

Pensions Committee

2.30 p.m., Wednesday, 17 December 2014

Pension Fund Cost Benchmarking

Item number	5.7
Report number	
Executive/routine	
Wards	All

Executive summary

The purpose of this report is to inform Committee of summary conclusions of the benchmarking of investment for Lothian Pension Fund and pensions administration costs for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund.

The report on investment costs relies on data provided by CEM, an independent provider of benchmarking data. Its database is comprised of 357 global pension funds. CEM concludes that Lothian Pension Fund's costs are low compared with those of the global peer group. This is almost certainly due to the Fund's 'implementation style' – the Fund manages a relatively high percentage of assets internally compared with the universe of pension funds.

Pension administration cost per member for this Council (£24.90) has been maintained at a similar level for the last few years and appears to be within the expected range, although this is higher than the selected local authority peer group.

Qualitative assessment of performance for both investment and pension administration is difficult to ascertain given the lack of readily comparable statistics.

Links

Coalition pledges

Council outcomes

CO26 - The Council engages with stakeholders and works in partnerships to improve services and deliver agreed objectives.

Single Outcome Agreement

Pension Fund Cost Benchmarking

Recommendations

- 1.1 Committee is requested to:
- Note the report;
 - Note that the CEM Investment Benchmarking Analysis and the CIPFA Pensions Administration Benchmarking 2014 comparator reports have been provided, on a confidential basis, to the Convener of the Pensions Committee, Convener of the Pensions Audit Sub-Committee and the Independent Professional Observer.

Background

- 2.1 The annual report 2013/14 for the pension fund identifies £31million of costs, with investment costs representing by far the largest proportion of the Fund's total expenses.
- 2.2 Benchmarking can be a helpful tool to help drive improvements and deliver value for money. It is intended that participation in the benchmarking of service provision should facilitate:
- Comparison between the costs and performance;
 - Provision of evidence to support decisions on budget and improvement and thereby enhance customer satisfaction;
 - Sharing of information and ideas with peer(s)
 - Review of LPF performance trends over time.
- 2.3 In an effort to better understand its investment expense base, Lothian Pension Fund has contributed to CEM's database for the last two years. CEM's global database comprises 357 funds representing £5.0 trillion in assets, three fifths of which are based in North America. It includes 35 UK pension funds with aggregate assets of £196bn. The size of the funds range between £30 million and £510 billion. The median fund size was £2.9bn, which compares with Lothian Pension Fund's assets under management of £4.3bn at 31 December 2013. However, care should be taken in deriving conclusions from the headline data. CEM itself states that "being high or low cost is neither good nor bad". What matters is whether a pension fund is receiving sufficient value for the costs incurred. This is reflected in the long term returns of pension funds, net of costs.

- 2.4 Chartered Institute of Public Finance and Accountancy (CIPFA) pensions administration benchmarking club has been used for a number of years to assess the costs of administration of the Lothian Pension Fund, Lothian Buses Pension Fund and the Scottish Homes Pension Fund. The outputs and analyses have served to supplement internal performance management information.

Main report

CEM Investment Cost Benchmarking Analysis

- 3.1 CEM aims to provide comparable data but is unable to capture all investment costs from all funds. Accordingly, it excludes transaction costs and private asset performance fees from its analysis. For this reason, and also because the data is collected on a calendar year basis rather than a financial year basis, the actual costs differ from those reported in Lothian Pension Fund's annual report.
- 3.2 CEM calculates a benchmark cost for Lothian Pension Fund reflecting the Fund's size, asset mix and domicile. Lothian's actual cost of approximately 0.50% was below the benchmark cost of 0.59%. The 0.09% difference amounts to approximately £3.5m per year.
- 3.3 CEM concludes that the primary reason for costs being low compared with the benchmark is almost certainly 'implementation style' – a relatively high percentage of assets are internally managed and fund-of-fund usage is less than average. External active management tends to be much more expensive than internal management, while fund-of-funds tend to be the most expensive type of external management.

CIPFA Pensions Administration Benchmarking Club

- 3.4 The CIPFA Pensions Administration Benchmarking Club aims to collect the transactional volumes and processing costs for administering members' LGPS benefits (i.e. excluding investment) using standard definitions. "Employing authority work" and any work associated with the administration of non-LGPS pensions are excluded.
- 3.5 Each administering authority has scope to select a suitable peer group for the "comparator report" and also the submission by any individual LGPS administering authority is also available through the club database "interactive" report. The selected peer group comprises similar sized English and Welsh authorities, but also including some from Scotland. In total, nineteen Funds are included.
- 3.6 CIPFA has stated that, in order to protect its commercial interests, its report "Pensions Administration Benchmarking Club 2014" "cannot be put in the public domain. It is for internal uses only within the authority....and for contacting and communicating with other members of the club". Accordingly, the full comparator and interactive reports have been provided, on a confidential basis,

only to the Convener of the Pensions Committee, Convener of the Pensions Audit Sub-Committee and the Independent Professional Observer.

- 3.7 It is emphasised that it would be incorrect to derive definitive conclusions on the basis of apportioned costs. This is an inherent issue given the scale of central support costs which are typically apportioned to the pension fund by the host Councils, the extent of co-provision of employer services and also the bases of overhead apportionment to the pension administration function, as distinct from other activities within the Fund Accounts.
- 3.8 Recognising this caveat, summary findings on costs and other observations on differences in the make-up of the Fund are as follows:
- LPF cost per member of £24.90 is within the range of the 18 comparable funds, £14.85 to £27.23. However LPF cost is higher than the peer group average (£20.28);
 - Cost per member for LPF has been maintained at a similar level for the last few years. LPF cost and the average from a similar peer group from 2008/09, were £24.39 and £19.86 respectively;
 - Staff costs (£13.34 per member for LPF) show similar results to those of total costs;
 - Active members represent a higher percentage of overall membership for LPF than the peer group average, but not significantly so. The proportion of pensioners to total membership is again higher, with the consequence being that the proportion of deferred members is lower than that of the typical fund. These factors would tend to increase pension administration and payroll workload;
 - Previous benchmarking reports have showed LPF as having the highest number of employers (in 2008/09, approximately 170 compared to an average of 105). Recently in England, the average number of employers has increased significantly with the inclusion of academy schools as separate entities and now LPF's number of employers is broadly comparable with the average; and
 - LPF's staff turnover was low in the year to 31 March 2014 relative to other funds although it should be noted that LPF turnover has increased significantly in 2014/15.

Performance Benchmarking

- 3.9 Qualitative assessment of performance for both investment and pension administration is difficult to ascertain given the lack of readily comparable statistics.
- 3.10 CEM highlights that investment costs should be taken in the context of a fund's long term net returns. However, relevant comparisons of long-term returns are not readily available.

- 3.11 For pension administration, fewer than half the peer group, including LPF, have provided “industry standard performance indicators” to CIPFA. Work is being progressed to ensure that this can be provided in future.

Pensions Administration - Service Improvement Initiatives

- 3.12 Benchmarking reports in recent years have showed higher payroll costs for LPF compared to a peer group. This was one of the drivers behind the transfer of the payroll service in 2013 from the Council’s payroll system to the pension administration system. Payroll cost per pensioner is now broadly in line with the average.
- 3.13 Efficient electronic transfer of member data has also been the focus over recent years, including the recent implementation of PensionsWeb, which has helped to improve efficiency as well as customer service.
- 3.14 Lothian Pension Fund is actively engaged on the matter of consistency of performance indicators with the pension administration supplier in order to facilitate performance reporting on a consistent basis in future. From April 2014, Lothian Pension Fund has revised its performance management information in order to best comply with The Pensions Regulator and CIPFA’s requirements. Comparison with other funds should be available for 2014/15.
- 3.15 Officers of the Fund continue to learn from other pension funds on a regular basis including site visits to specific funds as well as attending regular meetings of the Scottish Pensions Liaison Group.
- 3.16 The need to focus on continuous improvement to the pensions administration service is recognised. The Fund intends to review its pensions administration procedures to ensure continuing alignment to best practice and also reinforce performance management where appropriate. This will include further liaison with other LGPS administering authorities. Synergies with current initiatives being undertaken by Corporate Governance Directorate with regard to the maintenance of member records and also the potential for channel-shifting to more efficient web-based self-service methods will be explored.

Measures of success

- 4.1 Benchmarking of costs provides management information, which serves to inform the service planning and budgetary process of the three Lothian Pension Funds.

Financial impact

- 5.1 There are no financial implications arising directly from this report. Out of the pension funds' total cost of £31million for 2013/14, pension administration costs included in amounted to £2.014million, with the remaining largely attributable to investment. Continuous improvement initiatives will be met from the approved budget 2014/15.

Risk, policy, compliance and governance impact

- 6.1 The provision of summarised conclusions of benchmarking is intended to enhance the governance of the three Lothian Pension Funds.

Equalities impact

- 7.1 There are no adverse equalities impacts arising from this report.

Sustainability impact

- 8.1 There are no adverse sustainability impacts arising from this report.

Consultation and engagement

- 9.1 The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading / external references

Not applicable.

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Links

Coalition pledges

Council outcomes CO26 - The Council engages with stakeholders and works in partnerships to improve services and deliver agreed objectives.

Single Outcome Agreement

Appendices None