SCOTTISH BORDERS COUNCIL
PENSION FUND COMMITTEE AND PENSION BOARD

MINUTES of Meeting of the PENSION FUND COMMITTEE AND PENSION BOARD held in Council Chamber, Council Headquarters, Newtown St Boswells on Thursday, 14 September 2017 at 10.00 am

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Present:-	Councillors D Parker (Chairman), J A Fullarton, D Moffat, S Mountford, S Scott, S Aitchison, Mr M Drysdale, Ms K Hughes, Ms L Ross.
Apologies:-	Councillors Brown, Edgar, Mr A Barclay, Mr C Hogarth, Mr P Smith.
In Attendance:-	Chief Financial Officer, Capital and Investment Manager, HR Shared Services Manager, Mr D O'Hara (KPMG), Mr Singh (KPMG), Democratic Services Officer (J Turnbull).

1. **MINUTE**
There had been circulated copies of the Minute of the Meeting of 22 June 2017.

DECISION
NOTED for signature by the Chairman.

2. **PENSION FUND INVESTMENT & PERFORMANCE SUB-COMMITTEE**
There had been circulated copies of the Minute of the Pension Fund Investment and Performance Sub-Committee dated 21 August 2017.

DECISION
NOTED the Minute.

3. **PRESENTATATION - ENVIRONMENTAL SOCIAL GOVERNANCE**
Mrs Robb, Capital and Investment Manager gave a presentation to the Pension Fund Committee and Pension Board on Environmental Social Governance (ESG). Mrs Robb began by detailing the joint committee's fiduciary duties: Any policy should not specifically exclude the choice of investment purely based on non-financial consideration; the committee should seek to obtain the best return for the Fund while acting prudently; and, that there should be no policy in place that would restrict the choice of investment available to the Fund. Members also had to ensure that they did not to use any information for their own benefit or take part in any decision where they had a conflict of interest. Mrs Robb advised that the Fund's current position with regards to ESG was contained in the Statement of Investment Policy (SIP). The SIP recognised the committee's responsibility to exercise voting rights and that these voting rights had been delegated to investment managers. KPMG's report provided a brief summary of how investment managers had used these voting rights at shareholders meeting. Mrs Robb went on to advise that to ensure investment managers fulfilled the Fund's ESG responsibilities, they had all been encouraged to sign up to the United Nations Principles Responsible Investment (UNPRI) Stewardship Code. Mrs Robb asked the joint committee to consider if they felt this was sufficient to fulfil ESG responsibilities? Mrs Robb concluded by advising that the following presentations from PIRC and Baillie Gifford would provide further information to assist in their decision.

DECISION
NOTED the presentation.

4. **PRESENTATION - VOTING CONSULTANT**
The Chairman welcomed Mr Ian Jones and Ms Tessa Younger from PIRC, presentation slides had been circulated with the agenda. Mr Jones began by advising that PIRC had

been set up by pension funds in 1986. They were regulated by the Financial Conduct Authority (FCA) and were recognised as a professional body, providing institutional investors with corporate governance advice on proxy matters including voting. PIRC were a large team, focused purely on corporate governance and responsible investment issues. For UK portfolios, including many pension funds, they provided a proxy reporting service, incorporating environmental and social analysis, governance coverage and voting recommendations. Mr Jones continued that PIRC focused on capital maintenance and the stewardship of capital. They undertook extensive research for their clients, unpicking unreliable accounting practices and calculating the costs. PIRC were completely independent, with no corporate conflicts, therefore could raise difficult issues with companies. For example, PIRC had been the market leader on calling for a shareholder vote on executive remuneration. Presently they were taking a stance on share buy backs and pre-emption rights. Mr Jones went on to detail their research process, highlighting issues that were relevant to the client's portfolio e.g. environmental issues such as low carbon emissions. Ms Younger then detailed PIRC's service which included: a global coverage of client equity portfolios; a proxy report, incorporating environmental and social analysis; coverage in any market based on a client's own corporate governance policy; voting guidelines and capital strategies/stewardship coverage. In response to a question, Mr Jones advised that the charge for their service would be dependent on the Pension Fund's portfolio, a quotation could be provided if required. Regarding a question on PIRC's ethical policy, Ms Younger advised that their engagement with companies could make a difference. PIRC would also report on ESG issues that might have an impact on shareholder values. In response to a question regarding interaction and possible conflict with investment managers, Mr Jones advised they did not interact directly with investment managers. PIRC advised the client and then voted directly for the client; alternatively, they issued the client with a report and the client executed the vote themselves or through their investment managers. In terms of fund performance, Mr Jones advised that there would be no direct effect, PIRC's emphasis being on stewardship duties, engagement with companies and ensuring that their clients had robust engagement with companies when exercising their voting rights. The Chairman thanked Mr Jones and Ms Younger for their attendance and presentation.

DECISION
NOTED the presentation.

5. **PRESENTATION - BAILLIE GIFFORD**

The Chairman welcomed Mr Tom Wright and Mr Andrew Cave, Baillie Gifford, who were in attendance to continue the above discussion from an investment manager's perspective. Mr Wright began by advising that Baillie Gifford's ongoing assessment of governance was a core part of understanding companies. Their assessment might change their view on buying, selling or resizing their clients' holdings. It also determined how they used their voting rights at shareholder meetings and their engagement with managers, which they considered were two principal levers for influencing change. Their assessment also factored in a company's performance in relation to ESG issues. For example, researching companies exposed to carbon issues and also investigating emerging issues, such as Google and Amazon's tax status. Voting rights were an integral part of their commitment to stewardship and an important part of their long term investment process, for this reason they preferred to retain this responsibility. In response to a question regarding the joint committee's ESG considerations, Mr Cave responded by referring to Ryanair and the companies unconventional approach to labour relations. Their view differed from PIRC in that they considered brand, future earnings potential and the reputation of business when considering a long term investment. Mr Cave continued that a formulaic approach to governance could also be restrictive. For example, attempting to vote a successful Chief Executive such as Mark Zuckerberg, Facebook, off a board because they were also company chairman did not make sense from an investment perspective. In response to a question regarding share buy-back, he advised that they would not be opposed to this if it was to benefit the company. With regard to the voting service they offered, it was explained that they offered a bespoke, fully customised service for each client. Mr Cave acknowledged that it appeared they had not provided sufficient details when communicating their voting decisions. He advised that future investment reports would contain more information and include specific examples, which could be discussed by the committee. In response to a question regarding their investment in smaller UK companies, the Chief Financial Officer, Mr Robertson, advised that Baillie Gifford had undertaken to provide a presentation on their UK Smaller Companies Fund at the next appropriate Pension Fund Investment Sub-Committee. The Chairman thanked Mr Wright and Mr Cave for their attendance and presentation.

DECISION
NOTED the presentation.

6. **KPMG - SUMMARY**

Mr O'Hara, Lead Investment Advisor - KPMG, discussed the presentations. He clarified that the joint committee had been given two different models to consider. Presently, the committee delegated all voting rights to their investment managers. With regard to Baillie Gifford, they had a strong, research team and included detailed information in their reports. However, not all of the committee's investment managers supplied a similar analysis. The alternative was for the committee to appoint a company such as PIRC. They could provide a service that would consolidate information and: (a) provide a report for the committee to consider and vote direct, which in terms of the present committee structure would be challenging; (b) vote on the committee's behalf, this would mean taking the right away from investment managers and transferring this responsibility to PIRC; (c) provide research and vote on the committee's behalf; and or (d) engage with companies and represent the committee. Mr O'Hara considered that the issue appeared to be around reporting and challenging the information provided by investment managers and not the outsourcing of voting responsibility. In response to questions, Mr O'Hara advised that transferring voting rights to PIRC would not change the investment managers' strategies. He further advised that KPMG could place pressure on investment managers to improve the information they provided to the committee. KPMG could also carry out due diligence and provide more detailed reports. However, this would not be to the same level as PIRC could provide. There would also be an additional charge for this work. The joint committee discussed the presentations and it was agreed that voting rights should remain with the investment managers. However, it was requested that more detailed information on their voting choices be included in their reports. The committee also requested that KPMG provide information on the additional service they could provide, including costs.

DECISION
AGREED

(i) That voting rights remain with Investment Managers;

(ii) To request that Investment Managers provide more detail in their reports on their voting choices;

(iii) To request the KPMG provide further information on the additional service they could provide, including costs; and

(iv) To bring back a further report back for the Committee's consideration at the next meeting.

7. **RISK REGISTER UPDATE**

With reference to paragraph 10 of the Minute of 22 June 2017, there had been circulated a report by the Chief Financial Officer which formed part of the risk review requirements and provided the Pension Fund Committee and Pension Board with a full register and proposed management actions to mitigate risks. Identifying and managing risk was a corner stone of effective management and was required under the Council's Risk

Management Policy and process guide and CIPFA's guidance "Delivering Governance in Local Government Framework 2007". It was further reflected and enhanced in the "Local Government Pension Scheme" published by CIPFA. A full risk review was undertaken on 10 May 2017 and the revised risk register was approved by the Joint Pension Fund Committee and Pension Board on 22 June 2017. Appendix 1 to the report detailed the risks within the approved risk register which have been identified as management actions and the progress of these actions to date. In response to questions Mrs Robb advised that no new risks had been identified. With regard to Risk 4.1, she advised that Liquidity was progressing and there would be an update at the next meeting. With regard to Risk 6.2, she explained that legislation changes were monitored on a regular basis.

DECISION

(a) AGREED to a key risk review being undertaken in December 2017 and reporting of progress on the risk management actions.

(b) NOTED:

(i) No the management actions progress as contained in Appendix 1 to the report; and

(ii) New quantifiable risks had been identified since the last review.

8. **GUARANTEED MINIMUM PENSION (GMP) RECONCILIATION**

There had been circulated a report by the Chief Officer Human Resources seeking approval to engage external support to progress the reconciliation of Guaranteed Minimum Pension (GMP) between the Pension Fund and Her Majesty's Revenue and Customs. The Business Plan approved on 22 June 2017 agreed to the carrying out of a full reconciliation of GMP amounts between the Pension Fund and Her Majesty's Revenue and Customs, this report gave consideration as to how the Fund could achieve this. The reconciliation exercise should be carried out for Stage 1 and Stage 2 as outlined in paragraph 4.4 of the report, through the use of external resources, with Stage 3 to be completed in-house. The appointment of external assistance to meet the deadline of 31 December 2018 was proposed to be undertaken via procurement under the Norfolk framework by direct award.

Mr Angus, HR Shared Services Manager, advised that there would be a one off payment of £1,500 to utilise the Norfolk Framework. The cost would be fully met from the Pension Fund. The cost for undertaking the GMP reconciliation was estimated at a maximum of £99,000 this cost would also be fully met from the Pension Fund.

DECISION

AGREED:

(a) The use of the Norfolk Framework for the procurement;

(b) To delegate responsibility for the direct award of external resources to completed the Guaranteed Minimum Pension reconciliation exercise, capped at a maximum of £99,000, to the Chief Financial Officer

9. **BUDGET MONITORING TO 30 JUNE 2017**

There had been circulated a report by the Chief Financial Officer providing the Pension Fund Committee and Pension Board with an update position of the Pension Fund budget to 30 June 2017 including projections to 31 March 2018. The Local Government Pension Scheme (Scotland) Regulation 2014 required Administering Authorities to ensure strong governance arrangements and set out the standards they were to be measured against. To ensure the Fund met the standards a budget was approved on 16 March 201, following the recommendations within the CIPFA accounting guidelines headings. This report was the first quarterly monitoring report of the approved budgets. The total expenditure to 30 June 2017 was £0.026m with a projected total expenditure of £3.928m. This was against an approved budget of £3.829m giving a negative projected variance of

£0.099m. The variance had resulted from the externalisation of the GMP reconciliation as detailed in a separate report.

DECISION

(a) NOTED the actual expenditure to 30 June 2017; and

(b) AGREED the projected expenditure of £3.928m as the revised budget.

10. **MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE (MIFID II)**

There had been circulated a report by the Chief Financial Officer provides information on the rules for implementation of the Markets in Financial Instruments Directive (MiFID II), which was effective from 3 January 2018. Following a review by the European Commission the rules for Markets in Financial Instruments Directive (MiFID) was due to change on 3rd January 2018. The change would result in all UK Local Authority pension funds being automatically reclassified from “professional investors” to “retail” clients by default. The re-classification of “retail” would result in the Fund being unable to invest any financial instrument including the Fund’s current investments as set out in Funds Investment Strategy. To allow continued investment in the required classes the Fund required to apply to “opt-up” to “professional” status. The Local Government Association was currently developing a reporting template in conjunction with the Investment Association, which the Fund would be able to utilise for the “opt up” process.

DECISION

(a) NOTED the pending reclassification of the Fund to “retail” status under MiFID II

(b) AGREED

(i) The Fund would complete the required documentation to “opt up”; and

(ii) To notify the Fund’s Investment Managers and the Custodian of the intention to “opt-up”.

11. **COMMUNICATION STRATEGY**

There had been circulated a report by the Chief Financial Officer requesting approval of the Communication strategy for the Pension Fund Committee and Pension Board. The Communication Strategy would improve engagement with its members and enhance the availability of information via the establishment of a website for the Pension Fund. The Business plan approved on 22 June 2017 agreed to the development of a Communication Strategy and establishment of a website for the Pension Fund. The overarching Communication Strategy was detailed in paragraph 4.2 of the report and covered communication with all stakeholders. The implementation of the Communication Strategy and its website was proposed to be undertaken via a procurement under the Norfolk framework. The key dates of the procurement were detailed in paragraph 4.6. Under the procurement, a shortlist of bidders would be asked to present to Members of the Pension Fund Appointment Sub-Group with the final recommendations being presented to the Joint Pension Fund Committee and Pension Fund Board on 8th March 2018.

DECISION

(a) AGREED:

(i) The Communication Strategy as detailed in paragraph 4.2 of the report attached with the Agenda;

(ii) The use of the Norfolk Framework for the procurement;

(iii) The timetable as detailed in paragraph 4.6 of the report attached with the agenda.

(iv) The appointment of Councillors Parker, Mountford, Scott and Moffat as Members of the Appointment Sub-Group.

(b) **NOTED further reports and updates would be provided at future meetings.**

12. **INFORMATION UPDATE**

12.1 There had been circulated a briefing note by the Chief Financial Officer providing members of the Committee and Board with an update on a number of areas which were being monitored and progressing. Full reports on individual actions would be tabled as decisions and actions were required. In summary:-

12.2 **Tri-Annual Valuation**
The next valuation would take place in 2017 based on 31 March 2017 data. All queries and data would be completed by the end of September to allow the findings to be reported to the joint meeting on 4 December 2017.

12.3 **Progress on Investment Strategy Implementation**
The revised Investment Strategy was approved in September 2016 and updated on 16 March 2017. The Strategy now included an allocation to infrastructure which had resulted in three new managers and the requirement to rebalance a number of investment categories. Following a procurement process new managers were appointed for Private Credit and Long Lease Property. Due to the nature of new investments and the notice period for disinvestment of funds from LGT for the Alternative allocation, the implementation of the full revised Strategy would take approximately two years.

12.4 **Scheme Advisory Board Update**
Membership of the Scheme Advisory Board, representing the employer side, was currently being finalised. Following receipt of the final nomination, formal appointment letter would be issued to SPPA. The first meeting of the new Board was anticipated to be early October. The Chairman advised that he had been appointed to the National Scheme Advisory Board for teachers' pensions.

12.5 **Training Opportunities**
An investment training opportunity has been circulated by LGC. Training was two half days in Edinburgh, a number of members had already registered to attend. The IGG Group, a Pension Fund Officer group for LGPS's was organising a training event on 21 November. An agenda would be circulated once finalised. It was noted that officers would be available in the old Convener's office on 17 and 18 October to assist members in the completion of the Pension Fund Regulatory Trustee toolkit.

DECISION
NOTED the information update.

13. **ITEMS LIKELY TO BE TAKEN IN PRIVATE**
AGREED under Section 50A(4) of the Local Government (Scotland) Act 1973 to exclude the public from the meeting during consideration of the business contained in the following items on the ground that they involved the likely disclosure of exempt information as defined in paragraphs 6 and 8 of the part 1 of Schedule 7A to the Act.

SUMMARY OF PRIVATE BUSINESS

14. **MINUTE**
The Committee noted the Private Minute of the meeting of 22 June 2017.

15. **PENSION FUND INVESTMENT & PERFORMANCE SUB-COMMITTEE**
The Committee noted and agreed the Private Minute of the Pension Fund Investment and Performance Sub Committee on 21 August 2017.

16. **QUARTER PERFORMANCE UPDATE**

The Committee noted a Private report by KPMG.

17. **PROPERTY INVESTMENT UPDATE**
Members considered and approved a report by the Chief Financial Officer providing an update on the status of the property mandate and its ongoing restructure.

18. **INFRASTRUCTURE INVESTMENT - PROJECT**
Members considered and approved a report by the Chief Financial Officer regarding an infrastructure investment made by the Fund under delegated authority.

The meeting concluded at 1.00 pm