

Report of the Director of Customer & Business Support Services

Pension Investment in fossil fuels

Purpose of report

1. At its meeting on 8th October 2105 Council agreed a motion that required a report to Audit & Governance setting out the details of York's current direct and indirect investments in fossil fuels including current investment by North Yorkshire Pension Fund (around 7% of total according to 350.org) and giving a range of options for action on both direct and indirect investments, including an option to commit to no future investment and proposals for a process of total divestment and proposals to initiate similar discussions about their Pension Fund Policies & Strategies with the Pension Fund Committee (PFC) of the North Yorkshire Pension Fund.

Background

2. North Yorkshire County Council (NYCC, the Council) is the statutory administering authority for the North Yorkshire Pension Fund, which is part of the Local Government Pension Scheme (LGPS). All aspects of the Fund's management and administration, including investment matters, are overseen by the Pension Fund Committee (PFC). The Leader of City of York Council is a member of this committee.
3. The purpose of the Fund is to provide retirement benefits specified by the LGPS regulations for staff working for local authority employers, and other employers admitted by agreement, in the North Yorkshire area. The regulations also specify the member contribution rates as a percentage of pensionable pay, with employer contribution rates being set every three years by the Fund's Actuary. These contributions are supplemented by earnings on the Fund's investments in order to pay retirement benefits.
4. The day to day running of the Fund is delegated to the Treasurer who is the Corporate Director – Strategic Resources of the Council and is responsible for implementing the decisions made by the PFC. Supporting him is a team of

staff split into two sections. The Pensions Administration team administers all aspects of member records, pension benefits etc and the Integrated Finance team looks after the accounting and management information requirements of the Fund. All aspects of the day to day management of investment funds are undertaken by external fund managers

5. During the year the PFC meet, supported by its Independent Investment Adviser, Investment Consultant and the Independent Professional Observer, as well as the Treasurer. The Committee meetings provide a forum for discussion about economic and market trends, monitoring the performance of the investment managers and considering their individual investment strategies.
6. The government has published guidance for pooling Local Government Pension Scheme Fund assets into up to 6 British Wealth Funds, containing at least £25 billion of Scheme assets each. The government is now inviting administering authorities to come forward with their proposals for new pooled structures in line with the guidance to significantly reduce costs while maintaining overall investment performance, with the wider ambition of matching the infrastructure investment levels of the top global pension funds.

Analysis

7. NYCC is required, as the administering authority, to invest any NYPF monies which are not immediately required to pay pensions and other benefits. The LGPS Management and Investment of Funds Regulations 2009 set out certain restrictions as to individual investments, the purpose of which is to limit the exposure risk of an LGPS fund.
8. As at 31 March 2015 the following investment management arrangements were in place.
 - Baillie Gifford managed two active global (ie including UK) equity portfolios, namely Global Alpha and Long Term Global Growth (LTGG). Each of these portfolios is in the form of a pooled vehicle, rather than being invested in segregated holdings. Both are managed without reference to a benchmark, however the FTSE All World index is used for performance measurement purposes
 - Fidelity managed an active overseas equities (ex UK) portfolio comprising segregated holdings in overseas companies against a composite MSCI World (ex UK) index

- Standard Life managed an active UK equity portfolio comprising segregated holdings in UK companies against the FTSE 350 (excluding investment trusts) equally weighted index
- Amundi managed an active global fixed income portfolio through a pooled fund, against the “least risk” benchmark of index linked and fixed interest gilts
- ECM managed an active European corporate bond portfolio through a pooled fund on an absolute return basis, using 1-month LIBOR for performance measurement purposes
- M&G managed an active Gilts portfolio comprising segregated fixed income and index linked holdings, against the “least risk” benchmark
- Hermes managed an active UK Property portfolio through a pooled fund with the objective of outperforming the retail price index (RPI)
- Threadneedle and Legal & General both managed active UK Property portfolios during the year through pooled funds with the objective of outperforming RPI
- Standard Life and Newton both managed Diversified Growth Fund portfolios during the year through the Global Absolute Return Strategy (GARS) and Real Return (RR) pooled funds respectively, with the objectives of significantly outperforming the cash benchmark

9. The Fund also has a small investment in the Yorkshire & Humber Equity Fund. The residual cost of this investment at the year end was £0.08m.

10. The nature of the investments market, particularly the equity portfolios, means that it is difficult to clearly identify exactly where funds are ultimately invested. As an example, as at March 2015 14.9% of the NYPF was invested with Standard Life equity funds. The table below sets out the different sectors invested in by the Standard Life Equity Fund. This fund totals £2,094.5m as at 30/9/15.

Sector	% of equity fund
Financials	19.5
Industrials	14.5
Oil & Gas	9.2
Telecommunications	7.3
Utilities	4.0
Cash and Other	1.6
Consumer Services	14.9
Consumer Goods	12.9

Health Care	7.6
Basic Materials	5.2
Technology	3.3

11. The Council is not able to influence how and where these funds invest. They can only, through attendance at the Pension Committee, influence the investment strategy of NYPF. The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 require administering authorities to prepare a statement recording the investment policy of the Fund. The main areas covered by the statement are:
- Investment decision making process
 - Types of investments to be held
 - Balance between different types of investments
 - Risk
 - Expected return on assets
 - Realisation of investments
 - Socially responsible investments
 - Shareholder governance
 - Stock lending
 - Compliance with guidance from the Secretary of State
12. Furthermore, the government has recently published guidance for pooling Local Government Pension Scheme Fund assets into up to 6 British Wealth Funds, containing at least £25 billion of Scheme assets each. The government is now inviting administering authorities to come forward with their proposals for new pooled structures in line with the guidance to significantly reduce costs while maintaining overall investment performance, with the wider ambition of matching the infrastructure investment levels of the top global pension funds. In the light of this potentially significant change, it is considered unlikely that the PFC will consider a substantial change in the direction of the fund investment policy at this time.

Consultation

13. It is important to note that the NYPF is for the benefit of staff members who contribute to the scheme. Therefore, any recommendation which could see reduced performance of the fund should be consulted upon with all staff.

Implications

14. The implications are
- Financial – any decision to change the investment policy of the NYPF could result in a reduced return, which could in turn lead to increased contributions from the Council to make up any deficit.
 - Human Resources - there are no human resource implications to this report.
 - Equalities – there are no equality implications to this report.
 - Legal – pension fund investment managers are legally required to maximise returns for staff who contribute to the pension scheme. Any change in investment policy will need to be consulted upon with members of the scheme and formally agreed by the Pension Committee
 - Crime and Disorder - there are no crime and disorder implications to this report.
 - Information Technology - there are no information technology implications to this report.
 - Property –there are no property implications to this report.
 - Other – there are no other implications to this report.

Risk Management

15. Risk management is the process by which the Fund identifies and addresses the risks associated with its activities. Risk management is a key part of the North Yorkshire Pension Fund's governance arrangements, and the Pension Fund has its own dedicated risk register. Risks are identified and assessed, and controls are in place to mitigate risks. The Fund's risk register is reviewed every year, and the latest review highlighted:
- Pension Fund solvency remains a high risk due to the unpredictable and volatile nature of global financial markets on which both investment returns and certain market based actuarial assumptions used to value liabilities are based. The potential consequence of the risk occurring is a significant increase in contribution rates for the Fund's employers and/or an extension to the deficit recovery period. Despite a fall in solvency over the last year due to falling Gilt yields, the Fund investment strategy has continued to provide strong returns. No remedial action is presently required in order to deliver the deficit recovery plan.
 - The investment strategy has moved from a red to an amber risk, reflecting the low probability (under 30%) that it will fail to deliver adequate returns. The Fund's strong performance in every year since the financial crisis and

the diversification through the addition of new asset classes and managers are key reasons for this.

Recommendations

16. Members are asked to note the contents of the report and suggest any further areas they wish to see considered.

Reason: To ensure that the Council motion of 8 October 2015 is actioned.

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Specialist Implications Officer(s) None

Wards Affected: *List wards or tick box to indicate all* **All**

For further information please contact the author of this report

Background Working Papers

None