To approve the methodology for a revised 3 year financial plan, reset from the position as at 31 March 2016. The actual figures will be reported to Employer Funding Working Group before inclusion in the Annual Report.

Policy Implications:

The areas of additional expenditure are highlighted in the report. The budget reflects changes previously approved by the Management Panel and some proposals for development. As the Business Plan actions are progressed, approval will be sought for any cost implications at the time.

Financial Implications:

(Authorised by the Section 151 Officer)

Costs of £28.1 million for 2016/2017 are estimated to be met by the Fund. This equates to 0.17% of asset value. An analysis is detailed in the report.

The unit costs of the Fund continue to demonstrate that the Fund is a relatively low cost administering authority compared to other local authority funds.

Legal Implications:

(Authorised by the Solicitor to the Fund)

It is necessary to ensure that an adequate budget is set to ensure the Administering Authority meets its statutory duties and commitments.

Risk Management:

Effective budgetary control and approval of changes in expenditure is essential to the good management of the Fund. The report also highlights potential material changes to the Fund's cash-flow. Such changes have an impact on existing risks, such as increasing volatility of cost. Further reports will be submitted to future meetings examining the risks and the

case for taking measures to mitigate those risks.

ACCESS TO INFORMATION:

NON-CONFIDENTIAL

This report does not contain information which warrants its consideration in the absence of the Press or members of the public.

Background Papers:

The background papers used in the preparation of this report were:

1. The 2015/2016 Financial Ledger
2. Budget Working Papers.

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1 EXECUTIVE SUMMARY

- 1.1 The headline figures are that during the financial year 2016/17, it is estimated that GMPF will pay £737m in pensions and receive £551m in contributions from employers and employees. The Fund had a value of £16,953m at 31 December 2015. The proposed management costs of £28.1m for 2016/17 including £22.2m on investment management represent a cost of £81 per member of the scheme. Taken separately the investment management costs equate to £64 per member or 0.13% of total assets on a projected basis, and the administration costs £17 per member.
- 1.2 The Business Plan sets out key assumptions for 2016/17 and beyond. Where the actions have financial implications, separate approvals will be sought for any additional expenditure.
- 1.3 The reporting to panel on the budget last year changed significantly from previous years to reflect the CIPFA requirement to report on medium term financial and expenditure planning. The Fund is now approaching the end of the first year of the initial 2015-18 period. This report builds on last year's report and will:
 - (i) Review the medium term outlook for the pension fund
 - (ii) Review the medium term expenditure requirement
 - (iii) Seek approval for the 2016/17 expenditure budget
 - (iv) Show unit cost comparisons with other LGPS funds.
 - (v) Set out the key assumptions on which the estimates are based.

2 MEDIUM TERM FINANCIAL OUTLOOK

- 2.1 CIPFA guidance for annual reports of LGPS Funds requires these reports to include medium term financial planning. This, as set out in the table below was included for the first time last year in both the reports to Panel and the Annual Report and Accounts using the assumptions outlined in section 6. This is indicative as benefits paid and contributions received may be materially impacted by employer decisions arising from the impact of budget reductions. Investment performance can have material effects on the out-turn. The limitations of this approach are pointedly demonstrated by this year's result which is likely to differ substantially from prediction due to disappointing investment performance.
- 2.2 The out-turn will be reported to a future meeting of the panel. The 3 year financial planning will be re-set following a realignment of the actual position as at 31 March 2016. The long term assumptions will not change. Panel are asked to approve the methodology for this and the figures will be reported to the Employer Funding Working Group in the first instance.

Table 1 – Medium Term Financial Outlook as at December 2014

	2015/16	2016/17	2017/18
	£m	£m	£m
Fund Size at Start of Year	17,591	18,272	18,936
Fund Size at end of Year	18,272	18,936	19,583
Pensions Paid	698	737	778
Contributions received	559	551	544
Transfers	0	0	0
Net Cashflow	(139)	(186)	(234)
Administration Costs	24	26	26
Investment Income	311	326	342
Increase in Value of Investments	533	550	565
Net Return from Investments	844	876	907
Net Change in Fund	681	664	647

3 MEDIUM TERM EXPENDITURE PLAN

- 3.1 The table below shows a 3 year expenditure budget for the Fund compiled last year for the period 2015/18 as reported to Management Panel on 11 December 2014.

Table 2 – Medium Term Budget as at December 2014

Type of Expenditure	2015/16	2016/17	2017/18
	£	£	£
Staff Costs	5,277,710	5,594,411	5,806,999
Investment Management & Professional Fees	16,308,206	17,711,623	18,152,140
Accommodation	414,008	347,820	354,776
Other Services	1,649,340	1,682,327	1,715,973
Central Establishment Charges	379,340	379,340	379,340
TOTAL	24,038,604	25,715,521	26,409,228

- 3.2 The table below shows the original 2015/16 budget, the projected outturn and variances. There are a number of matters that are not yet reflected in the out-turn because final decisions have not yet been determined on the most appropriate accounting treatment,

these include:

- (i) The moved into the new building and the financing of some costs incurred;
- (ii) The provision of £650,000 for non-construction costs such as ICT infrastructure and audio visual equipment;
- (iii) The internal costs recovered from MOJ in delivering the transfer of the probation service to GMPF; and
- (iv) Recovery of staff costs chargeable to investment vehicles.

Table 3 – Comparison of Projected Out-turn v Estimate 2015/16

Type of Expenditure	2015/16	2015/16 Projected outturn	Variance
	£	£	£
Staff Costs	5,277,710	5,235,887	(41,823)
Investment Management & Professional Fees	16,308,206	12,425,235	(3,882,971)
Accommodation	414,008	455,435	41,427
Other Services	1,659,340	1,688,129	28,789
Central Establishment Charges	379,340	379,340	0
TOTAL	24,038,604	20,184,026	(3,854,578)

The key variances expected for 2015/16 are as detailed below:

Table 4 – Major Variations 2015/16

		£'000
(a)	Office Equipment: Additional costs incurred in purchasing hardware for GTDH.	77
(b)	Managers and Professional Fees: rebate received and delayed implementation of Credit Manager.	(3,883)
(c)	Recovery of Management and Legal Fees: recovery of legal fees less than budget.	73
(d)	Commission Recapture: over recovery of commission recapture fees	(60)

3.3 The table below shows the revised 3 year expenditure plan.

Table 5 – Expenditure Plan 2015/16 to 2017/18

Type of Expenditure	2015/16 (projected outturn)	2016/17 (new budget in section 4)	2017/18 Revised (using assumptions)
	£	£	£
Staff Costs	5,235,887	5,807,773	5,923,928
Investment Management & Professional Fees	12,425,235	19,294,017	20,220,130
Accommodation	455,435	816,787	833,123
Other Services	1,688,129	1,793,332	1,829,199

Central Establishment Charges	379,340	379,340	379,340
TOTAL	20,184,026	28,091,249	29,185,719

- 3.4 The table shows the 2016/17 budget estimate included within the medium term financial plan presented to the Management Panel on 11 December 2014, alongside the current budget proposal for 2016/17.

Table 6 – Variations to 2016/17 Budget

<u>Type of Expenditure</u>	2016/17 as estimated at Dec 14	2016/17 (new budget in section 4)	Variance
	£	£	£
Staff Costs	5,594,411	5,807,773	213,362
Investment Management & Professional Fees	17,711,623	19,294,017	1,582,394
Accommodation	347,820	816,787	468,967
Other Services	1,682,327	1,793,332	111,005
Central Establishment Charges	379,340	379,340	0
TOTAL	25,715,521	28,091,249	2,375,728

The key variances between the estimate made in December 2014 and the estimate at February 2016 are:

		£
(a)	Staff costs: increase in Employer National Insurance costs due to the end of contracting out and Employer Pension contributions as per actuarial rates set at last valuation.	213
(b)	Managers and Professional Fees stepped increase in fees of £1.1m, increase in estimated La Salle property investment management fees of £6950k, increase in professional services fees to include £150k for transitional manager support and other changes to ad valorem fees	1,582
(c)	Accommodation: financing and operating costs for GTDH higher than anticipated	469
(d)	Other services: includes purchase of additional member and employer database software. The business case for these two new modules will be considered by the Pensions Administration Working Group before purchase.	111

4. BUDGET 2016/17 DEVELOPMENTS AND RATIONALE

- 4.1 The Fund's main area of expenditure is on investment management fees. These are either charged as a percentage of assets under management, or on a flat fee basis. This means that when the Fund's investments rise in value and/or outperform benchmarks, the fees can rise or fall in line with the market. Therefore when this expenditure rises there is often a benefit to the Fund in terms of capital appreciation that outweighs the increase in fees

paid. The Fund is also looking for its active investment managers to achieve a return in excess of the benchmark indices. The Fund is in the process of implementing significant changes to investment strategy such as introducing a new global credit manager, increasing the allocation to the global equity and property managers, which have material impact on costs as shown in the table below. The intention is that these increases in fees are more than offset by improvements in corresponding investment performance.

- 4.2 The second highest area of expenditure is staffing. A provision is built into the budget for pay awards increments and an assumption is made on the level of vacancies. The estimates for 2016/17 allows for implementation of previously approved developments and filling of some vacant posts in investments and legal, which results in an increase of £285,000 from the previous year. This also includes investments, local investments, legal, reception staff for the new building and support for the Assistant Executive Director, Funding and Development.
- 4.3 The other increase in staffing of £209,000 relates to increases in NI rates with the end of contracting out and increased employer contribution rates.
- 4.4 The budget reflects the current senior management structure. The development of pooling, and other changes in priorities and workloads may have an impact on these arrangements which will in turn impact on the budget.
- 4.5 The budget estimate for 2016/17 includes a provision of income of £175,000 which relates to work conducted by GMPF staff that is to be recharged out to other organisations such as joint ventures for investments and the costs of buying and selling properties and this offsets some of the increased spending previously built into the 2016/17 budget.
- 4.6 For premises, the budget will increase this year due to the move to the new pensions building. This significant increase is primarily a financing charge for the new office. The new building represents a step change in the facilities available and that will allow for future expansion and supports improvements in working priorities.

The main estimate of costs for the building are:

Equivalent rental charge	£347,000
Operating Costs	£218,000
Rates	£111,000
Other (Utilities, security etc.)	£141,000

- 4.7 The areas of transport, supplies and third party payments (excluding investment management fees) show no material changes.
- 4.8 For departmental & central support charges, there is no change for both this year and subsequent years.
- 4.9 The table below shows headline budget figures for 2016/17 and compares them to 2015/16. A more detailed analysis of expenditure is provided in the appendices.

Table 7 – Comparison of 2015/16 and 2016/17 Budgets

<u>Type of Expenditure</u>	2016/17	2015/16	Difference
	£	£	£
Staff Costs	5,807,773	5,277,710	530,063

Investment Management & Professional Costs	19,294,017	16,308,206	2,985,811
Accommodation	816,787	414,008	402,779
Other Services	1,793,332	1,659,340	133,992
Central Establishment Charges	379,340	379,340	0
TOTAL	28,091,249	24,038,604	4,052,645

5 COMPARISON WITH OTHER AUTHORITIES

5.1 The table below shows past, current and projected cost figures for GMPF and comparative figures from other schemes.

	2013/14	2014/15	2015/16	2016/17
	£ per member	£ per member	£ per member (Est Feb 16)	£ per member (Est Feb 16)
GMPF Admin	16.22	14.50	16.84	17.03
GMPF Investments	44.88	39.01	41.17	63.73
GMPF Total	61.09	53.51	58.00	80.76
Mets Admin	20.06	15.91	n/a	n/a
Mets Investments	45.48	148.77	n/a	n/a
Mets All	65.54	164.68	n/a	n/a
All Funds Admin	26.81	25.19	n/a	n/a
All Funds Investments	99.92	144.65	n/a	n/a
All Funds All	126.73	169.84	n/a	n/a

The comparison of investment costs on a consistent basis has always been difficult. The comparisons for 2014/15 reflect the different approaches adopted by funds for reporting their investment management costs in 2014/15 v 2015/16.

6. BASIS FOR ESTIMATES

6.1 The method used to compile estimates of expenditure for 2016/17 and future years is as follows:

Staffing	Incorporates approvals for staff changes as set out in 4.2
Investment management Fees	Where fee is linked to asset values a 4.8% increase is assumed. No performance fees are assumed. Figures reflect a reduction in the share of the assets managed passively. The 2016/17 estimate is based on asset values as at 31 December 2015.
Accommodation	New Building costs include a rental equivalent charge of £13.10 p/sqft £347,000 plus rates utilities and other operating costs.
Transport Conferences and Subsistence	Estimated requirements for current year
Services and Supplies	Contracts where usage and cost is fixed, plus estimate for variable elements. £650,000 of capital expenditure relating to ICT infrastructure audio visual equipment furniture and fittings and telephone system was charged to previous year
Inflation adjustments	2%
Investment Performance	4.8% including income as an average for the Fund which is applied across all asset class. This is taken from actuarial report.
Membership of Fund and related expenditure and income	From actuarial valuation and AED Employer Funding projections.

7. RECOMMENDATIONS

- 7.1 To approve the budget including development items for 2016/2017 at £28.1million.
- 7.2 To note the future year estimates, medium term planning and costs comparison.
- 7.3 To approve the methodology for a revised 3 year financial plan, re set with position at 31 March 2016. The actual figures will be reported to Employer Funding Working Group before inclusion in the Annual Report.

APPENDIX 1

Greater Manchester Pension Fund Administration Expenses Original Estimate 2016/17

Type of Expenditure

Staff Costs

Direct Salaries
Direct On-Costs
Indirect On-Costs

Direct Costs

Publications and Subscriptions
Travel and Subsistence
Premises
Postage, Printing, Telephone
Office Equipment and Software
Investment Advisory Expenses
Bank Charges and Nominee Fees
Managers and Professional Fees
Performance Measurement Services
Communications

Central Establishment Charges

Less:

Recovery of Management and Legal Fees
Admin Fees
Commission Recapture

	(1) Original Estimate 2015/16	(2) Changes	(3) Original Estimate 2016/17
	£'000	£'000	£'000
-			
	4,160	285	4,445
	1,073	209	1,282
	45	36	81
	5,278	530	5,808
	66	4	70
	32	68	100
	414	403	817
	311	28	339
	943	113	1,056
	52	(2)	50
	380	6	386
	16,308	2,986	19,294
	96	6	102
	150	10	160
	18,752	3,622	22,375
	379	0	379
	(251)	(100)	(351)
	(20)	0	(20)
	(100)	0	(100)
	24,038	4,052	28,091