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PUBLIC

To: Members of Pensions and Investments Committee

Tuesday, 1 September 2020

Dear Councillor,

Please attend a meeting of the **Pensions and Investments Committee** to be held at **10.30 am** on **Wednesday, 9 September 2020** virtually; the agenda for which is set out below.

Yours faithfully,

Simon Hobbs
Director of Legal and Democratic Services

A G E N D A

PART I - NON-EXEMPT ITEMS

1. Apologies for Absence

   To receive apologies for absence (if any)

2. Declarations of Interest

   To receive declarations of interest (if any)

3. Minutes (Pages 1 - 8)

To confirm the non-exempt minutes of the meeting of the Pensions and Investments Committee held on 21 July 2020

4. To consider the reports of the Director of Finance and ICT on:

4 (a) Investment Report (Pages 9 - 90)

4 (b) Stewardship Report (Pages 91 - 134)

4 (c) Framework and Climate Strategy (Pages 135 - 154)

4 (d) SAAB & Investment Strategy Statement Report (Pages 155 - 182)

4 (e) Exit Credits Policy (Pages 183 - 190)

4 (f) MHCLG Amendments to the Statutory Underpin Consultation (Pages 191 - 266)

5. Exclusion of the Public

To move "That under Regulation 21 (1)(b) of the Local Authorities (Executive Arrangements) (Access to Information) (England) Regulations 2000, the public be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information as defined in Paragraph(s)… of Part 1 of Schedule 12A to the Local Government Act 1972"

PART II - EXEMPT ITEMS

6. Declarations of Interest

To receive declarations of interest (if any)

7. Minutes (Pages 267 - 268)

To confirm the exempt minutes of the meeting of the Pensions and Investments Committee held on 21 July 2020

8. To consider the exempt report of the Director of Finance and ICT on AADP Stage 2 (Pages 269 - 408)

PUBLIC

MINUTES of a meeting of the **PENSIONS AND INVESTMENTS COMMITTEE** held on 21 July 2020

PRESENT

Councillor J Perkins (in the Chair)

Derbyshire County Council

Councillors N Atkin, J Boult, P Makin, R Mihaly and B Ridgway

Derby City Council

Councillors L Care and M Carr

Derbyshire County Unison

Mr M Wilson

Also in attendance – D Kinley, P Peat, N Smith and S Webster.

N Calvert, R Graham and K Gurney (Derbyshire Pension Board)

Apologies for absence were received on behalf of Councillors R Ashton and S Marshall-Clarke (Derbyshire County Council).

27/20 **CHAIRMAN'S ANNOUNCMENTS** The Chairman welcomed Councillor Lucy Care to her first meeting of the Committee following her recent appointment from Derby City Council.

The Chairman announced that Mrs Kay Riley, the Assistant Director of Legal Services and the Committee's adjudicator for applications at AADP was soon to retire. On behalf of the Committee, Councillor Perkins wished to thank Mrs Riley for all the help and support she had given to members and this committee over the years, and wished her all the very best for the future.

28/20 **MINUTES** **RESOLVED** that the minutes of the meeting held on 10 June 2020 be confirmed as a correct record.

29/20 **PUBLIC QUESTION TO THE COMMITTEE** The following question had been received from Divest Derbyshire and Derbyshire Pensioners Action Group following the provision of their survey of members:

What is the response of the Pension Committee to the results of the survey?

Dawn Kinley, Head of Pension Fund responded as follows:

Councillor Perkins has asked me to acknowledge receipt of the results of a survey carried out by Divest Derbyshire and Derbyshire Pensioners Action Group to gather the views of members of the Pension Fund on how the Fund is invested. The results cover the views of the 128 members of the Fund who responded to the survey.

As previously noted, the Fund is currently developing a climate strategy, and is reviewing its Investment Strategy Statement. These strategies will be considered by this Committee in September and then the Fund's stakeholders, including the members and employers, will be consulted on the strategies before final approval. The results of the survey will considered at that time alongside the responses to the official consultation.

We intend to write to all of our members and employers to highlight the consultation in order to improve our engagement with members and we have also committed to developing a forum for our members as part of the development of the member self-service system.

The development of a meaningful climate strategy is difficult in the context of a pension fund which is required to deliver returns, taking into account risk, and when the climate related information on which decisions are based is so variable. Climate related disclosures from companies continue to develop and providers of climate related data and analytics can interpret climate related scores in very different ways. This adds to the complexity of formulating an appropriate strategy but we are making good progress and look forward to presenting the proposed strategy to Committee for consideration in September.

30/20 **EXIT CREDITS POLICY** The Local Government Pension Scheme Regulations 2013 (the 2013 Regulations) had been amended in 2018 to allow exit credits to be paid for the first time. The changes came into effect on 14 May 2018 but were backdated to 1 April 2014. Where an employer ceased to be a participating employer in the Local Government Pension Scheme (LGPS), an exit credit became due if their pension liabilities had been overfunded at their date of exit. The amendment was introduced to give administering authorities more flexibility to manage liabilities when employers had left the LGPS and to allow pension risks to be shared more fairly.

In May 2019, the Secretary of State for Housing, Communities and Local Government had opened a consultation on a number of proposed changes to the 2013 Regulations, including a proposed further change to the rules on exit credits. MHCLG announced its intention to amend the 2013 Regulations so that administering authorities may determine, at their absolute discretion, the amount of any exit credit payment due, having regard to any relevant

considerations. The 2020 Regulations came into force on 20 March 2020, but had effect from 14 May 2018, and details of the Regulations were presented.

The new responsibility placed on the administering authority for determining the level of any exit credit and the discretion available made it essential that the Fund adopted a fair and reasonable exit credits policy. The Fund's Exit Credits Policy (the Policy) would be incorporated into the Fund's Admission, Cessation and Bulk Transfer Policy which had been approved on 22 January 2020.

Given the potential impact on participating employers of the Fund's exercise of its discretion in relation to exit credits, the Fund would consult with scheme employers, the local pension board and other stakeholders on the proposed policy. The consultation period would run until 16 August 2020 and the results of the consultation will be reported to Committee in September 2020.

Members raised concerns that the costs associated with the determination of an exit credit could be significant and it was suggested that these costs be deducted from any exit credit payment at the Fund's discretion. This would be considered by officers when finalising the Policy.

Approval was sought for the Director of Finance & ICT, in conjunction with the Chairman of the Committee to consider the results of the consultation in the meantime, and to determine if any revisions to the proposed Policy were necessary following the consultation, to enable the Policy to be adopted as soon as possible. Members requested that the findings from the consultation be brought to the Committee for information.

RESOLVED to (1) approve the proposed Exit Credits Policy attached as Appendix 1 to the report, subject to the outcome of the consultation with the Fund's stakeholders; and

(2) delegate the consideration of the results of the consultation, and the determination of whether any revisions to the proposed Exit Credits Policy were necessary following the consultation, to the Director of Finance & ICT in conjunction with the Chairman of the Committee.

31/20 **DERBYSHIRE PENSION FUND RISK REGISTER** It was reported that the Fund's Business Continuity Plan had worked well and all of the Fund's critical activities had been maintained throughout the period of business disruption.

As a result of the current pandemic the Risk Register had been reviewed through a different lens, which had resulted in the addition of two new risks, one related to the governance framework (Risk No.1) and one related to internal and external suppliers (Risk No.17). Further details of these risks were

provided. The narratives attached to Risk No.2 (staffing risk) and Risk No.23 (employer covenants) had been strengthened due to the current situation, however the risk scores had not changed. The Risk Register has the following five High Risk items:

(1) Fund assets insufficient to meet liabilities (Risk No.19)
(2) Failure to consider the potential impact of climate change (Risk No.22)
(3) LGPS Central related underperformance of investment returns (Risk No.29)
(4) Impact of McCloud judgement on funding (Risk No.36)
(5) Impact of McCloud judgement on administration (Risk No.43)

An update relating to the McCloud judgement was provided. It was reported that MHCLG had recently issued a consultation on its proposed remedy for LGPS to extend the transitional protection 'underpin' to all active members between April 2014 and March 2022. This would create a huge administration task and a McCloud Project Team had been established to formalise the governance of this major impending project. It was anticipated that the first meeting of the Project Team would be held shortly. It was proposed that a response to the consultation would be brought to this Committee for approval in September, prior to submission to MHCLG.

In addition to the risk related to climate change, three other new risks had been added to the Risk Register and two risks related to the recruitment and retention of staff had been combined into one risk (Risk No.2).

(Risk No.1): The risk of failing to provide effective leadership, direction, control and oversight of the Pension Fund was particularly considered during the recent period of business disruption. This risk had been attributed an impact score of 5 (very high) and a probability score of 2 (unlikely). Robust governance arrangements were in place for the Pension Fund and the arrangements for maintaining the critical activities of the Fund during a period of business disruption had worked well.

(Risk No. 17): The risk of the internal providers of services (including treasury management, payments, pensioner payroll and legal advice) and the external providers of the pension administration system, actuarial services and fund management activities, being unable to provide their services to the Fund during a period of business disruption, had also been particularly considered in recent months. The business continuity arrangements of these providers had been received and continuity arrangements had worked well during the period of business disruption related to the Covid 19 pandemic.

(Risk No. 18): Exit credit payments had been introduced into the LGPS in April 2018. Amending legislation came into force in March 2020 allowing administering authorities of LGPS funds to exercise their discretion in

determining the amount of any exit credit due, having regard to certain listed factors plus 'any other relevant factors.' This discretion was open to wide interpretation and potential challenge from employers. This risk had been attributed an impact score of 3 (medium) and a probability score of 3 (possible). Legal and actuarial advice had sought in the formulation of the Exit Credits Policy presented to the Committee and the Fund would seek further external advice on a case by case basis if required.

The total risk score of employer contributions not being received and accounted for on time (Risk No. 25) had been increased from a 3 (low risk) to a 9 (medium risk) in recognition of the financial pressures on employers related to the Covid 19 pandemic. The Fund had reminded employers of their responsibility to provide information and to pay contributions by relevant deadlines.

The total risk score related to the risk of the new pension administration system failing to meet service requirements (Risk No. 38) had been reduced from a 9 to a 6 as the Altair system had now achieved business as usual status.

RESOLVED to note the risk items identified in the Risk Register.

32/20 **APPOINTMENT OF ADJUDICATOR FOR AADP STAGE 1 APPLICATIONS AND ESTABLISHMENT OF AN APPEALS SUB-COMMITTEE FOR AADP STAGE 2 APPLICATIONS** The current adjudicator for applications at AADP Stage 1 against decisions made by the administering authority, was Mrs Kay Riley, Assistant Director of Legal Services, Derbyshire County Council. Due to the impending retirement of Mrs Riley, it was necessary for the Fund to appoint a new adjudicator.

In order to maintain continuity of the role within the Legal Services Department of the County Council, it was proposed that Mrs Riley's successor in post as Assistant Director of Legal Services be appointed to the role of administering authority adjudicator for the consideration of applications at AADP Stage 1.The recruitment process was currently underway and it was proposed that the successful candidate would be announced to the committee in September.

To date, the Committee's cycle of 8 meetings per year had enabled AADP Stage 2 applications to be considered within the 2 months' statutory timeframe allowed. However, that may not always be possible in the adjusted future cycle of 6 meetings per year. In order to reduce the likelihood of an application being considered outside the 2 months' timeframe, Committee was asked to establish an Appeals Sub-committee.

The sub-committee's terms of reference would be to solely consider AADP Stage 2 applications which could not be determined within the 2 months limit by the revised meetings cycle of the main Committee. The sub-committee would be comprised of three members of the main Committee and would be chaired by the Chairman of the main Committee. A summary of all cases determined by the Committee and sub-committee would be reported to Committee after each year ending on 31 March.

Following discussions between the Members it was felt that rather than form a sub-committee to hear the Stage 2 applications, an extra virtual meeting of the full committee could be arranged at relatively short notice when these instances arose.

RESOLVED (1) to note that Mrs Riley's successor in post as Assistant Director of Legal Services will be appointed as the adjudicator for AADP Stage 1 appeals where scheme members disagreed with a decision of the Pension Fund; and

(2) that the establishment of an Appeals Sub-committee to consider cases outside of the 2 months' timeframe allowed, was not required.

33/20 **EXCLUSION OF THE PUBLIC** **RESOLVED** that the public be excluded from the meeting during the Committee's consideration of the remaining items on the agenda to avoid the disclosure of the kind of information detailed in the following summary of proceedings:-

SUMMARY OF PROCEEDINGS CONDUCTED AFTER THE PUBLIC HAD BEEN EXCLUDED FROM THE MEETING

1. To receive declarations of interest (if any)

2. To confirm the exempt minutes of the meeting held on 10 June 2020 (contains exempt information)

3. To consider the exempt report of the Director of Finance and ICT on LGPS Investment Pooling (contains information relating to the financial or business affairs of any particular person (including the Authority holding that information))

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Agenda Item No. 4 (a)

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

9 September 2020

Report of the Director of Finance & ICT

INVESTMENT REPORT

1 Purpose of the Report

To review the Fund's asset allocation, investment activity since the last meeting, long term performance analysis and to seek approval for the investment strategy in the light of recommendations from the Director of Finance & ICT and the Fund's independent adviser.

2 Information and Analysis

(i) Report of the External Adviser

A copy of Mr Fletcher's report, incorporating his view on the global economic position, factual information for global market returns, the performance of the Fund and his recommendations on investment strategy and asset allocation, is attached as Appendix 1.

(ii) Asset Allocation and Recommendations Table

The Fund's latest asset allocation as at 31 July 2020 and the recommendations of the Director of Finance & ICT and Mr Fletcher, in relation to the Fund's strategic asset allocation benchmark, is set out overleaf.

The table also shows the recommendations of the Director of Finance & ICT, adjusted to reflect the impact of future investment commitments. These commitments (existing plus any new commitments recommended in this report) relate to Private Equity, Multi-Asset Credit, Property and Infrastructure and total around £310m (£320m at 30 April 2020). Whilst the timing of drawdowns will be lumpy and difficult to predict, the In-house Investment Management Team (IIMT) believes that these are likely to occur over the next 18 to 36 months.

Asset Category	Benchmark	Fund Allocation	Fund Allocation	Permitted Range	Benchmark Relative Recommendation		Recommendation		Adjusted for Commitments (1)	Benchmark Sterling Return	Benchmark Sterling Return
		30/04/20	31/07/20		AF 9/09/20	DPF 9/09/20	AF 9/09/20	DPF 9/09/20	DPF 9/09/20	3 Months to 30/6/20	3 Months to 31/7/20
Growth Assets	**57.0%**	**53.2%**	**54.6%**	**+/- 8%**	**-**	**(1.0%)**	**57.0%**	**56.0%**	**57.7%**	**n/a**	**n/a**
UK Equities	16.0%	15.8%	15.3%	+/- 4%	-	-	16.0%	16.0%	16.0%	10.2%	1.3%
Overseas Equities:	37.0%	34.2%	36.2%	+/- 6%	-	(0.2%)	37.0%	36.8%	36.8%	n/a	n/a
North America	12.0%	10.6%	11.2%	+/- 4%	-	(1.0%)	12.0%	11.0%	11.0%	21.9%	9.3%
Europe	8.0%	7.8%	8.4%	+/- 3%	-	-	8.0%	8.0%	8.0%	18.8%	11.8%
Japan	5.0%	6.3%	5.6%	+/- 2%	-	+0.6%	5.0%	5.6%	5.6%	12.2%	(0.2%)
Pacific ex-Japan	4.0%	4.6%	4.2%	+/- 2%	-	+0.2%	4.0%	4.2%	4.2%	19.8%	12.4%
Emerging Markets	5.0%	4.3%	4.6%	+/- 2%	-	-	5.0%	5.0%	5.0%	18.9%	13.6%
Global Sustainable	3.0%	0.6%	2.2%	+/- 2%	-	-	3.0%	3.0%	3.0%	19.7%	9.0%
Private Equity	4.0%	3.2%	3.1%	+/- 2%	-	(0.8%)	4.0%	3.2%	4.9%	10.3%	1.5%
Income Assets	**23.0%**	**21.3%**	**20.7%**	**+/- 6%**	**+2.0%**	**(2.0%)**	**25.0%**	**21.0%**	**24.7%**	**n/a**	**n/a**
Multi-Asset Credit	6.0%	6.1%	6.1%	+/- 2%	+2.0%	0.2%	8.0%	6.2%	7.7%	6.5%	6.0%
Infrastructure	8.0%	6.9%	6.8%	+/- 3%	-	(1.0%)	8.0%	7.0%	9.0%	0.6%	0.6%
Direct Property (3)	5.0%	4.9%	4.5%	+/- 2%	+1.0%	(0.5%)	5.0%	4.5%	4.5%	(2.2%)	(2.2%) (2)
Indirect Property (3)	4.0%	3.4%	3.3%	+/- 2%	(1.0%)	(0.7%)	4.0%	3.3%	3.5%	(2.2%)	(2.2%) (2)
Protection Assets	**18.0%**	**18.3%**	**18.1%**	**+/- 5%**	**(2.0%)**	**(0.1%)**	**16.0%**	**17.9%**	**17.9%**	**n/a**	**n/a**
Conventional Bonds	6.0%	5.8%	5.5%	+/- 2%	(3.0%)	(0.5%)	3.0%	5.5%	5.5%	2.5%	(0.1%)
Index-Linked Bonds	6.0%	6.2%	6.2%	+/- 2%	-	-	6.0%	6.0%	6.0%	10.3%	6.0%
Corporate Bonds	6.0%	6.3%	6.4%	+/- 2%	+1.0%	+0.4%	7.0%	6.4%	6.4%	8.5%	5.1%
Cash	**2.0%**	**7.2%**	**6.6%**	**0 – 8%**	**-**	**+3.1%**	**2.0%**	**5.1%**	**(0.3%)**	**0.0%**	**0.0%**

Total Investment Assets totaled £5,142m at 31 July 2020.
(1) Recommendations adjusted for investment commitments at 31 July 2020 and presumes all commitments are funded from cash.
(2) Benchmark Return for the three months to 30 June 2020.
(3) The maximum permitted range in respect of Property is +/- 3%.

The table above reflects the following three categorisations:

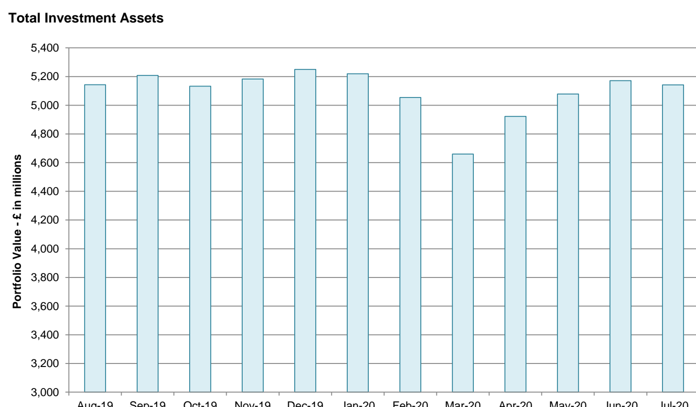
- **Growth Assets**: largely equities plus other volatile higher return assets such as private equity;
- **Income Assets**: assets which are designed to deliver an excess return, but with more stable return patterns than Growth Assets because income represents a large proportion of the total return of these assets; and
- **Protection Assets**: lower risk government or investment grade bonds.

Relative to the benchmark, the Fund as at 31 July 2020, was overweight in Protection Assets and Cash, and underweight in Growth Assets and Income Assets.

If all of the Fund's commitments (existing plus any new commitments recommended in this report) were drawn-down, the cash balance would reduce by 6.0% to -0.3%. However, in practice as these commitments are drawn-down, they will be partly offset by new net cash inflows from investment income, distributions from existing investments and changes in the wider asset allocation.

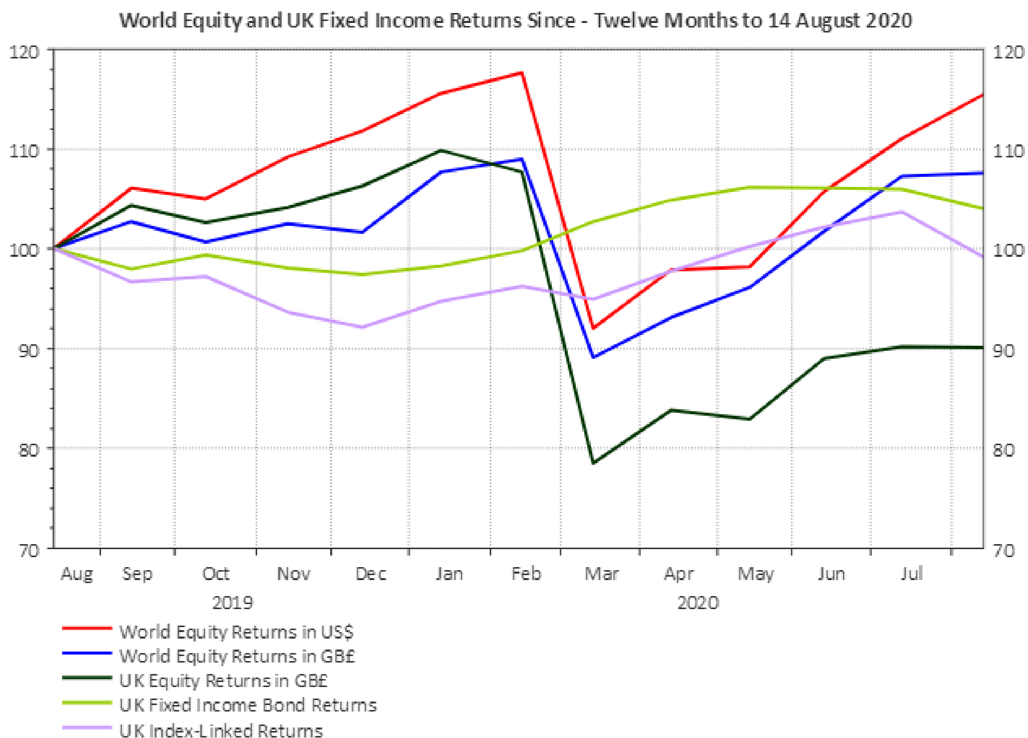
(iii) Total Investment Assets

The value of the Fund's investment assets increased by £219m (+4.5%) between 30 April 2020 and 31 July 2020 to £5.142bn, comprising a non-cash market gain of around £200m, and cash inflows from dealing with members & investment income of around £20m. Over the twelve months to 31 July 2020, the value of the Fund's investment assets has fallen by £32m (-0.6%), comprising a non-cash market loss of around £190m, partly offset by an advance contribution of £58m and cash inflows from dealing with members & investment income of around £100m. A copy of the Fund's valuation is attached at Appendix 2.



The Fund's valuation can fluctuate significantly in the short term, reflecting market conditions, and supports the Fund's strategy of focusing on the long term.

(iv) Market returns over the last 12 months



The chart above shows market returns for Global Equities in Sterling and the US dollar, UK Equities, UK Fixed Income and UK Index Linked bonds for the twelve months to 14 August 2020.

Q2 2020 was a very strong quarter for equities and credit as central banks and governments acted quickly to provide unprecedented levels of stimulus and economies started to reopen. Despite the strong rebound in risk assets, sovereign bonds held up well.

As economies started to reopen, economic indicators improved, supported by the willingness of central banks to keep government and corporate borrowing costs low. For example, the policy measures taken by the UK government included a Coronavirus Job Retention Scheme, tax deferrals, business grants and loan guarantees. UK borrowings are now likely to exceed 15% of national income, or over £300bn, in 2020-21; the biggest deficit since World War II. The worst case scenario of the Covid19 pandemic causing a liquidity crisis was avoided.

The FTSE All World Index in US dollar terms recovered the vast majority of the losses reported across February and March 2020, and in the year to 14 August 2020 provided a positive total return of 16.8%. The return for sterling investors was lower at 9.0% as the pound strengthened against the US dollar; safe haven demand for the US dollar fell in Q2 2020, and US real yields (nominal yield less the rate of inflation) fell compared to the wider market.

Despite a significant fall in US Q2 2020 GDP (annualised fall of 32.9%; around 10% quarter-on-quarter decline (qoq)), and an increase in the number of Covid 19 new infections from mid-June 2020, US equities returned +13.8% in local currency terms in the three months to 31 July 2020 (+2.9% year to date (YTD)). Markets chose to look through the economic data and focus on the economic recovery, the ongoing fiscal and monetary support, and positive news about the development of several vaccines; it is too early to say whether these vaccines will be successful and receive full regulatory approval. Sector performance varied significantly. For example, online retailers performed strongly, whereas traditional high-street retailers underperformed, along with other sectors that have been most affected by the Covid 19 pandemic, such as travel and leisure. Quality significantly outperformed value.

Asia Pacific Ex-Japan and Emerging Market equities were the strongest performing regions in local currency terms in the three months to 31 July 2020, returning +17.0% and +18.2%, respectively, reflecting a weaker dollar (+1.4% and -2.1% YTD).

UK equities were one of the worst performing regions in the three months to 31 July 2020, returning +1.3% (-20.5% YTD). The UK went into recession in Q2 2020, with Q2 2020 GDP falling by 20.4% (qoq), significantly higher than many other developed markets, driven by a sharp fall in consumer spending, and the dominance of the UK service sector which was hard hit by the Covid19 pandemic. Brexit uncertainty also continued to weigh on investor confidence and business investment.

UK sovereign bonds held YTD gains despite the sharp recovery in equity markets. UK Gilts returned -0.1% in the three months to 31 July 2020, whereas UK Index-Linked bonds returned 6.0% as the significant rise in Quantitative Easing (central bank purchases of bonds) and stagflation fears (stagnant economic activity coupled with higher inflation) pushed up inflation expectations. G7 yields remain near historic lows, consistent with expectations for a prolonged period of zero-or-below policy rates in response to the economic backdrop.

Investment grade and non-investment grade (i.e. high-yield bonds) credit also rallied, as credit spreads narrowed, following the US Federal Reserve's announcement that it would purchase investment grade bonds and 'fallen angels' (i.e. investment grade bonds downgraded to high yield status) to support credit markets. Credit spreads are now closer to these immediately prior to the Covid19 pandemic.

The IIMT note that while markets have rebounded sharply since the lows of March 2020, the recovery is heavily dependent on continued fiscal and

monetary stimulus, and the assumption that the number of new cases can be controlled without the need for further national lockdowns. Whilst it appears that the number of new cases has been brought under control in much of Asia and Europe, there continues to be regional outbreaks, and the number of new cases in the USA is an ongoing concern. Furthermore, new cases are rising in several emerging markets, including India and much of Latin America. The economic recovery may take several years, with countries emerging from the Covid 19 pandemic at different rates. The longer it takes for activity to return to normal, the longer the potential for long-term economic damage.

Political risk also remains, with the US election fast approaching, tensions between the USA and China escalating (UK relations with China have also deteriorated), and Brexit uncertainty continuing as trade negotiations between the UK and European Union appear to make little progress.

Capital Economics note that whilst there has been an encouraging initial rapid pick-up in economic activity, households and firms remain in cautious mode, preventing a full V-shaped recovery. While policy is set to remain supportive, the recent huge stimulus must ultimately be wound down with likely adverse effects. Capital Economics believe that after shrinking by around 4.5% this year, the world economy will be over 3% smaller than it would have been without the coronavirus outbreak by the end of 2022. The recovery will be uneven, with China, Korea and Taiwan amongst those furthest along the road to recovery, while economies in southern Europe, Latin America and Africa will lag behind.

It is also notable that the International Monetary Fund (IMF) has downgraded its global growth forecasts for 2020 from -3.0% in April 2020 to -4.9% in June 2020 (-8.0% advanced economies / -3.0% emerging markets). The IMF forecast that global growth will pick-up to +5.4% in 2021, but by the end of 2021, the global economy will still be 6.6% smaller than forecast before the start of the Covid 19 pandemic.

Asset class weightings and recommendations are based on values at the end of July 2020. As shown in the charts below, equity markets have now largely recovered most of the March 2020 sell off, albeit this differs by market. For example, the US market is now generally higher than at any time in the last five years, whereas the recovery in the UK market has been much more muted.

(v) Longer Term Performance

Figures provided by Portfolio Evaluation Limited show the Fund's performance over 1, 3, 5 and 10 years to 30 June 2020.

Per annum	**DPF**	**Benchmark Index**
1 year	0.8%	1.1%
3 year	4.2%	4.1%
5 year	7.4%	6.9%
10 year	8.5%	8.2%

The Fund under-performed relative to the benchmark over one year but out-performed the benchmark over all other time periods.

(vi) Category Recommendations

	Benchmark	Fund Allocation	Permitted Range	Recommendation		Benchmark Relative Recommendation	
		31 Jul-20		AF	DPF	AF	DPF
Growth Assets	57.0%	54.6%	± 8%	57.0%	56.0%	-	(1.0%)
Income Assets	23.0%	20.7%	± 6%	25.0%	21.0%	+2.0%	(2.0%)
Protection Assets	18.0%	18.1%	± 5%	16.0%	17.9%	(2.0%)	(0.1%)
Cash	2.0%	6.6%	0 – 8%	2.0%	5.1%	-	+3.1%

At an overall level, the Fund was overweight Protection Assets and Cash at 31 July 2020, and underweight Growth Assets and Income Assets, although if commitments waiting to be drawn down were taken into account, the Fund would move to an overweight position in Growth and Income Assets. The table on page 2 assumes that all new commitments will be funded out of the current cash weighting; in practice as private market commitments are drawn down they are likely to be funded partially out of cash and partially by distributions (income and capital) from existing investments and sales of public market assets. The Fund has progressively reduced its exposure to Growth Assets over the last two years, as equity valuations have become increasingly stretched, and increased the allocation to Income Assets and Protection Assets.

The IIMT recommendations reflected in this report: increase Growth Assets by 1.4% to 56.0% (1.0% underweight), with a change in the regional composition to reflect the implementation of the allocation to sustainable equities: United Kingdom Equities +0.7%; North American Equities -0.2%; European Equities -0.4%; Emerging Markets +0.4%; and Global Sustainable Equities +0.8%; increase Income Assets by 0.3% (Infrastructure +0.2% and Multi-Asset Credit +0.1%); reduce Protection Assets by 0.2% (Index-Linked Bonds -0.2%); and reduce Cash by -1.5%. The IIMT notes that the recommendations are subject to market conditions, which continue to be volatile. The IIMT continues to recommend a defensive cash allocation, reflecting both the general market uncertainty and cash held to fund existing commitment drawdowns.

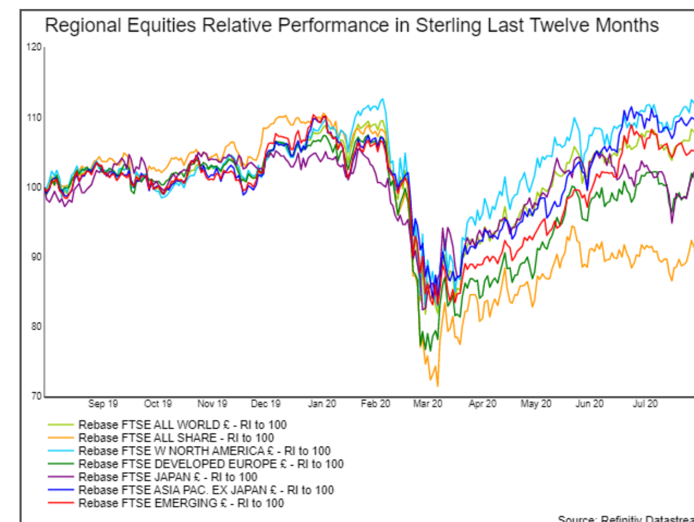
Growth Assets

At 31 July 2020, the overall Growth Asset weighting was 54.6%, up from 53.2% at 30 April 2020, reflecting relative market strength. The IIMT recommendations below increase the weighting to 56.0%; 1.0% underweight (listed equities -0.2% and private equity -0.8%).

Equity markets recovered sharply in Q2 2020 following the Q1 sell-off. The FTSE All World in Sterling terms fell by -16.0% in Q1, and increased by +19.8% in Q2 2020. Equity markets have been more subdued in Q3 2020 to date, albeit with bouts of sizeable market volatility (FTSE All World +2.5% quarter-to-date).

The IIMT believes that a small underweight position of 1.0% in Growth Assets is justified because the recovery from the Covid 19 pandemic is unlikely to be straight even and equity markets appear to be ignoring significant headwinds including: considerable uncertainty about the shape of the economic recovery; whether economic activity can return to pre-outbreak levels; rising new cases and localised lockdowns; no guarantee that a vaccine will be developed (until there is a vaccine restrictions are likely to be periodically ramped up and down); a re-escalation of US-China tensions; and the uncertainty caused by an upcoming US Presidential Election.

The Chart opposite shows the relative regional equity returns in Sterling terms over the last twelve months, and the charts overleaf show the returns since the last Investment Report was presented to Committee and in Q2 2020. Equity markets trended upwards throughout 2019 but fell sharply in February and early March 2020 as the coronavirus outbreak escalated and lockdown measures were introduced across the globe. Markets recovered strongly in April and May 2020, driven by



Benchmark Return	Q3 2020 (*)	Q2 2020	1 Year	3 Year	5 Year
FTSE All World	2.5%	19.7%	5.7%	8.4%	12.3%
FTSE UK	0.3%	10.2%	(13.0%)	(1.6%)	2.9%
FTSE North America	3.0%	21.9%	10.9%	12.5%	15.8%
FTSE Europe	2.1%	18.8%	0.6%	3.6%	8.7%
FTSE Japan	(0.4%)	12.2%	6.8%	4.9%	9.0%
FTSE Asia Pacific Ex-Japan	3.8%	19.8%	2.8%	5.0%	9.8%
FTSE Emerging Markets	3.5%	18.9%	(0.4%)	4.6%	8.0%

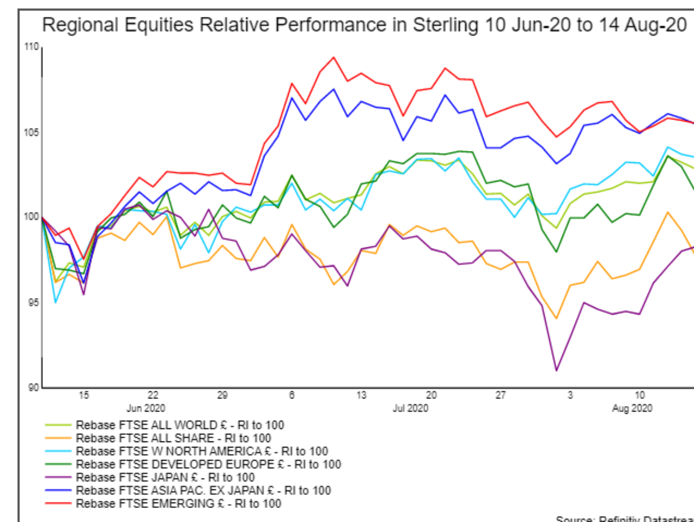
Source: Performance Evaluation Limited
(*) 1 July 2020 to 14 August 2020

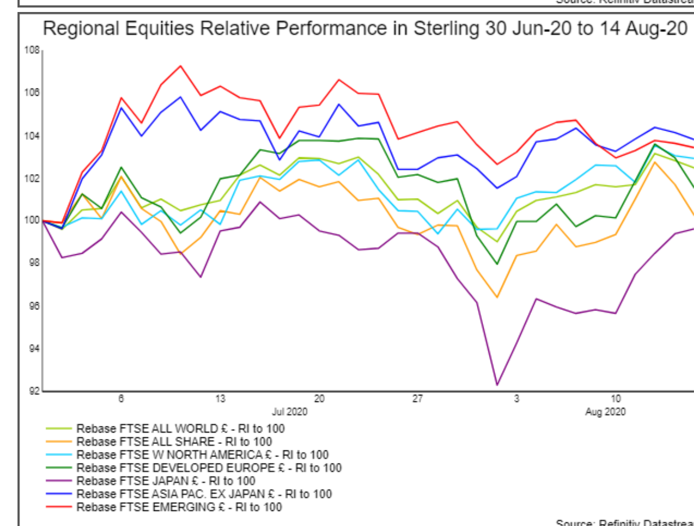
unprecedented levels of fiscal stimulus and a gradual easing of lockdown restrictions as the number of new cases fell in developed markets.

In the year to 14 August 2020, the US market provided the strongest returns (+6.2%) in local currency terms, followed by Asia Pacific Ex-Japan (+3.6%). The UK market produced the lowest return (-17.3%).

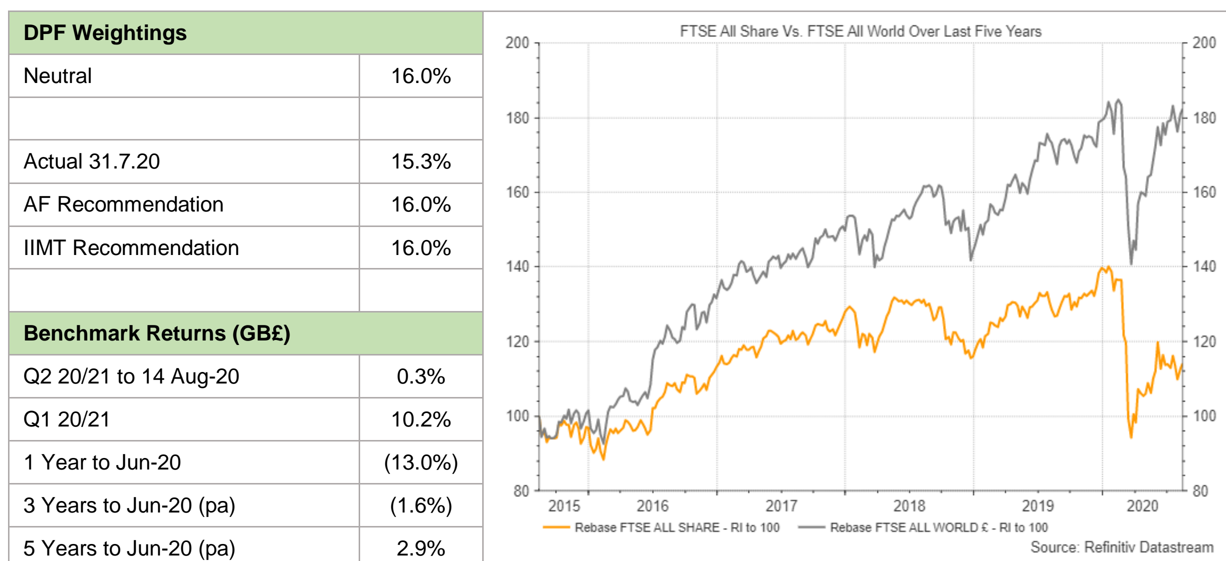
Sterling investors benefited from a weaker pound over the period, which pushed up regional equity returns. This increased the US return from +6.2% in local currency to +7.3% in Sterling terms.

UK Equities lagged all other regional markets in the year to 14 August 2020 due to a longer and more problematic Covid 19 lockdown than many peers, the impact of Brexit uncertainty, and the fact that the UK index has a high concentration of energy and commodity stocks (i.e. some of the sectors most affected by the pandemic), and a low concentration of technology stocks (e.g. some of the companies best positioned to benefit from the Covid 19 pandemic).





United Kingdom Equities



DPF Weightings	
Neutral	16.0%
Actual 31.7.20	15.3%
AF Recommendation	16.0%
IIMT Recommendation	16.0%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	0.3%
Q1 20/21	10.2%
1 Year to Jun-20	(13.0%)
3 Years to Jun-20 (pa)	(1.6%)
5 Years to Jun-20 (pa)	2.9%

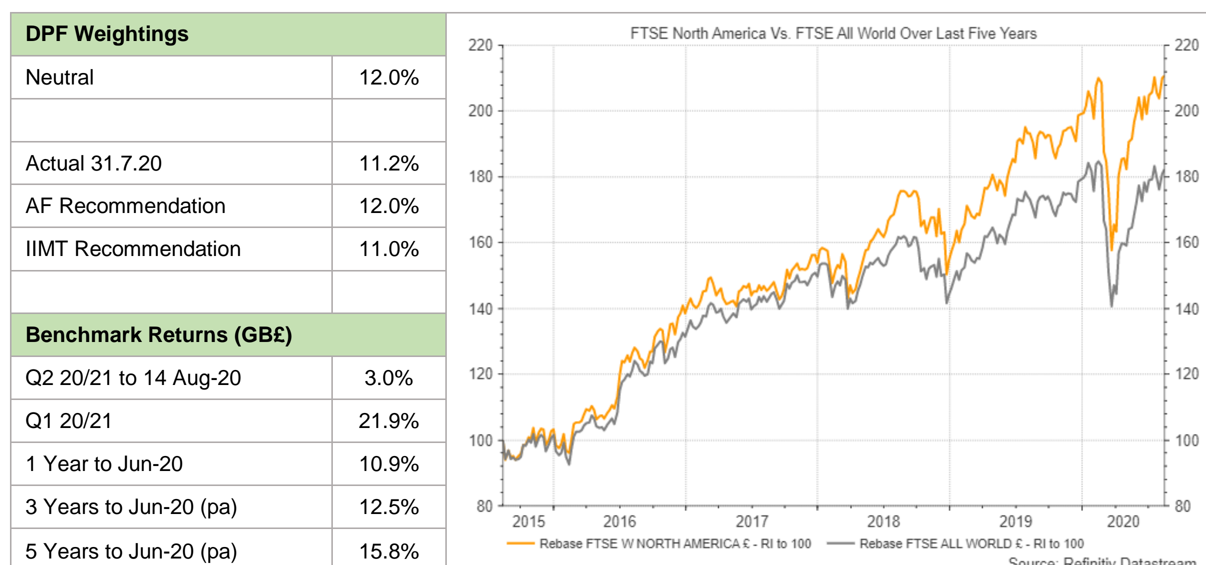
Relative market weakness reduced the UK Equity allocation from 15.8% at 30 April 2020 to 15.3% at 31 July 2020; 0.7% underweight.

Mr Fletcher recommends a neutral weighting across all of the Fund's regional equity allocations. Mr Fletcher notes that the recovery in equity markets has so far been driven by the unprecedented monetary and fiscal stimulus measures and better than expected high frequency data (time series economic data including consumption, retail sales, employment, inflation, etc.). The risk for markets from here is that the number of new cases is increasing as the level of actively in the economy increases. This is leading to new restrictions on activity and a slowing of the pace of coming out of lockdown, which further weakens and extends the earnings recovery. Mr Fletcher continues to believe that over the next 12 to 18 months the Fund could be presented with the opportunity to adjust the regional allocations and maybe even move overweight in Growth Assets. However, at the present time, with the current level of uncertainty, maintaining a neutral or even slightly underweight position relative to the strategic benchmark may be the most prudent action.

UK GDP fell by -20.4% qoq (which hides a bigger peak to trough fall of -25.6% between February and April 2020), with the majority of the fall to date being borne by the UK government and businesses. Whilst daily new cases appear to have stabilised (albeit with localised outbreaks) and lockdown measures are being gradually relaxed, the end of the government's job furlough scheme is likely to see unemployment rise and place pressure on household income. Consensus Forecasts for August 2020, forecast that the UK economy will shrink by 9.9% in 2020, before recovering by 6.4% in 2021.

The IIMT believes that whilst UK Equity returns are likely to be volatile in the short-term as the uncertainty caused by the Covid19 pandemic and on-going Brexit negotiations weigh on investor confidence, UK equity valuations are attractive on a relative basis, albeit short to medium term earnings forecast are significantly reduced. The IIMT notes that UK Equities also pay a higher dividend than most other regional equity markets, albeit these are likely to be lower in the short to medium terms as companies preserve cash (176 companies have cancelled pay-outs altogether and 30 have reduced the amount payable) and around 70% of the earnings of the UK market are generated overseas increasing diversification. As a result, the IIMT recommends increasing the allocation by 0.7% to a neutral allocation of 16.0%.

North American Equities



DPF Weightings	
Neutral	12.0%
Actual 31.7.20	11.2%
AF Recommendation	12.0%
IIMT Recommendation	11.0%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	3.0%
Q1 20/21	21.9%
1 Year to Jun-20	10.9%
3 Years to Jun-20 (pa)	12.5%
5 Years to Jun-20 (pa)	15.8%

There were no transactions in the period and relative market strength increased the weighting from 10.6% at 30 April 2020 to 11.2% at 31 July 2020; 0.8% underweight.

Mr Fletcher recommends a neutral weighting across all of the Fund's regional equity allocations; 12% in respect of North American Equities.

The IIMT notes that the US equity market has recovered sharply since the March 2020 sell off, and is now close to an all-time high. US Equities in local currency terms have returned 3.9% YTD, and 12.4% over the twelve months to 31 July 2020. The Q2 2020 earnings season was considered to be positive, with over 80% of companies reporting actual earnings in excess of expectations.

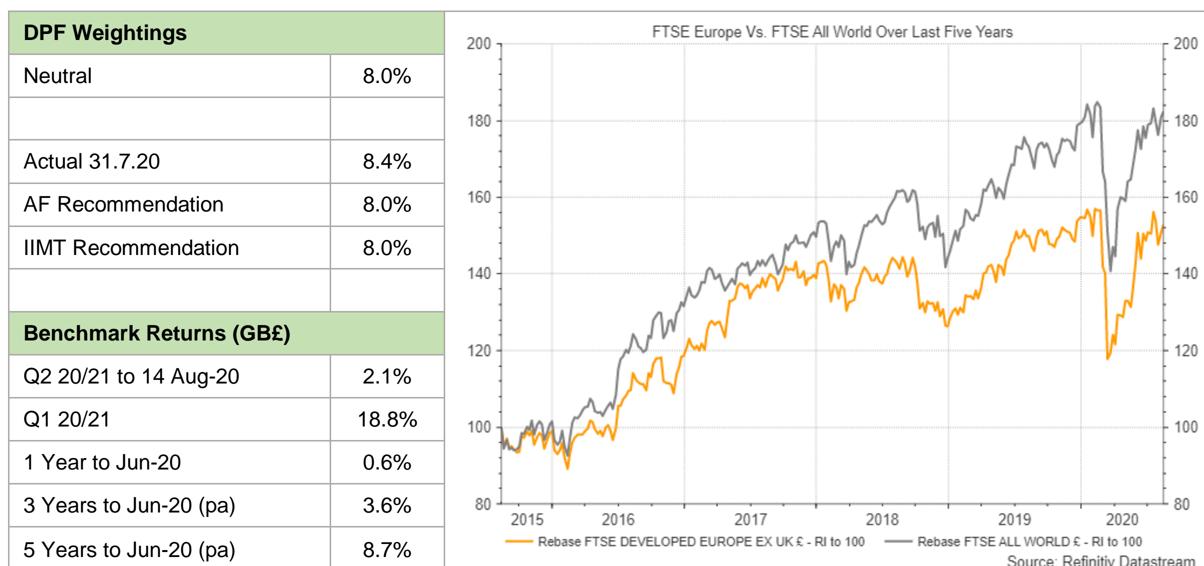
The YTD recovery has largely been concentrated in a handful of large-cap technology and online retail stocks (Facebook +23.6%; Apple +44.7%; Alphabet (Google) +11.0%; Amazon +71.3%; Netflix +51.1%; and Microsoft +30.0%), significantly increasing the concentration risk of the US equity market. These businesses have business models which have been well suited to the coronavirus outbreak, and there is significant performance dispersion versus the rest of the US market.

The IIMT believes that the shape of the economic recovery from the Covid 19 pandemic is uncertain. Daily new cases in the US have been rising since mid-June 2020 (albeit the number of new daily deaths is lower now than at its peak), and some localised lockdown restrictions have been reintroduced. Whilst there are early signs that the rate of new cases are starting to stabilise, the impact on US consumer and business confidence is unclear.

It is worth noting that consumer incomes have so far been protected by support measures from the US government which provided $1,200 stimulus cheques as well as a $600 per week boost to unemployment benefits. These payments ceased at the end of July 2020, and although President Trump has since signed an executive order to provide unemployed workers with a $400 a week extra payment, the long term sustainability of these payments is unclear. Furthermore, trade tensions between the US and China continue to escalate, and political uncertainty is also likely to rise in the run-up to the US Presidential Election in November 2020.

Given the strong relative performance of the US Equity market over the last twelve months, the IIMT continues to believe that an underweight position remains justified, and recommend a 1.0% underweight allocation of 11.0%.

European Equities



DPF Weightings	
Neutral	8.0%
Actual 31.7.20	8.4%
AF Recommendation	8.0%
IIMT Recommendation	8.0%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	2.1%
Q1 20/21	18.8%
1 Year to Jun-20	0.6%
3 Years to Jun-20 (pa)	3.6%
5 Years to Jun-20 (pa)	8.7%

Whilst there were no transactions in the period, relative market strength increased the Fund's allocation to European Equities to 8.4% at 31 July 2020; 0.4% overweight.

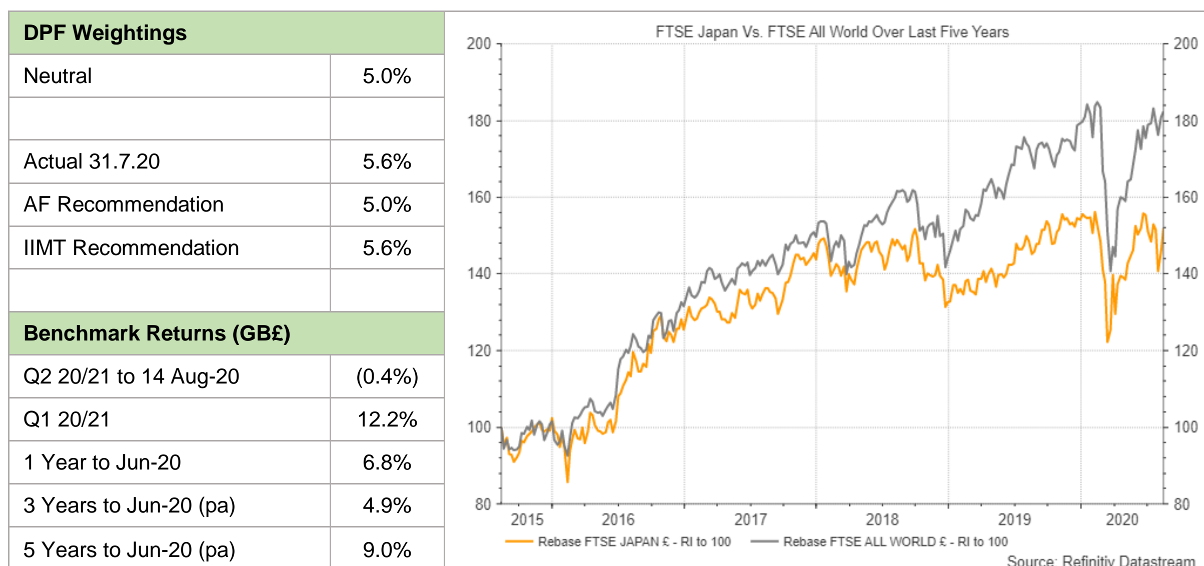
Mr Fletcher recommends a neutral weighting across all of the Fund's regional equity allocations; 8% in respect of European Equities.

A large part of Europe appeared to have managed the Covid 19 outbreak better than any other region in Q2 2020, although there are growing concerns about a second wave of infections as lockdown restrictions have been eased. Economic activity has been recovering across the region, particularly in Germany, where new infections have been low for several months. However, recent outbreaks across numerous European countries, have come at the peak of the summer tourist season, casting some doubt on the potential for a swift economic recovery.

Eurozone GDP fell by -12.1% in Q2 2020 (the largest quarterly fall in the Eurozone's history), and there were some sizeable regional variances: Spain was the hardest hit, suffering an -18.5% contraction compared to -10.1% in Germany. In response to the crisis, the European Union agreed a €750bn Recovery Fund (aid packages), and the European Central Bank's Pandemic Emergency Purchase Programme (an asset purchase programme) was increased to €1,350b; these stimulus programmes increased the demand for European assets. European Equities returned 7.7% in local currency terms in the three months to 31 July 2020; -4.0% YTD.

The IIMT notes that the economic backdrop in the Eurozone was weak even before the Covid 19 pandemic despite continued monetary support. Whilst the finalisation of the Recovery Fund is positive, and points to further fiscal integration across the European Union, several countries have been badly impacted by the Covid 19 pandemic, and the ongoing outbreak of new localised infections, means that the shape of the economic recovery across Europe is unclear. As a result, the IIMT recommends that the current allocation of 8.4% is trimmed back to a neutral weight of 8.0%.

Japanese Equities



DPF Weightings	
Neutral	5.0%
Actual 31.7.20	5.6%
AF Recommendation	5.0%
IIMT Recommendation	5.6%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	(0.4%)
Q1 20/21	12.2%
1 Year to Jun-20	6.8%
3 Years to Jun-20 (pa)	4.9%
5 Years to Jun-20 (pa)	9.0%

Net divestment of £32m (switched into Global Sustainable Equities), together with relative market weakness, reduced the Fund's weighting in Japanese Equities to 5.6% at 31 July 2020; 0.6% overweight against the benchmark.

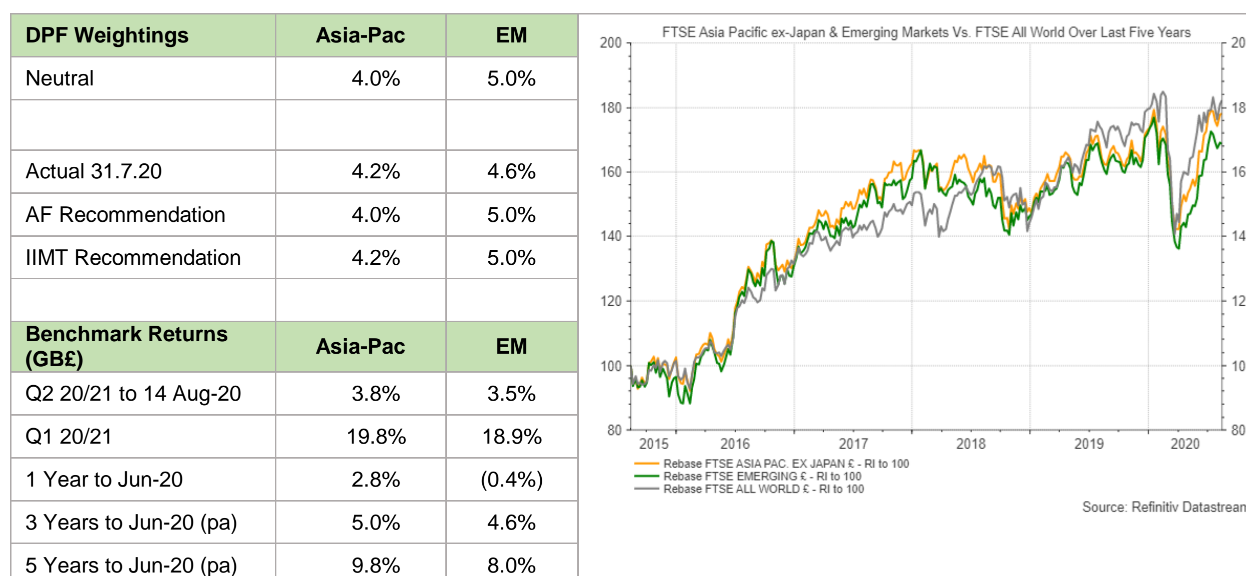
Mr Fletcher recommends a neutral weighting across all of the Fund's regional equity allocations; 5% in respect of Japanese Equities.

Similar to the Eurozone, the Japanese economy was suffering from weakness prior to the Covid 19 pandemic, and fell into recession in Q1 2020 with a 2.2% contraction. The economy fell by a further 27.8% (annualised) in Q2 2020, wiping-out the benefits brought by Prime Minister Abe's 'Abenomics' stimulus policies employed since late 2012. Consensus forecasts for August 2020, expect the Japanese economy to contract by -5.3% in 2020, before growing by +2.5% in 2021. Similar to other developed markets, the Japanese government has provided significant levels of financial stimulus in response to the pandemic.

Notwithstanding the 2019-20 economic slowdown, the IIMT believes that the long term story in Japan remains intact supported by attractive relative valuations, improving corporate governance, and the diversifying and defensive qualities of the Japanese market (e.g. the safe-haven status of the ¥). Furthermore, Japan has a low reliance on tourism, safe banks, healthy corporate balance sheets and high levels of fiscal stimulus which should help the Japanese economy to recover more quickly from the pandemic by international standards.

The IIMT believes that an overweight position remains appropriate and recommend that the current allocation 5.6% is maintained.

Asia Pacific Ex-Japan and Emerging Market Equities



DPF Weightings	Asia-Pac	EM
Neutral	4.0%	5.0%
Actual 31.7.20	4.2%	4.6%
AF Recommendation	4.0%	5.0%
IIMT Recommendation	4.2%	5.0%
Benchmark Returns (GB£)	**Asia-Pac**	**EM**
Q2 20/21 to 14 Aug-20	3.8%	3.5%
Q1 20/21	19.8%	18.9%
1 Year to Jun-20	2.8%	(0.4%)
3 Years to Jun-20 (pa)	5.0%	4.6%
5 Years to Jun-20 (pa)	9.8%	8.0%

Divestment of £34m into market strength reduced the Fund's allocation to Asia Pacific Ex-Japan Equities to 4.2% at 31 July 2020. There were minimal net transactions in respect of Emerging Market Equities but relative market strength increased the Fund's allocation to 4.6% at 31 July 2020.

Mr Fletcher recommends a neutral weighting across all of the Fund's regional equity allocations; 4% in the case of Asia Pacific Ex-Japan and 5% in Emerging Market Equities.

The IIMT continues to believe in the long-term growth potential of these regions, noting that these regions have accounted for well over half of global growth over the last ten years, and as shown below, Asia Pacific is forecast to grow at a faster rate than developed markets in 2020 and 2021.

Region	Real GDP 2019 (A)	Real GDP 2020 (F)	Real GDP 2021 (F)
Asia Ex-Japan	4.0%	(1.2%)	5.8%
Latin America	0.6%	(8.0%)	4.0%
Eastern Europe	2.4%	(5.0%)	4.2%
North America	2.2%	(5.3%)	4.1%
Japan	0.7%	(5.3%)	2.5%
Eurozone	1.3%	(7.9%)	5.7%
United Kingdom	1.5%	(9.9%)	6.4%

Source: August 2020 Consensus Forecasts

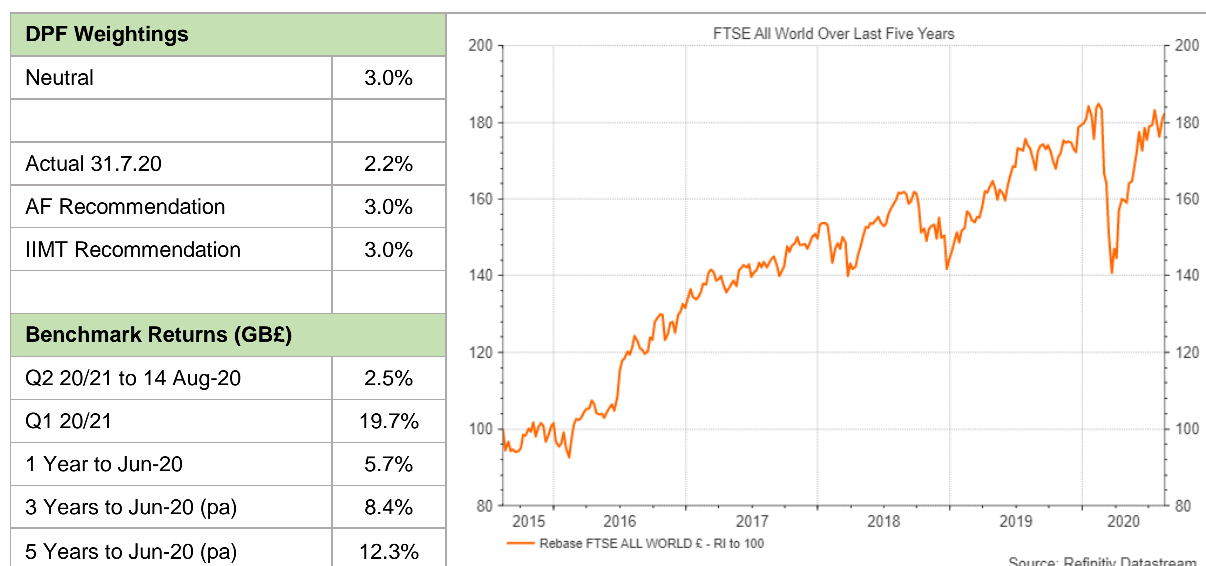
Notwithstanding the strong growth dynamics, particularly in respect of Emerging Asia, this has failed to convert into strong relative returns for emerging market investors. Over the last five years to July 2020, Asia Pacific and Emerging Market equity returns have been relatively weak; cumulative total dollar returns from US equities totalled 102.8%, compared to 67.3% from Asia Pacific equities and 60.7% from emerging market equities.

The poor relative performance of Asia Pacific Ex-Japan and Emerging Market Equities has been attributed to three key drivers: a stronger dollar acting as a headwind for further migration of western savings pools towards these regions; tepid global growth, including an on-going slowdown in China; and the increase in more domestically focused political agendas (e.g. at the expense of further globalization).

The economic impact of the Covid 19 pandemic remains unclear, albeit the consensus forecasts for the Asia Pacific region appear positive and the response from most of the countries in the region to the coronavirus outbreak was seen as timely and decisive, and the lockdown measures introduced have now been largely relaxed. Furthermore, there are growing signs that the tensions between the US and China are escalating again, and there is a risk that following the pandemic, political agendas and supply chains will become much more domestically focused (e.g. at the expense of further globalisation).

The IIMT recommends holding the Asia Pacific Ex-Japan Equity weighting at 4.2% (0.2% overweight), whilst adding 0.4% to Emerging Market's to also bring it into line with a neutral weighting of 5%.

Global Sustainable Equities



DPF Weightings	
Neutral	3.0%
Actual 31.7.20	2.2%
AF Recommendation	3.0%
IIMT Recommendation	3.0%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	2.5%
Q1 20/21	19.7%
1 Year to Jun-20	5.7%
3 Years to Jun-20 (pa)	8.4%
5 Years to Jun-20 (pa)	12.3%

Net investment in the three months to 31 July 2020 totalled £68m, taking the asset class weighting to 2.2% at end of July 2020.

Mr Fletcher recommends a neutral weighting across all of the Fund's regional equity allocations; 3% in respect of Global Sustainable Equities.

The IIMT expects to allocate further capital to the asset class over the next quarter subject to market conditions, and to move towards a neutral weighting of 3%.

Private Equity

DPF Weighting					
Netural		Actual 31.7.20	Committed 31.7.20	AF Recommendation	IIMT Recommendation
4.0%		3.1%	4.9%	4.0%	3.2%
Benchmark Returns (GB£)					
Q2 20/21 to 14 Aug-20	Q1 20/21	1 Year to Jun-20	3 Years to Jun-20 (pa)	5 Years to Jun-20 (pa)	
0.4%	10.3%	(12.0%)	(0.6%)	3.8%	

The Private Equity weighting fell from 3.2% at 30 April 2020 to 3.1% at 31 July 2020 reflecting the flow through of March 2020 valuation reports incorporating the valuation impact of the Covid 19 pandemic.

Mr Fletcher recommends a neutral weighting of 4% in Private Equity.

The IIMT believes that the coronavirus outbreak is likely to lead to a period of lower private equity multiples, particularly in respect of small and mid-cap deals, and note that the Fund's outstanding private equity commitments should be well positioned to benefit from these opportunities. The IIMT recommends that the Private Equity weighting is increased by 0.1% to 3.2% (0.8%% underweight) in the forthcoming quarter, in anticipation of existing commitment drawdowns.

(vii) Income Assets

At 31 July 2020, the overall weighting in Income Assets was 20.7%, down from 21.3% at 30 April 2020, principally reflecting relative market weakness compared to growth assets. The IIMT recommendations below would take the overall Income Asset weighting to 21.0%, and the committed weighting to 24.7%.

Multi Asset Credit

DPF Weighting				
Neutral		Actual 31.7.20	AF Recommendation	IIMT Recommendation
6.0%		6.1%	8.0%	6.2%
Benchmark Returns (GB£)				
Q2 20/21 to 14 Aug-20	Q1 20/21	1 Year to Jun-20	3 Years to Jun-20 (pa)	5 Years to Jun-20 (pa)
3.5%	6.5%	(0.3%)	2.3%	n/a

There were minimal net transactions in the three months to 31 July 2020, with commitment drawdowns being matched by distributions, and the asset class weighting stayed at 6.1%. Adjusting for commitments, the weighting increases to 7.7%. Whilst this implies the pension fund will be 1.7% overweight should all the commitments be drawn-down, in practice it is unlikely that the commitments will be fully drawn, and some of the existing closed-ended investments have now entered their distribution phase (i.e. returning cash to investors).

Mr Fletcher continues to recommend a 2% overweight allocation to Multi-Asset Credit believing that the main opportunity comes from global high yield bonds, emerging debt, loans and the dynamic allocation between these sectors of the bond market. Mr Fletcher notes that whilst spreads have narrowed significantly since March 2020, central banks remain determined to support the markets through bond purchases and an extended period of low policy rates and government bond yields. As always with this type of asset avoiding the risk of default is the key to success, but even at the current level of spread, Mr Fletcher believes that sub-investment grade assets appear attractive despite the increased risk of default.

Whilst the IIMT continues to be positive about the long-term attractions of the asset class, with a strong bias towards defensive forms of credit, it is noted that spreads have narrowed significantly since mid-March 2020 (e.g. US 7-10 year high yield bond spreads initially increased from around 375 basis points

prior to the outbreak to around 1,100 basis points by mid-March but have subsequently fallen to around 500 basis points). The IIMT believes that it is unclear whether the current level of spread is sufficient to compensate for the increased risk of default, particularly when the shape of the economic recovery is unclear, and the recovery cannot easily be benchmarked to previous trends. It is also likely to differ significantly by country and sector.

The IIMT recommends increasing the invested weighting by 0.1% to 6.2% in the upcoming quarter (0.2% overweight) to cover anticipated commitment drawdowns.

Property

DPF Weighting				
Neutral		Actual 31.7.20	AF Recommendation	IIMT Recommendation
9.0%		7.8%	9.0%	7.8%
Benchmark Returns (GB£)				
Q2 20/21 to 14 Aug-20	Q1 20/21	1 Year to Jun-20	3 Years to Jun-20 (pa)	5 Years to Jun-20 (pa)
Not Available	(2.2%)	(2.7%)	3.0%	4.6%

The Fund's allocation to Property fell by 0.5% to 7.8% at 31 July 2020. Direct Property accounted for 4.5% (0.5% underweight) and Indirect Property accounted for 3.3% (0.7% underweight). The committed weight was 8.0% at 31 July 2020.

Mr Fletcher recommends that the property allocation remains neutral overall. The uncertainty over the future use of buildings created by Covid-19 has increased the potential volatility of returns from the asset class. Certain types of buildings my need to be re-purposed, at a minimum property could see a medium term downward re-rating and the income generated from rents could have an impact beyond the short-term. Mr Fletcher notes that as a long-term investor, the Fund can afford to 'look-through' the volatility and low yield environment, and property probably remains an attractive asset class.

Colliers Capital, the Fund's Property Manager, note that the coronavirus pandemic has had a dramatic and unprecedented effect on the economic health of the UK and in turn the UK commercial property market. The retail and leisure sectors have been particularly badly affected with many businesses being closed down during the lockdown. Rent collection has been a significant issue for landlords during this time. The Fund's portfolio continues to perform well relative to the benchmark, with a total return of -

2.0% in Q2 2020, versus a benchmark return of -2.2% (last twelve months +0.4% versus -2.7%). The current portfolio void rate is 6.0%, versus a benchmark void rate of 7.6%. The focus now is largely on additional investment into the industrial sector. In light of the effect of the coronavirus on the retail and leisure sector, further investment in those areas is unlikely at present.

The IIMT recommends that in the short term the Fund's current allocation to Direct Property (4.5%; 0.5% underweight) and Indirect Property (3.3%; 0.7% underweight) are maintained but liquidity of up to £50m is made available to the Direct Property manager to make further investments at the right time should they identify suitable investment opportunities.

Infrastructure

DPF Weighting					
Neutral		Actual 31.7.20	Committed 31.7.20	AF Recommendation	IIMT Recommendation
8.0%		6.8%	9.0%	8.0%	7.0%
Benchmark Returns (GB£)					
Q2 20/21 to 14 Aug-20	Q1 20/21	1 Year to Jun-20	3 Years to Jun-20 (pa)	5 Years to Jun-20 (pa)	
0.3%	0.6%	2.7%	2.7%	2.5%	

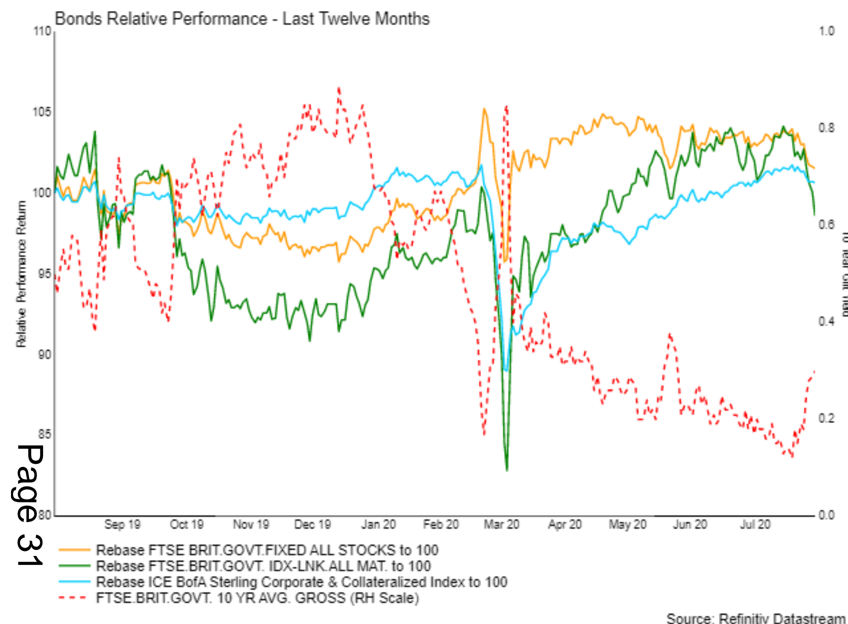
Relative market weakness reduced the Fund's allocation to Infrastructure from 6.9% at 30 April 2020 to 6.8% at 31 July 2020; 9.0% on a committed basis.

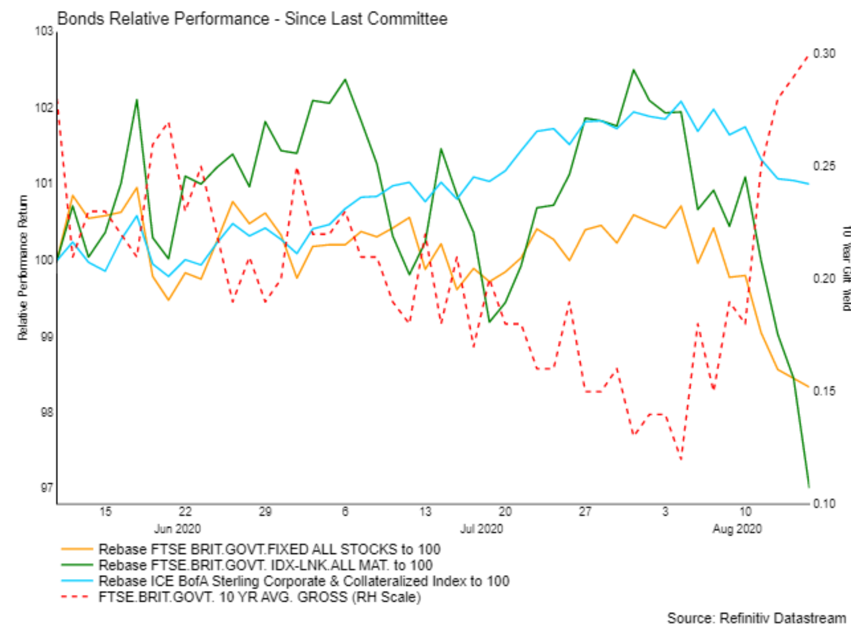
Mr Fletcher recommends a neutral weighting of 8% allocation.

The IIMT continues to view Infrastructure as an attractive asset class, and favours a bias towards core infrastructure assets. Core infrastructure assets can offer low volatility; low correlation to equity and fixed income; and reliable long-term cash flows. Notwithstanding the noted favourable characteristics of the asset class, the IIMT continues to believe that infrastructure assets are exposed to increased political and regulatory risk, and this risk is managed through asset type and geographical diversification. Further investment opportunities, which are in line with these objectives, continue to be assessed, including a focus on additional renewable energy commitments.

The IIMT recommends that the Infrastructure weighting is increased by 0.2% to 7.0% (1.0% underweight) in the next quarter, in anticipation of existing commitment draw-downs.

(ix) Protection Assets

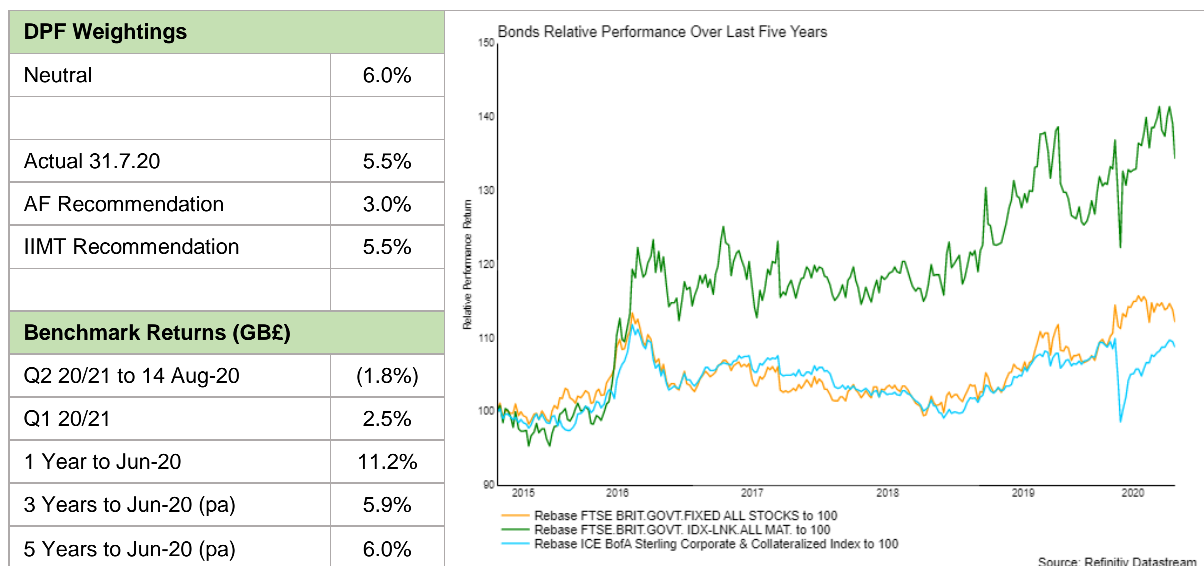




The weighting in Protection Assets at 31 July 2020 was 18.1%, down from 18.3% at 30 April 2020, reflecting relative market weakness. The IIMT recommendations below reduce the weighting to 17.9%.

Government bond yields gradually fell (i.e. prices rose) in June and July before rallying slightly in August 2020. Bond yields have not risen despite the equity market rally since mid-March 2020, and the expectations of significant bond issuance going forward. G7 yields remain near historic lows, consistent with expectations for a prolonged period of zero-or-below policy rates in response to the economic backdrop.

Conventional Bonds



DPF Weightings	
Neutral	6.0%
Actual 31.7.20	5.5%
AF Recommendation	3.0%
IIMT Recommendation	5.5%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	(1.8%)
Q1 20/21	2.5%
1 Year to Jun-20	11.2%
3 Years to Jun-20 (pa)	5.9%
5 Years to Jun-20 (pa)	6.0%

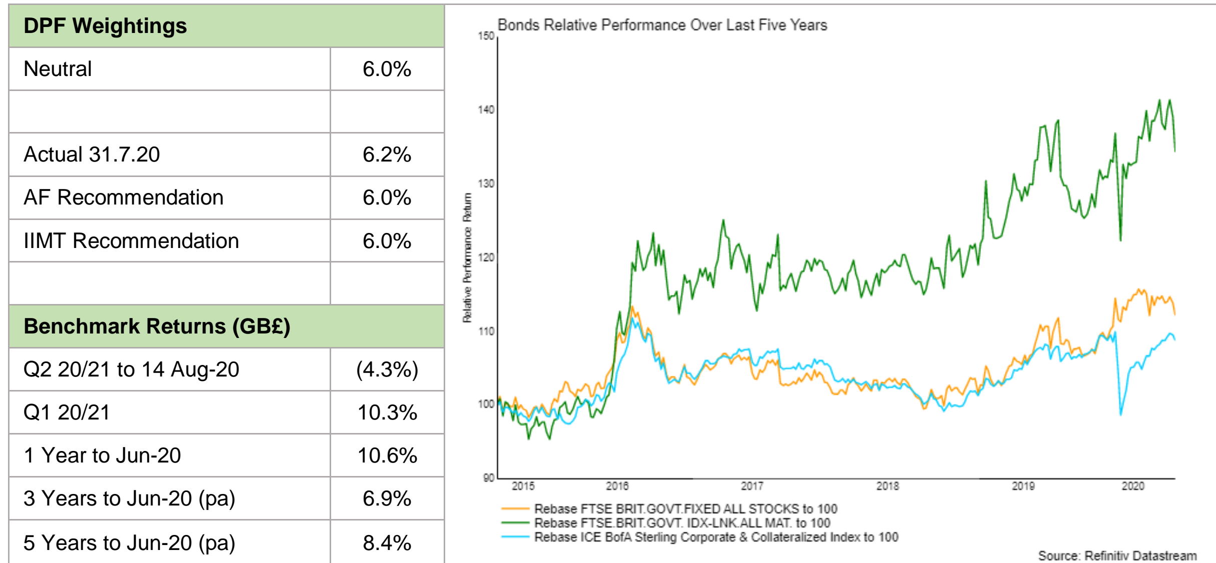
There were no transactions in the period, and relative market weakness reduced the Fund’s allocation to Conventional Bonds by 0.3% to 5.5% at 31 July 2020; 0.5% underweight.

Mr Fletcher has maintained his recommended allocation to Conventional Bonds at 3% (3% underweight) noting that government bond yields have continued to fall, making new ‘All Time Lows’ as markets have responded to the Covid19 pandemic. Mr Fletcher expects government bond yields to remain around their current levels for a long time, and does not expect central bank policy rates to change for the next 12 to 18 months. Over the long term, Mr Fletcher does expect government bond yields to rise and there is the risk that yield curves could steepen if inflation becomes more of a concern, but for now central banks will do all they can to keep government yields at or close to their current levels.

The IIMT continues to believe that whilst conventional sovereign bonds do not appear to offer good value at current levels with yields around historic lows, they are diversifying assets and continue to afford greater protection than other asset classes in periods of market uncertainty as evidenced during the Covid 19 pandemic (+7.0% year to 14 August 2020, 3.8% higher than the FTSE All World).

The IIMT recommends that the current 0.5% allocation of 5.5% is maintained.

Index-Linked Bonds



DPF Weightings	
Neutral	6.0%
Actual 31.7.20	6.2%
AF Recommendation	6.0%
IIMT Recommendation	6.0%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	(4.3%)
Q1 20/21	10.3%
1 Year to Jun-20	10.6%
3 Years to Jun-20 (pa)	6.9%
5 Years to Jun-20 (pa)	8.4%

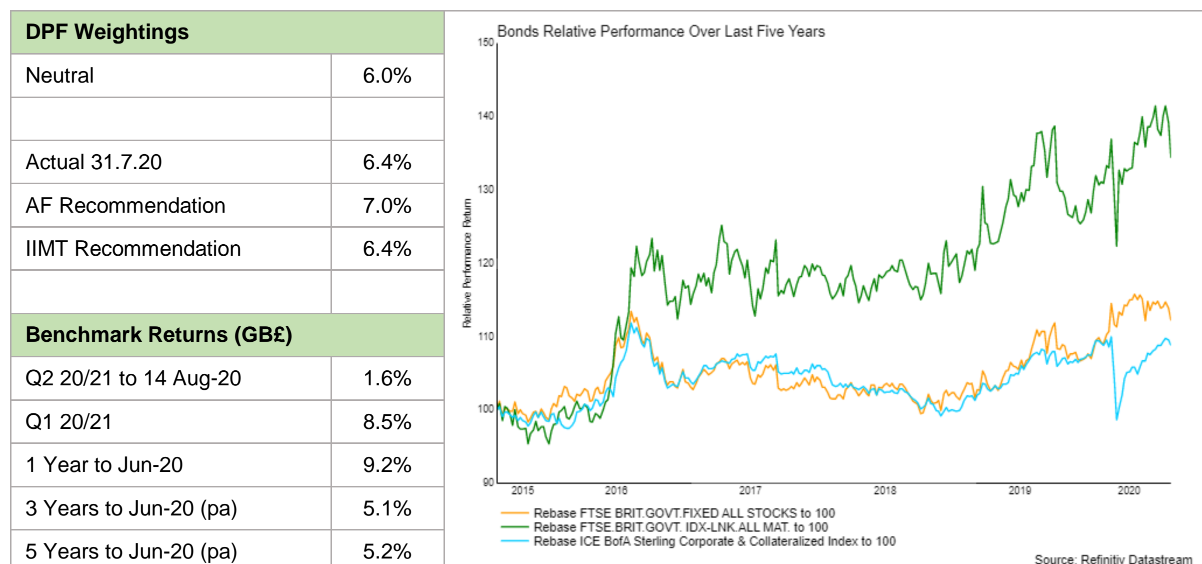
The Fund's allocation to Index-Linked Bonds remained flat at 6.2% between 30 April 2020 and 31 July 2020; 0.2% overweight.

Mr Fletcher recommends a neutral 6% allocation to Index-Linked Bonds (Linkers), with a preference to remain 2% underweight UK Index-Linked Bonds and 2% overweight US Treasury Inflation Protected (TIPS) Bonds. Mr Fletcher notes that whilst the real yield on TIPS has fallen over the last quarter, UK Index Linked yields have fallen further, meaning that there is still a yield pick-up for holding TIPS, and the US market is not subject to the potential change in the calculation of the inflation measure used to uplift coupon and principal repayments. The consultation on the proposed changes to the method of calculating the RPI measure of inflation closes in August 2020. Mr Fletcher notes that UK Index Linked market has only priced in about 50% of the potential impact of the change to the inflation measure on the market valuation of UK inflation protected bonds. Whilst asset managers continue to lobby for no change to the inflation measure or compensation, corporate Pension Fund trustees with RPI liabilities appear more relaxed about the proposed change. Mr Fletcher notes that there is an increasing consensus that the Chancellor will endorse the change in the Autumn Budget Statement without compensation to bond holders.

In line with the IIMT's recommendation in respect of Conventional Bonds, the IIMT notes that whilst Index-Linked Bonds appear expensive at current levels, it is too early to call the bottom of the Covid 19 pandemic. The IIMT believes that inflation expectations in the short-term are muted reflecting the deflationary effects of weaker demand and lower oil prices but in the medium term inflation is likely to pick-up driven by the enormous policy stimulus (both

fiscal and monetary) and tighter global supply chains. The IIMT recommends a 6% neutral allocation to Index-Linked Bonds, and that the current exposure to US TIPS (around 20% of the Index-Linked portfolio) is maintained.

Corporate Bonds



DPF Weightings	
Neutral	6.0%
Actual 31.7.20	6.4%
AF Recommendation	7.0%
IIMT Recommendation	6.4%
Benchmark Returns (GB£)	
Q2 20/21 to 14 Aug-20	1.6%
Q1 20/21	8.5%
1 Year to Jun-20	9.2%
3 Years to Jun-20 (pa)	5.1%
5 Years to Jun-20 (pa)	5.2%

Relative market strength increased the Fund's allocation to the asset class from 6.3% at 30 April 2020 to 6.4% at 31 July 2020; 0.4% overweight.

Mr Fletcher has maintained is 1% overweight allocation to Corporate Bonds noting that the recent rise in credit spreads is more than sufficient to compensate for the additional default risk.

The IIMT notes that credit spreads have narrowed significantly since mid-March 2020 (e.g. US 7-10 year investment grade bond spreads initially increased from around 100 basis points prior to the outbreak to around 400 basis points by mid-March but have subsequently fallen to around 130 basis points), and it is unclear whether the current level of spread is sufficient to compensate for the increased default, particularly when the shape of the recovery is unknown, and the recovery cannot easily be benchmarked to previous trends. It is also likely to differ significantly by country and sector, and there is an increased risk of 'zombie' companies (companies weighed down by debt who are keep going by low interest rates/banks' unwillingness to recognise the write down that would be associated with an insolvency). Whilst the impact of the current situation on corporate profitability, balance sheets and cash flows remains unclear, the IIMT believes that the more modest overweight allocation of 6.4% is warranted.

(x) Cash

The Cash weighting at 31 July 2020 was 6.6% (4.6% overweight relative to the benchmark).

Mr Fletcher has maintained his 2% neutral allocation to Cash but notes that a sizeable proportion of this is already promised to future investments (i.e. existing contractual commitments). Mr Fletcher notes that given the current level of uncertainty a higher cash balance remains a good strategy for the Fund.

Global markets have recovered following the sharp sell-off in Q1 2020, but this has been heavily dependent on substantial and unprecedented central bank monetary support. The recovery from the Covid 19 pandemic is likely to be uneven, and markets appear to be ignoring significant headwinds including considerable uncertainty about the shape of the economic recovery; whether economic activity can return to pre-outbreak levels; rising new cases and localised lockdowns; no guarantee that a vaccine will be developed (until there is a vaccine restrictions are likely to be ramped up and down occasionally); a re-escalation of US-China tensions; and the uncertainty caused by an upcoming US Presidential Election.

The IIMT recommends a defensive cash allocation of 5.1% due to the highly uncertain economic outlook This will also ensure that the Fund has sufficient operational headroom after adjusting for term-loan maturities (i.e. short-term loans provided by the Fund to other public sector bodies) to cover upcoming investment commitment drawdowns (expected to be in excess of £120m over the course of 2020-21), and to cover the likelihood that cash inflows into the Fund, particularly, from investment income, reduce as a result of the Covid 19 pandemic.

3 Other Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal and human rights, human resources, equality and diversity, health, environmental, transport, property and prevention of crime and disorder.

4 Background Papers

Files held by the Investment Section.

5 Officer's Recommendations

5.1 That the report of the external adviser, Mr Fletcher, be noted.

5.2 That the asset allocations, total assets and long term performance analysis in this report be noted.

5.3 That the strategy outlined in the report be approved.

Peter Handford

Director of Finance & ICT

MJ HUDSON
Allenbridge

Second Quarter 2020 Investment Report

PREPARED FOR:

Derbyshire County Council Pension Fund: Pensions and Investment Committee Meeting

SEPTEMBER 2020

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Investment Report for Derbyshire County Council Pension Fund

This report has been prepared by Anthony Fletcher "External Investment Advisor" of Derbyshire County Council Pension Fund (the Fund). At the request of the Pension and Investment Committee the purpose of the report is to fulfil the following aims: -

- Provide an overview of market returns by asset class over the last quarter and 12 months.
- An analysis of the Fund's performance by asset class versus the Fund specific benchmark for the last quarter and the last 12 months.
- An overview of the economic and market outlook by major region, including consideration of the potential impact on the Fund's asset classes
- An overview of the outlook for each of the Funds asset classes for the next two years; and recommend asset class weightings for the next quarter together with supporting rationale.

The report is expected to lead to discussions with the in-house team on findings and recommendations as required. The advisor is expected to attend quarterly meetings of the Pensions and Investment Committee to present his views and actively advise committee members.

Meeting date 2nd September 2020
Date of paper 21st August 2020

1. Market Background (Second quarter 2020)

Overall, the Covid 19 outbreak and the enormous central bank and government support packages put in place to counter the effects of lock downs, continued to be the dominant global theme driving markets, and they are likely to continue to do so until a vaccine is developed, or the number of new cases significantly decreases.

Europe and Asia started to re-open as their outbreaks have been brought under control, while the United States saw a resurgence in cases, with some States starting to reverse their re-openings. In the second quarter the regional infection hotspots were the United States, Russia, and Brazil. In the US and Brazil, the outbreak was made worse by the political response to what should have been treated as a universal public health emergency. In both counties the response has undermined the presidential leadership. This is bad news for President Trump who is looking to be re-elected later this year, he is now trailing in the polls to the Democrat candidate Joe Biden.

Risk assets, mainly equities and high yield bonds had a strong quarter with prices rising sharply as can be seen in table 1 and 2 below. Within the regional indices, there was a marked dispersion in sector performance. Those indices with a high weight to technology stocks produced the strongest returns whereas Indices like the FTSE 100 with a high weight to energy, commodity and financial stocks performed less well.

All bond markets produced solid returns with the highest duration and unusually the most economically sensitive sectors producing the highest returns, as central bank started buying not just government but also corporate bonds.

Most economies are probably in recession at the end of the second quarter of 2020, the depth and length of the recession is highly uncertain, due to the progression of the virus, the time taken to come out of lockdown, the risk of a second wave of lockdowns as infections increase and because of the potential for people, companies and governments to change their longer term behaviour.

Table 1, below shows the total investment return in pound Sterling for the major asset classes, using FTSE indices except where noted; for the month of July 2020 and the 3 and 12 months to the end of June 2020.

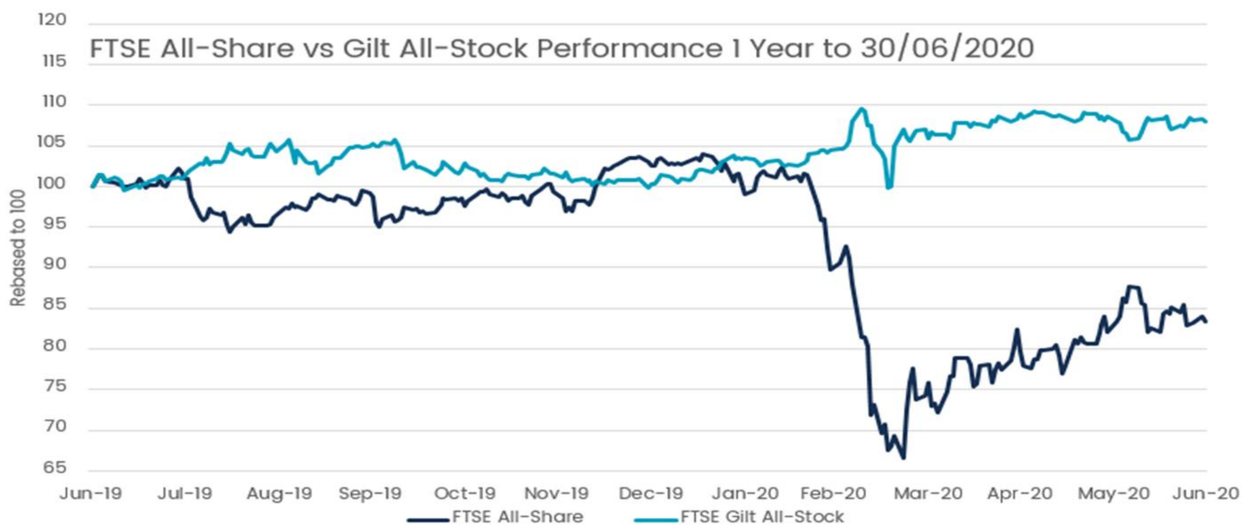
% TOTAL RETURN DIVIDENDS REINVESTED

MARKET RETURNS

		Period end 30th June 2020	
	July 2020	**3 months**	**12 months**
Global equity ACWI^	-1.3	19.7	6.5
Regional indices			
UK All Share	-3.6	10.2	-13.0
North America	-0.4	21.9	10.9
Europe ex UK	-1.5	18.8	0.6
Japan	-7.7	12.2	6.8
Pacific Basin	1.5	19.8	2.8
Emerging Equity Markets	2.7	18.9	-0.4
UK Gilts - Conventional All Stocks	0.4	2.5	11.2
UK Gilts - Index Linked All Stocks	0.7	10.3	10.6
UK Corporate bonds*	1.9	9.0	6.5
Overseas Bonds**	0.9	0.9	5.3
UK Property quarterly^	-	-2.2	-2.7
Sterling 7 day LIBOR	0.01	0.02	0.5

^ MSCI indices * iBoxx £ Corporate Bond; **Citigroup WGBI ex UK hedged

Chart 1: - UK bond and equity market returns - 12 months to 30th June 2020



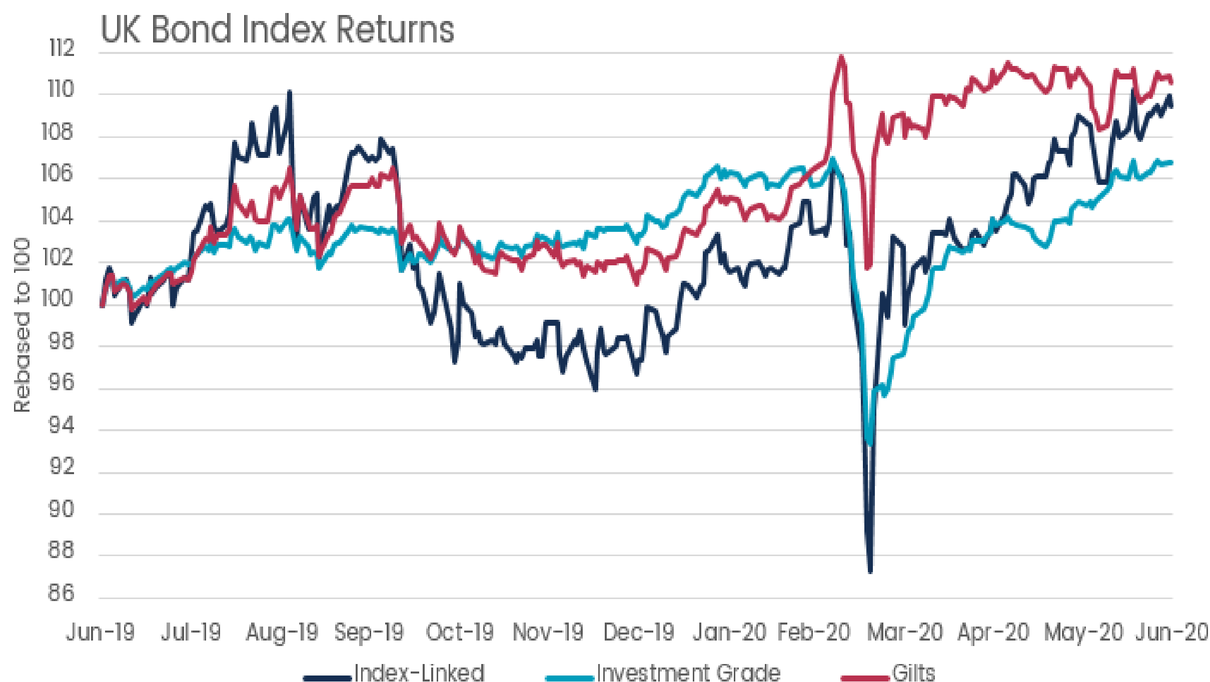
Source: - Bloomberg

Table 2: - Change in Bond Market yields over the quarter and 12 months.

BOND MARKET % YIELD TO MATURITY	31st March 2020	30th June 2020	Quarterly Change %	31st June 2019	Current 7th August 2020
UK GOVERNMENT BONDS (GILTS)					
10 year	0.35	0.17	**-0.18**	0.83	0.11
30 year	0.82	0.64	**-0.18**	1.47	0.65
Over 15y Index linked	-1.91	-2.36	**-0.45**	-1.88	-2.33
OVERSEAS 10 YEAR GOVERNMENT BONDS					
US Treasury	0.67	0.66	**-0.01**	2.01	0.57
Germany	-0.46	-0.46	**0.00**	-0.33	-0.53
Japan	-0.01	0.02	**0.03**	-0.16	0.01
NON-GOVERNMENT BOND INDICES					
UK corporates	2.96	1.95	**-1.01**	2.39	1.74
Global High yield	9.39	6.61	**-2.78**	5.59	5.47
Emerging markets	6.16	4.38	**-1.78**	4.36	3.91

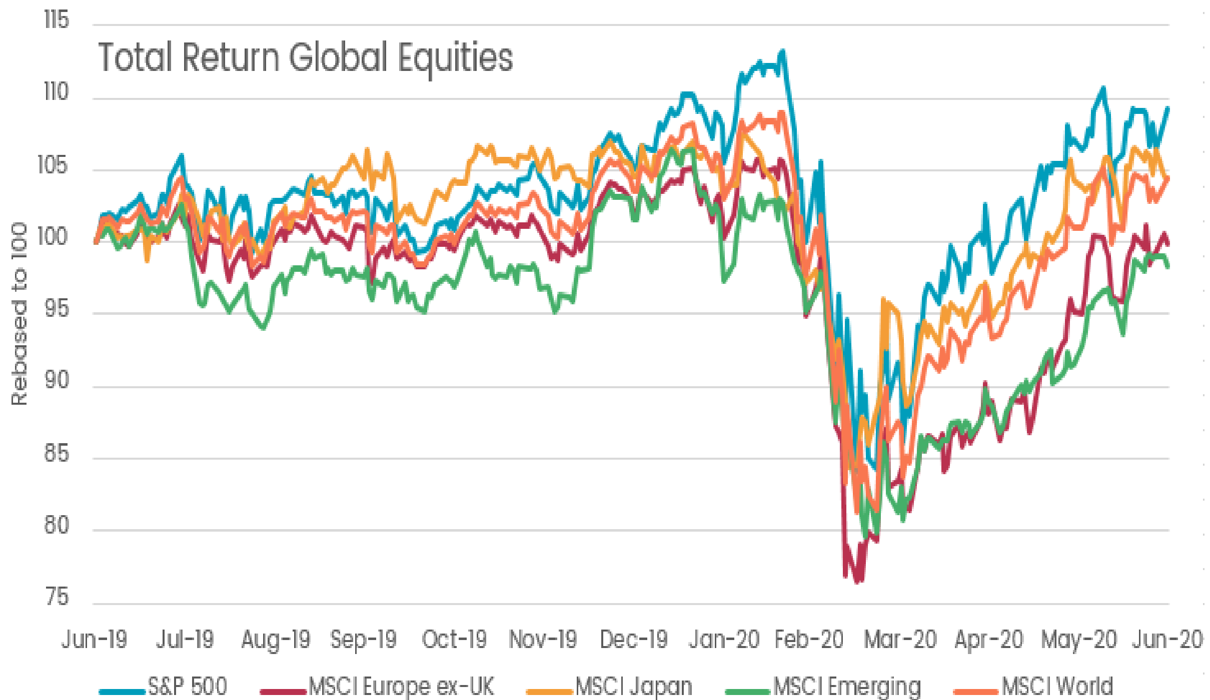
Source: - Bloomberg, G8LI, UC00, HW00, EMGB, ICE indices 7th August 2020.

Chart 2: - UK Bond index returns, 12 months to 30th June 2020.



Source: - Bloomberg

Chart 3: - Overseas equity markets returns in Sterling terms, 12 months to 30th June 2020.



Source: - Bloomberg

Recent developments (July and August 2020)

In July and August global equity market have continued to rally in local currency terms, but because of the weakness of the US dollar equity returns look much more mixed from a UK point of view as shown in table 1 above. The dispersion of sector and regional returns noted in the first half of 2020, remains in place as Covid remains the main driver of performance. The UK markets were further hindered by the strength of Sterling, which dents the earnings of most of the major companies in the FTSE indices.

The recovery from the first wave of Covid and the experience of a second wave of infections is most advanced in China and the Asia-pacific region. As economic activity has increased it has not been accompanied by a significant increase in infections save for a small number of isolated outbreaks which have been dealt with quickly and efficiently by the local authorities. The situation in Europe and the UK is much more mixed and is leading to more uncertainty especially in the UK where the government seems to stumble from one mis-step to another. The pace of economic activity in the USA seems to be slowing as the focus of infections moves away for the North-East to the South, Central and West coast states, which arguably both went into lockdown and then re-opened too early. Hence the rapid increase in infections and hospitalisations as activity increased.

Central bank policy makers have largely stepped back from making further monetary policy provisions, but fiscal policy makers in Europe have stepped up with new measures. In the UK the Chancellor announced a modified but also extended support for employment, reduced VAT for food and hospitality and sprinkled a bit of “helicopter money” in the form of “eat out to help out” in August. Much more significantly in Europe, the European Union agreed a Euro 750 billion Covid

recovery fund. This fund will be backed by bonds issued by the European Commission, this is a significant step on the path to fiscal integration and will benefit the southern European, smaller and newer member states the most. Sadly, the situation the USA is not as clear due to the further politicisation of the issue by President Trump. The employment support package, which had significantly boosted the income of the lowest paid workers in the US, expired at the end of July and as of 17th August a new package of measures has not been agreed. Officially 10.2% of the workforce is unemployed, but when the "absentee" workforce is added to the data the number is closer to 20%. Therefore, failure to approve even a reduced value support package could lead to a significant impact on the prospects for employment and future personal earnings and consumption.

July and August has also seen an increased temperature in the political situation in the USA. Joe Biden the Democrat Candidate for President has appointed the highly regarded Kamala Harris as his running mate. President Trump has been trying to do anything to help his chances of re-election, including a ban on postal votes, asking friendly state governors to close polling stations in some swing constituencies, in order to make it more difficult to vote. He has even suggested a delayed election date due to Covid, or what he prefers to call the "china virus". He has also turned up the pressure on China by closing embassies, sanctioning members of the Hong Kong administration and ordering Chinese companies operating in the USA to cease business operations, in order to try and recapture his lost popularity in poll ratings.

MJ HUDSON
Allenbridge

2. Investment Performance

Table 3 shows the performance of the Derbyshire Pension Fund versus the fund specific benchmark for the 3 months and year to the end of June 2020. The Fund's value sharply rebounded in the second quarter reversing most of the negative performance seen in the first quarter on 2020. At the end of June 2020, relative performance was slightly behind the benchmark over 3 and 12 months, but it should be remembered that the value of some of the Fund's Private market and Property assets may be subject to "material uncertainty" at both the March and June valuation points. Measured against longer time horizons, more appropriate for Pension Fund performance, the Fund continues to deliver positive returns and has outperformed the strategic benchmark on rolling 3,5,10 years and since inception on a net of fees basis.

Over 10 years the Fund has achieved a total return of 8.5% per annum.

Table 3: - Derbyshire Pension Fund and Benchmark returns

% TOTAL RETURN (NET) 30TH JUNE 2020	3 MONTHS		12 MONTHS	
	Derbyshire Pension Fund	**Benchmark**	**Derbyshire Pension Fund**	**Benchmark**
Total Growth Assets	**16.3**	**16.0**	**-2.0**	**-1.3**
UK Equity	10.5	10.2	-12.5	-13.0
Total Overseas Equity	**20.6**	**19.2**	**3.4**	**5.4**
North America	23.2	21.9	10.5	10.9
Europe	18.7	18.8	0.6	0.6
Japan	18.8	12.2	5.3	6.8
Pacific Basin	19.3	19.8	-2.0	2.8
Emerging markets	19.7	18.9	-5.6	-0.4
Global Sustainable Equity	17.8	19.7	0.0	5.7
Global Private Equity	0.2	10.3	-3.3	-12.0
Total Protection Assets	**6.1**	**7.1**	**7.7**	**9.0**
UK Gilts	1.6	2.5	7.9	11.2
UK & Overseas Inflation Linked	6.6	10.3	9.4	10.6
Global Corporate bonds	9.8	8.5	-	-
Total Income Assets	**1.8**	**1.0**	**2.6**	**-0.2**
Multi-asset Credit	6.2	6.5	-1.4	-0.3
Infrastructure	0.9	0.6	9.1	2.8
Property (all sectors)	-0.5	-2.2	0.6	-2.7
Internal Cash	0.0	0.0	0.2	0.4
Total Fund	**9.9**	**10.5**	**0.8**	**1.1**

Total fund value at 30th June 2020 £5,168 million

After a shocking performance in March, most equity markets have rebounded strongly in April, May and June, but the monthly pace of price moves slowed over the quarter. The country indices which were Technology sector heavy like the US and South-east Asia had the strongest returns and those with high weights to Cyclical, Energy and Financial sector stocks like the UK and Europe have lagged.

Over 3 months, Growth assets strongly outperformed the rest of the Fund, over 12 months the benefits of a diversified portfolio can clearly been seen given the mixed performance of growth, protection and income generating asset classes.

Growth assets – Equity performance

Over the quarter most of the regional portfolios outperformed their indices, but over the 12 months the performance is much more mixed and in aggregate growth assets underperformed their respective benchmarks. The negative performance of the UK over 12 month dominates this contribution but it should be noted that all regional equity portfolios underperformed their benchmark with the exception of Private Equity and the passively managed European equity portfolio.

North American equity performance was 1.3% ahead of the 22% market performance in the quarter, this has gone someway to repairing the poor relative 12 month, 3 and 5 year performance numbers. North American equity has delivered the highest annualised returns over 10 years at 17.1% p.a. and the highest outperformance of the benchmark index at +1.5% p.a.

The UK and continental European equity portfolios are passively managed by LGIM and UBS. The 3 and 12 month returns are in line with the benchmark.

The other equity assets are invested in Japan, the Pacific Basin and Emerging Markets equities, via a number of pooled funds selected by the in-house team, there were no significant changes in allocation. All 3 regional portfolios continue to deliver mixed performance over shorter periods but over the long term have in aggregate delivered reasonable returns and they have been an overall diversifier of risk, especially Japan.

Private equity continues to deliver strong positive absolute and relative returns that are significantly ahead of the benchmark over the more meaningful 3, 5 and 10 year periods, after US equity this is the second strongest performing equity allocation, but with the largest outperformance of the benchmark.

In April the in-house team began allocating cash to sustainable equity, at the end of the quarter the allocation was 1.7% compared to an index neutral allocation of 3%.

Protection assets - Fixed Income Performance

Over the quarter the bond portfolio delivered a return of 6.1% compared to the benchmark of 7.1%, despite the strong rebound in Index Linked Gilts and Global corporate bonds. This is because the Fund is slightly underweight relative to the strategic allocation and the Fund's assets have lower

aggregate duration (interest rate sensitivity) than the benchmark. The underperformance over 12 months can be attributed to the same reasons.

Income assets – Property, Infrastructure and MAC

Over the year, the combined portfolio of income assets has outperformed, the benchmark. Infrastructure and total property delivered another positive and above benchmark return. MAC experienced a strong rebound in the second quarter but remains behind benchmark over 1 year, but over 3 years returns are positive and slightly better than benchmark.

The total allocation to all property produced positive returns that were ahead of the benchmark over 3 months and well ahead of benchmark over 12 months. Over the longer-term direct property investments have helped the allocation outperform the benchmark whereas indirect property returns have been more mixed.

Infrastructure allocations continue to produce positive absolute returns well ahead of the benchmark, over 10 years returns have been the highest in the Fund at 14.8% p.a. This will not always be the case but it does demonstrate the value of diversification.

The Multi-Asset Credit (MAC) allocation a combination of private debt, high yield and emerging market debt had a strong quarter delivering a return of 6.2% with all sectors achieving positive returns. The 3y returns have recovered somewhat at 2.4% p.a. compared to 3.6% for the LIBOR based benchmark.

3. Economic and Market outlook

Economic outlook

It goes without saying that the Covid 19 Pandemic and the actions being taken by governments and central banks have the power to dominate all other drivers of economic activity in 2020 and into 2021. Until the virus is contained the global central banks are likely to continue their policy of "Financial Repression" meaning that interest rates and government bond yields will be held at extremely low levels in the hope that this will be enough to support economies and financial markets as they recover.

2020 will record the lowest level of global economic growth in the modern era. The almost total shut down of activity in the second quarter by all the developed and many of the developing economies cannot be offset by the recovery that began in China and south-east Asia. As I mentioned in my last report, it is the path of progress of the virus, the rate of recovery in the actual data and how the stimulatory measures are removed, that will drive the markets over the next 12 to 18 months. The longer the restrictions on activity remain in place the longer it will take to recover and the more likely that the economy will see permanent "scarring". While the development of a vaccine looks promising, it will be some time before it becomes clear which combination of the 29 vaccines that are being worked on, enables the infection to be contained.

The charts below are an attempt to assess how activity is increasing and the impact this is having on the level of infections in the USA and Europe. Chart 4 shows the USA, the left hand chart shows the level of infections and hospitalisations as they started to come out of lockdown in May. These are total cases for the whole of the USA, the first peak was driven by infections in New York and New Jersey, the second peak is driven by Florida, Arizona, Texas and California, where Covid arrived later, so this is not an indication of a second wave effect. It just reflects the later arrival of the first wave if infections in those states, in part probably because they locked down too early. The right hand charts are potentially more worrying from an economic point of view, especially as the employment support programme finished at the end of July. Small businesses and the consumer (like the UK) are the backbone of the US economy, both of these have flattened off and may be declining, having failed to return to their levels before Covid. Clearly the re-imposition of lockdown measures in some states and the fear and uncertainty created by the level of infections is slowing the pace of economic recovery.

Chart 4: - LHS. Total USA Covid cases. RHS. Small business and consumer activity

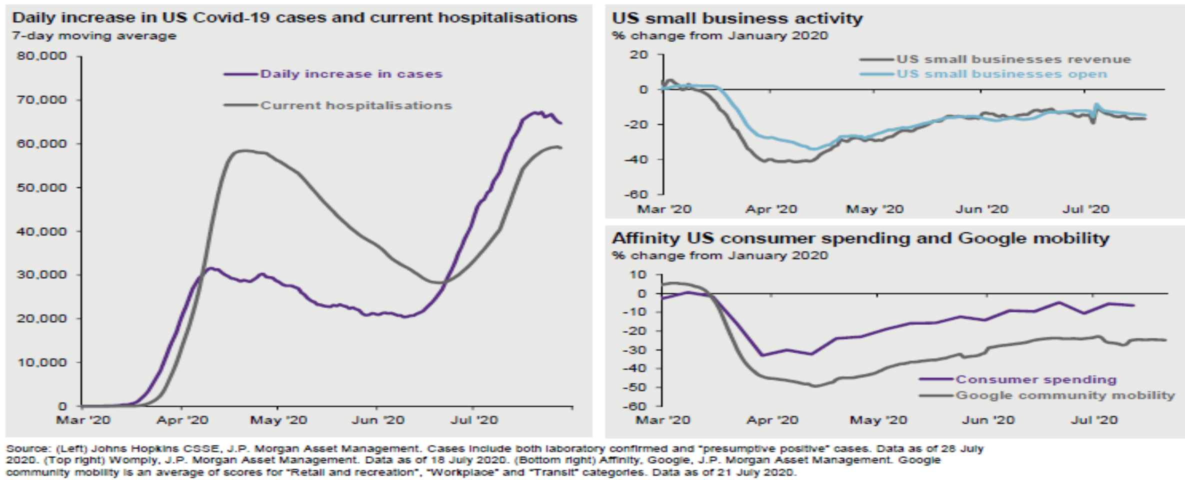


Chart 4: - LHS. Transportation activity. RHS. Reported cases of Covid in UK and Europe.

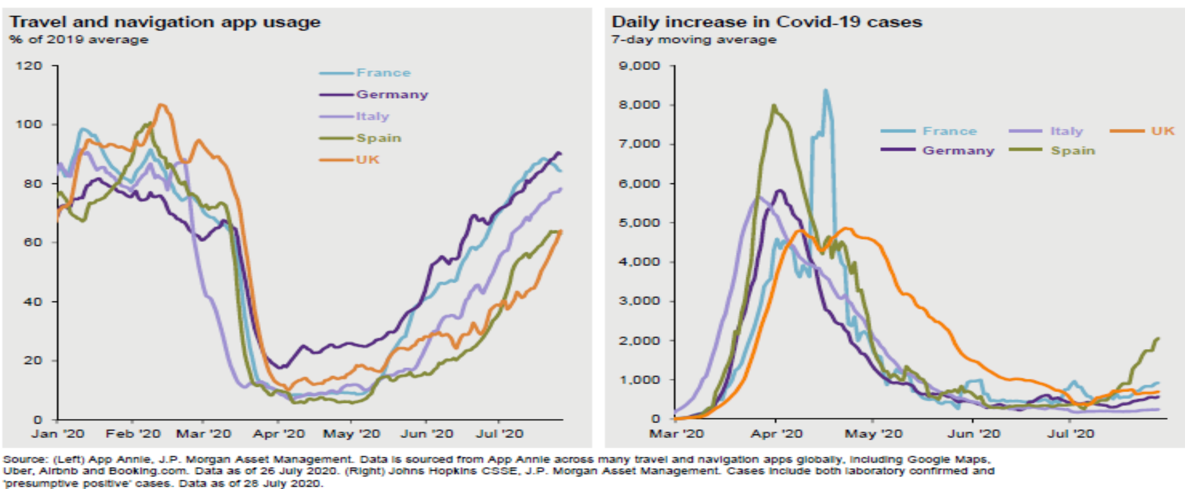


Chart 5 is an attempt to show the picture in Europe but here we only have transportation activity data to go on. The left hand chart appears to show that in much of Europe and the UK motor vehicle journeys have returned to near normal, but anecdotally I would suggest that journeys by public transport have not. The right hand chart shows the level of Covid infections, which outside of Spain seems to have remained broadly flat. Spain can probably be explained by the holiday season, Spain remains the place of choice for many people in Northern Europe to take their summer holiday, in the UK we tend to fly there, most of the rest of Europe drives there. Unlike the USA, most of Europe has kept its employment support schemes in place for longer which should help. In the UK the chancellors "Eat out to Help out" and VAT measures and the introduction of the widespread wearing of "masks" has encouraged people to feel more confident. Again anecdotally this does seem to be helping as some people are going out for the first time since March, but all the places to eat in holiday destinations are full of "staycationers" and for local pubs and restaurants, all it has done is shift eating out from Thursday, Friday and Saturday to Monday, Tuesday and Wednesday.

The observation I am trying to make using this data is that I believe economies have stopped shrinking and while weaker, the recovery has probably begun. The risk is the pace of the recovery could easily slow and take much longer to be achieved even if long term human behaviour has not been permanently changed by the pandemic. Also, the risk of localised lockdowns to contain

outbreaks of infection and the uncertainty this creates for businesses and the consumer, is a further reason to be cautious on near term economic growth.

On a more optimistic note, we know a lot more about Covid now and treatments to mitigate its effect are becoming increasingly available therefore I believe peak infection rates, hospitalisations and deaths could be substantially lower in each future wave of infection.

In the long term Covid and the mitigating actions put in place to tackle the virus are likely to be temporary but that does not mean that the virus may not have an impact on some of the long term issues that are already influencing the future development of the global economy.

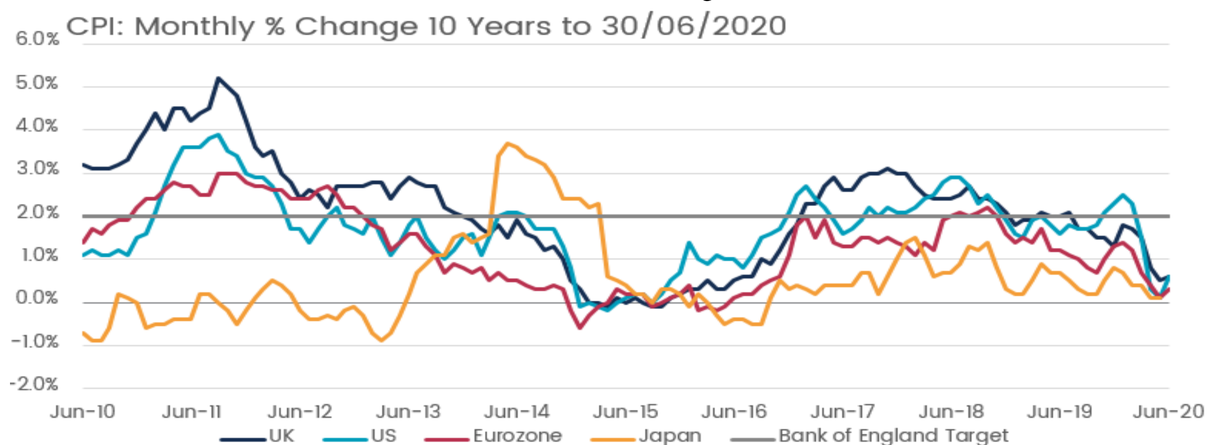
Thus far China and the south-east Asian economies appear largely unaffected by Covid compared to those of Europe and the USA where domestic consumption and leisure activities dominate the mix of economic activity. Technology and communications services which have been major beneficiaries of the pandemic and are at the core of future economic development. Aggregate demographics still favour emerging markets and expect the "fulcrum" of global economic power will continue to shift East towards Asia.

The Developed world will increasingly be weighed down by debt and demographics, with lower aggregate levels of return. In general, Emerging markets should do better because of the development of their own domestic markets, creating consumption for themselves rather than for the developed countries, as a result trade in goods could become more regional. The trend away from traditional retail to increased ecommerce will continue.

Inflation

While the most recent inflation prints for the developed economies have been higher as can be seen in chart 6 below, the medium term trend for inflation is broadly lower and well below the central bank's target rate of 2% p.a. In aggregate I expect it to remain low for a very long time, but there could be localised, short term hotspots resulting from extra costs caused by the implementation of Covid protection measures.

Chart 6: - Inflation – Annual rate versus Central Bank Target



Source: - Bloomberg

Central Banks

The Central banks have been pretty quiet since they announced their unprecedented levels of support for markets in March. The support measures put in place have stabilised the financial system, underpinned a huge rally in the value of global equity and both Investment grade and Sub-investment grade debt.

In the US the Fed made it clear in their recent meetings that the Fed Funds rate is unlikely to be changed until 2022. They also said they were unlikely to use negative policy rates as a tool but they would consider yield curve management. This means that they could attempt to fix long term bond yields, for instance the yield on 10 year US Treasury bonds at a certain level. Since the beginning of March, the US Fed has been the main buyer of debt issued by the US Government.

The Bank of England have raised the issue of negative rates further up the Agenda and have asked Banks and Building Societies to prepare for the possibility. I still believe that the lessons learned from the experience of the ECB and the Bank of Japan and the negative impact these policies have had on the profitability of the banking system will discourage their use in both the UK and the USA.

Politics

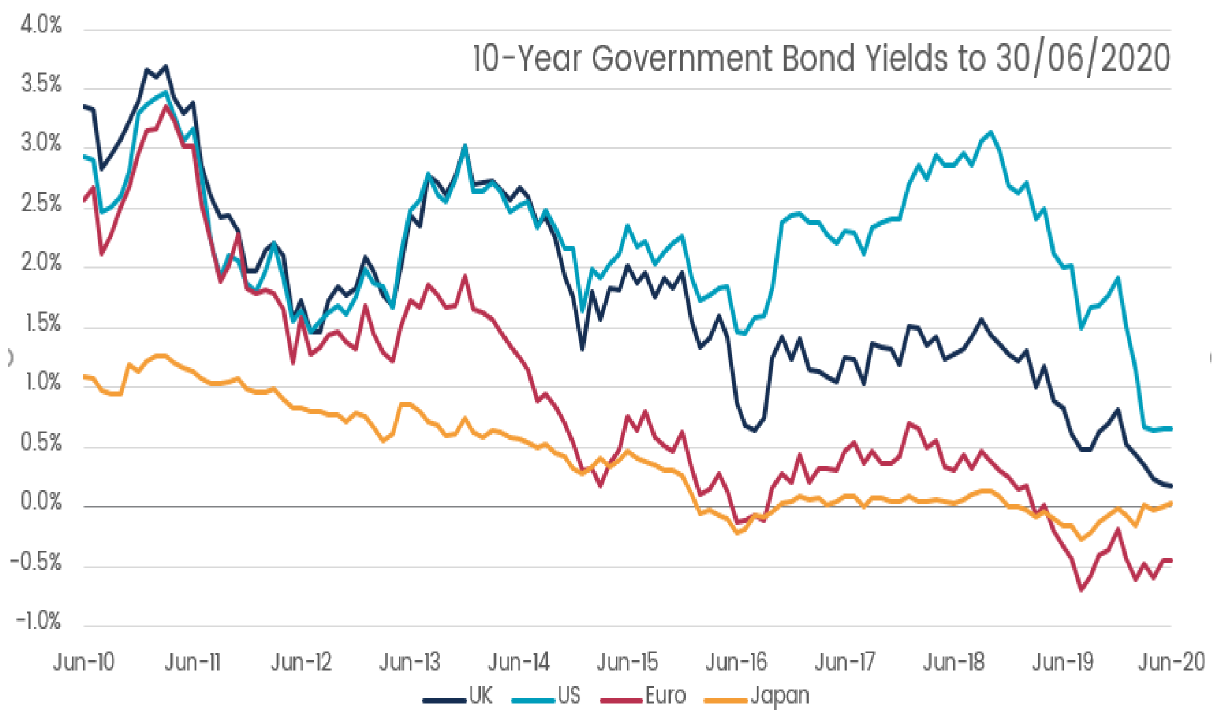
As mentioned above the US Presidential Election campaign is beginning to warm up, Mr Trump had to cancel the Republican Party convention in Florida due to the Pandemic. This will now be a virtual conference; it seems the Democrats had decided some time ago that theirs to be an on-line event. So far Mr Biden has not had to properly campaign and has just left Mr Trump to damage his chances of re-election, judging by the polls this is proving to be the right strategy at the moment. Should Mr Biden win and have a Democrat majority in Congress, the new administration is likely to adopt a less belligerent style in its negotiations with China, increase spending on Healthcare and do an about-face on Climate change policies. Equally because most of President Trump's "legislation" has been by Executive Order, most of it has not actually been passed into law by Congress, so much of it will simply disappear if he leaves office. If Mr Trump wins, then it will be more of the same as he is unlikely to win a majority in Congress. He is likely to continue to pack the supreme court with Conservative judges and is also expected to try and fill the Fed with people who are more compliant to pressure from the White House on the direction of monetary policy.

The European Union has agreed a Euro 750 billion Covid Recovery fund, Euro 390 billion will be in the form of Grants with the balance in loans. In terms of money it represents a net transfer from the richer Northern European countries of between 1 and 2% of GDP, to the poorer and smaller Southern European and new member countries, where the impact will be between 2% and 3% for Italy and Spain and 9% for Greece and 12% for Croatia. Most significantly, the recovery fund will be backed with common bond issuance by the European Commission. This is a significant step toward potential fiscal integration and further strengthens the European Union.

Government bonds

As can be seen in table 2 above and chart 7 below, Government bond yields have broadly tracked sideways close to their all-time lows since their dramatic falls in March and April. Unless the UK and US adopt a negative interest rate policy, I believe that government bond yields have reached the lower boundary and cannot fall much further on a sustainable basis. If the Fed adopts a policy of yield curve management, this will be achieved by targeted buying of certain maturities, thereby pegging the level of bond yields close to their current low levels. During the time that this policy is in place it would provide greater certainty for borrowing costs and allow government bonds to provide protection in the event of future equity market volatility, but it would also lead to extremely low cash like returns and could result in a sharp rise in yields once the policy comes to an end. Given the extremely high interest rate sensitivity of Government bonds this could lead to significant negative returns. Either way I maintain my view that over the longer term government bond yields will rise.

Chart 7: - Government bond yields, last 10 years.



Source: - Bloomberg

Non-government bonds

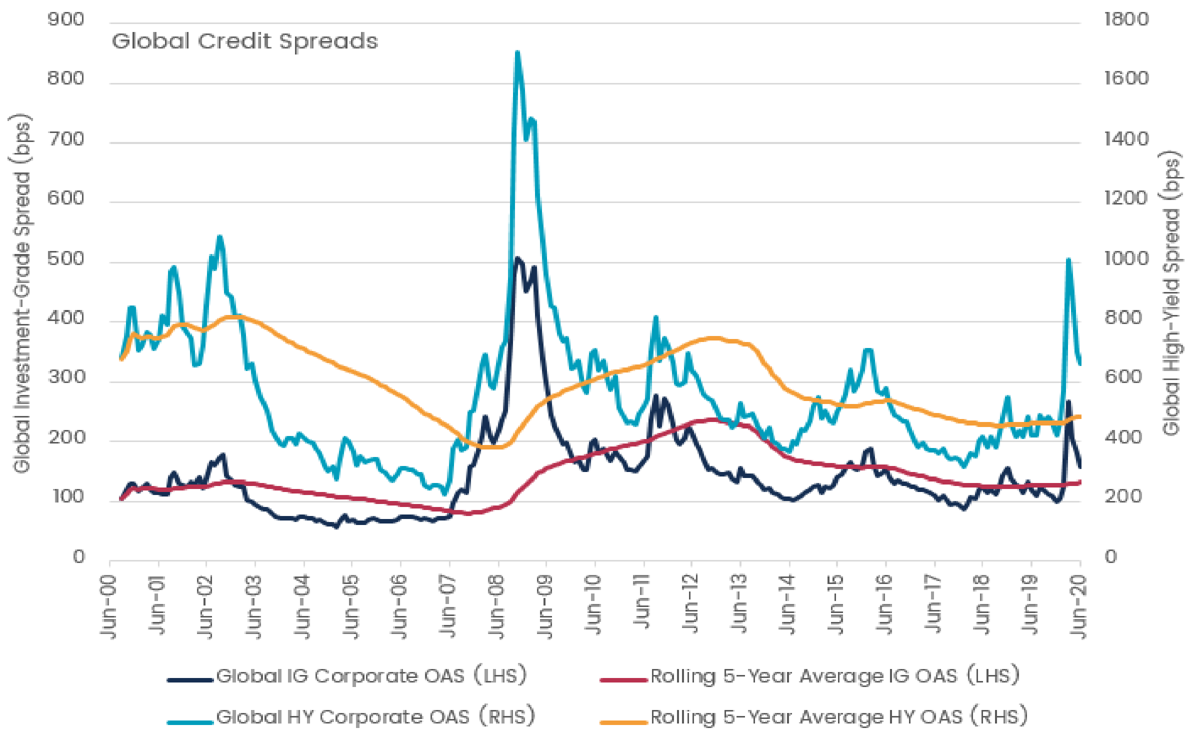
As can be seen in Chart 8 below, the excess yield spread for both investment grade non-government and high yield bonds narrowed sharply in the second quarter, as a result of the policy measures put in place by central banks, including offering to buy significant amounts of mostly investment grade corporate debt.

I still believe there is an opportunity to be exploited in sub-investment grade debt that can probably best be delivered by a Multi-Asset Credit manager. If my comments above, about a period of extended central bank financial repression are correct then both investment grade and sub-investment

grade bonds will deliver better returns than government bonds provided they have a lower default experience.

Spreads have narrowed significantly since the end of the second quarter, so the future return achieved from this asset class is likely to much more driven by the yield or income rather than the capital gain of further spread narrowing.

Chart 8: - Credit spreads, extra yield over government bonds, last 10 years.

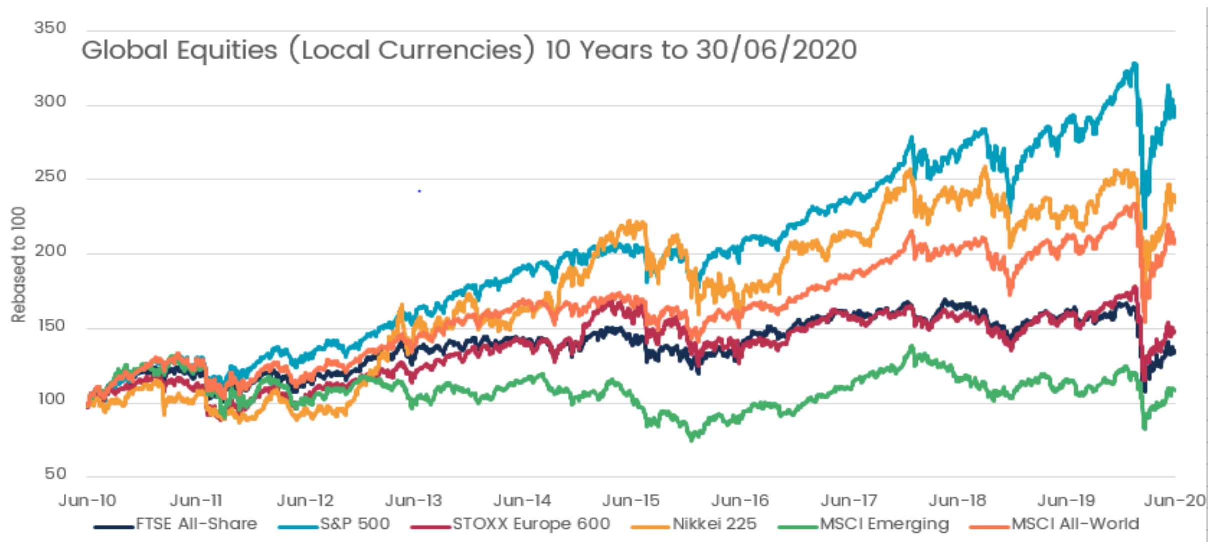


Source: - Bloomberg

Equities

As can be seen in Chart 9 below and in table 1 above equity market returns have been strongly positive in the second quarter. They are all still negative since the beginning of the calendar year but all equity market indices except the UK are positive over 12 months. In local currency and Sterling terms equity market index returns have been more mixed in July and August. Technology stocks continue to drive index returns, hence indices with higher weights to technology like emerging Asia and the USA have delivered the best returns.

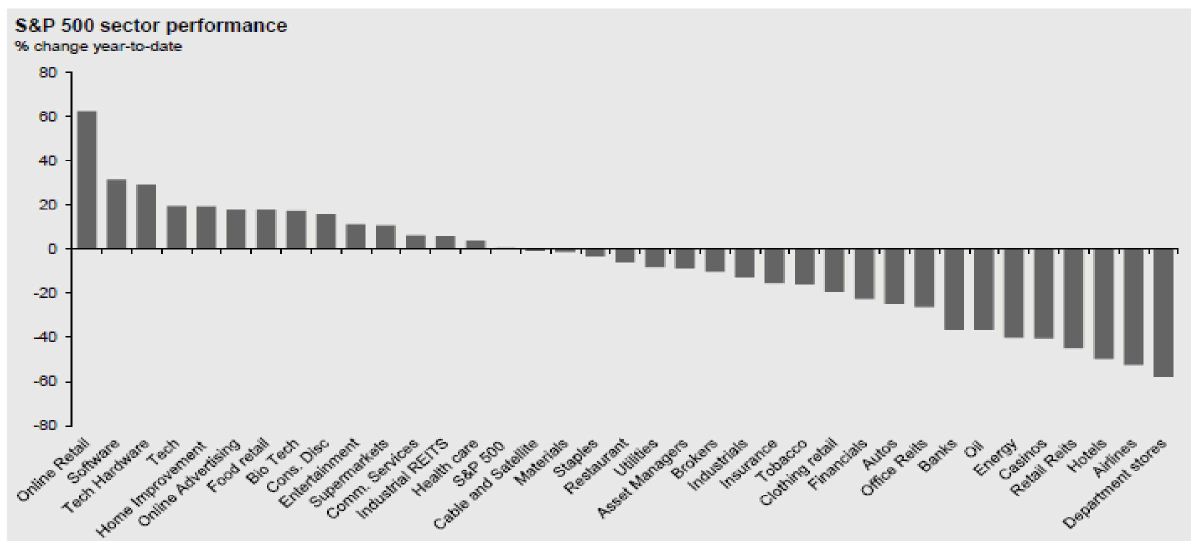
Chart 9: - Global equity indices, last 10 years.



Source: - Bloomberg

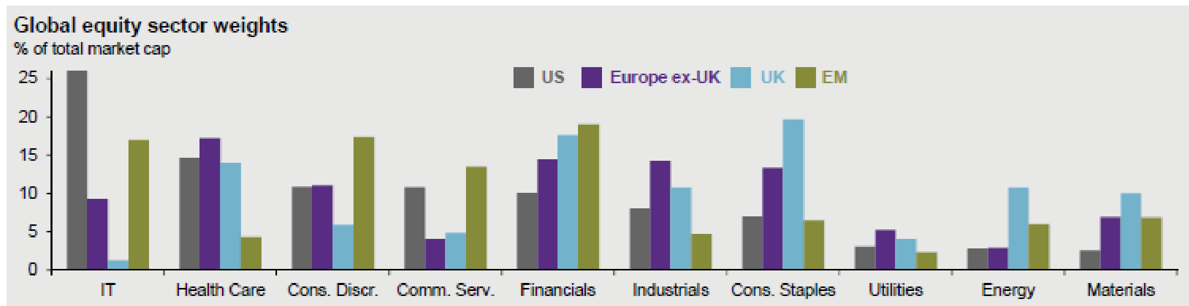
The recovery in markets remains highly differentiated by sector as can be seen in chart 10 below. This chart is for the US S&P 500, but it is a similar story for all other equity indices. This trend may continue for a while but over the longer term as activity returns, those equity market sectors and indices hardest hit like the UK should start to see improved performance.

Chart 10: - S&P 500 sector returns calendar year to date.



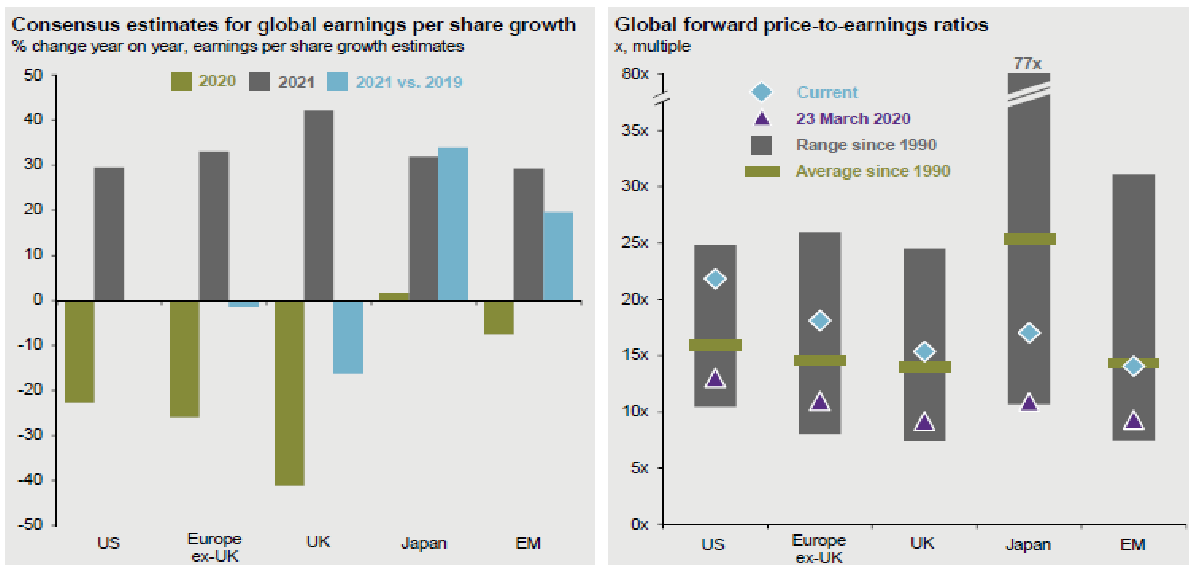
Source: Refinitiv Datastream, Standard & Poor's, J.P. Morgan Asset Management. Data as of 21 July 2020.

Chart 11: - Global equity sector weights.



Taking a look at the range of returns shown in chart 10 and the global sector weights in chart 11, it is clear to see the winners so far, but as the recovery broadens most of the other sectors should catch up over time.

Chart 12: - Left Hand Chart; Consensus earnings per share; Right Hand Chart; P/E ratios.



Source: JP Morgan Asset Management 30th June 2020

In chart 12 above I have shown consensus estimates for earnings per share (EPS) in 2020 and 2021 compared to actual EPS in 2019 and the resulting price earnings ratios at the 30th June compared to their history since 1990. As can be seen only in Japan and Emerging markets is EPS expected to be higher than 2019, elsewhere EPS is expected to be lower in 2021 than it was in 2019. This has elevated the P/E ratios to above average especially in the US, which leaves the markets vulnerable. either to fear of an increase in interest rates or lower earnings. While higher rates looks extremely unlikely, lower EPS is highly likely given the uncertainty being caused by an increase in the level of Covid infections as economies come out of lockdown.

For these reasons I would not recommend being overweight any part of the equity market, but I would suggest that the allocation is maintain as close to neutral as possible.

GDP

Table 4 shows the consensus forecasts for GDP growth in calendar 2020 and 2021 and my expectations in May and August 2020.

Table 4: - GDP forecasts - Consensus versus Advisor expectations.

% CHANGE YOY	2020				2021			
	MAY		AUGUST		MAY		AUGUST	
	Consensus	AF	Consensus	AF	Consensus	AF	Consensus	AF
US	-5.4	**-6.0**	-5.2	**-6.0**	4.3	**5.0**	4.0	**4.0**
UK	-7.9	**-9.0**	-9.9	**-10.0**	6.1	**6.5**	6.4	**6.4**
Japan	-5.5	**-6.0**	-5.3	**-6.0**	2.4	**3.0**	2.5	**2.5**
EU 28	-7.2	**-8.0**	-7.8	**-8.0**	5.6	**6.0**	5.3	**5.3**
China			2.1	**2.5**			7.8	**8.0**
SE Asia			-3.6	**-3.2**			5.7	**6.0**

Source: - Consensus Economics August 2020

Since the last PFC in June economies have been gradually coming out of lockdown, starting in the far east and through Europe and into the USA. At the same time the level of economic activity has increased and with it the number of infections. The increase in infections has caused local lock downs or restrictions on activity and/or movement to be re-imposed. The high frequency data that was surprising to the upside has been softened somewhat in response to the uncertainty created by the re-imposition of restrictions.

As can be seen in the table above consensus forecasts for GDP have not materially changed from May. I have maintained my more pessimistic view for developed economies in 2020 and I am now less optimistic for 2021, but I remain optimistic for China and South East Asia. I continue to believe that the numbers are not useful but the direction of growth expectations are reasonable. I also believe that it will take longer for these economies to return to the level of activity seen before the start of the pandemic.

In terms of actual data, first quarter GDP in China was revised to -10% quarter on quarter marking the 1st quarter of negative growth in the modern era. In the second quarter growth rebounded by 11.5% as both domestic and external demand improved following the removal of most Covid 19 restrictions.

In the US, fourth quarter 2019 growth was revised higher to 2.4% annualised. The estimate of first quarter growth was revised to -5%, but the advance figure for the second quarter was truly shocking - 32.9% the worst ever recorded. The US Fed expects the economy to shrink by 6.5% in 2020.

In the UK, the growth rate in the first quarter was -2.2% and the advance estimate of second quarter 2020 growth was -20.4%. Like the US this was the worst ever reported decline in GDP, but both outcomes were better than expectations.

The Japanese economy shrank by 7.8% in the second quarter of 2020, it was the third quarter of negative growth, this means the economy is 10.3% smaller than it was 12 months ago.

In the Euro-area second quarter growth was -12.1% after a slightly revised fall of 3.6% in the first quarter. The rest of the European economy joins Germany and France that were already in recession.

Consumer Price Inflation

Table 5 shows the consensus forecasts for Consumer Price Inflation in calendar 2020 and 2021 and my expectations in May and August 2020.

Table 5: - Consumer Price Inflation forecasts - Consensus versus Advisor expectations

% CHANGE YOY								
	2020				2021			
	MAY		AUGUST		MAY		AUGUST	
	Consensus	**AF**	Consensus	**AF**	Consensus	**AF**	Consensus	**AF**
US	0.7	**0.7**	0.8	**0.7**	1.8	**1.6**	1.7	**1.6**
UK	1.0	**1.0**	0.7	**0.6**	1.4	**1.2**	1.4	**1.2**
Japan	-0.4	**-0.4**	-0.1	**-0.2**	0.1	**0.0**	0.2	**0.0**
EU 28	0.5	**0.5**	0.6	**0.5**	1.2	**1.0**	1.2	**1.0**
China			2.7	**2.5**			2.0	**2.0**
SE Asia			1.0	**0.9**			2.1	**2.0**

Source: - Consensus Economics August 2020

The consensus forecasts for inflation in calendar 2020 and 2021 have not been materially changed. Despite the recovery in the oil price demand remains subdued. Anecdotal evidence would suggest some service prices have been marked higher due to Covid induced capacity constraints but these are being more than offset elsewhere. I continue to expect inflation to be lower than the consensus forecasts for some time to come.

The annual rate of US headline inflation picked up to 1% in July after recording a 4.5 year low of 0.1% in May, food and medical service prices were higher but energy prices were lower. Ex food and energy, core inflation also increased from an annual rate of 1.4% in April to 1.6% in July.

In July the UK headline inflation rate (CPIH) which includes housing costs was higher than the 0.8% reported in June at 1.1%, but this is down from 1.5% in March. Core inflation which excludes food, energy, alcohol and tobacco in the UK, was also lower at 1.4% p.a.

The July "flash" report of inflation in the Euro Area remains 0.4% p.a. but the core rate continues to steadily pick up and now stands at 1.2%.

The Japanese inflation rate was only 0.1% p.a. in June and the core rate that excludes fresh food was 0% p.a.

4. The outlook for the securities markets

As the shock and awe of the initial impact of unprecedented interventions from central banks and governments has subsided equity and credit markets have slowed their rate of advance. We now have the reality of navigating a path out of lock down and to containment of the virus through a vaccine or through learning to live with it.

The quick response of the central banks and their promises to underwrite the financial markets has bought governments time to work out what to do next. Going forward the outlook for the securities markets is now dominated by the respective national government response. The failure of the US government to extend the employment support programme is a concern as it will further slow the rate of the consumers recovery and risks dramatically increasing unemployment. The response in the UK and the deal on the recovery fund in the EU leaves these regions in a much better place. Equally the recovery of economic activity in China and South East Asia, the first regions to be impacted by the virus, gives some reason for optimism. But for the developed markets the short term outlook remains highly uncertain and the pace of economic activity looks likely to be lower.

The challenge for a pension fund is to look through the short term and focus on the medium to long term. The history of past crises is that after a sharp sell-off and recovery markets grind higher over an extended period of time. The easy money from the market recovery has been made now the chances are that we could have a set-back especially if either activity levels disappoint or infection rates get out of hand. However, over the medium to long term I expect equity and credit markets to deliver stronger returns than cash or government bonds.

Covid has turbo-charged many of the disruptive themes that have been acting on markets and economies for a while, even as we return to more normal levels of economic activity things may have changed and human behaviour and attitude to personal risk may be different. The Fund's allocation and the managers used may need to be adjusted to take advantage of the potential new landscape for investment. It is also possible that the regulatory framework for companies may change just as it did after the GFC. I believe it will be seen as unreasonable for companies not to be more resilient to market or financial shocks in future, especially if they have sought government support in this crisis. This could mean that the overall return on equity may be lower and practices like distributing high dividends, using debt to retire shareholder capital and taking on higher levels of leverage; could attract a higher degree of regulatory scrutiny as well as carrying a higher risk premium for investors.

Bond Markets

In table 6, below I have set out my expectations for 3 month LIBOR interest rates and benchmark 10 year government bond yields, over the next 3 and 12 months. They are not meant to be accurate point forecasts, more an indication of the possible direction of yields from August 2020.

Table 6: - Interest rate and Bond yield forecasts

%	CURRENT	MARCH 2021	SEPTEMBER 2021
UNITED STATES			
3month LIBOR	0.26	0.25	0.25
10 year bond yield	0.71	0.75	0.75
UNITED KINGDOM			
3month LIBOR	0.07	0.10	0.10
10 year bond yield	0.25	0.5	0.5
JAPAN			
3month LIBOR	-0.05	-0.10	-0.10
10 year bond yield	0.05	0.10	0.10
GERMANY			
3month EURIBOR	-0.50	-0.50	-0.50
10 year bond yield	-0.45	-0.25	-0.25

Source: - Bloomberg, Trading Economics; 14th August 2020

As can be seen in table 2 above government bond yields have continued to fall, making new "All Time Lows" as markets have responded to the Covid 19 pandemic. While 3 and 5 year government bonds in the UK have joined Germany and Japan in printing negative yields since mid-June, US government nominal yields remain above zero across the whole yield curve. There continues to be a lot of discussion about negative central bank policy rates, but I believe the Bank of England and the US Fed, will choose to adopt yield curve management instead, in order to prevent disruption in the wider banking and money markets. The main message I want to give from my forecasts in table 6 is that I expect government bond yields to remain around their current levels for some time. I do not expect central bank policy rates to change for the next 12 to 18 months. Over the long term I expect government bond yields to rise and there is the risk that yield curves could steepen if inflation becomes more of a concern, but for now central banks will do all they can to keep government yields at or close to their current levels.

With a background of very low central bank policy rates and low refinancing costs, the extra yield spread for non-government bond and high yield bonds in particular is very attractive, but spreads have narrowed significantly already. With most of the global economy in recession it is highly likely that the level of defaults in credit markets will increase, especially in those sectors of the economy that are more at risk from the pace of recovery. Active management, dynamic asset allocation and security selections skills will now, more than ever will be the key to success for investment in this asset class.

Bond Market (Protection Assets) Recommendations

The total allocation to Protection assets in the strategic benchmark is 18%. I continue to suggest that this is reduced to 16% and this 2% given to the MAC allocation in the Income asset portion of the Fund. I would take this 2% from conventional gilts and within the allocation to Protection assets I would take a further 1% from conventional gilts and allocate this money to Global corporate bonds, increasing this allocation to 1% overweight.

I believe this underweight recognises the value of owning protection assets against the risk of another sell off in growth assets, but it also reflects my view that government bonds will not provide as much protection as they have done in the past at these extremely low levels of yield.

As usual in table 7 below I have updated the data and recalculated my estimates of the total return impact of rising yields for government and non-government bond indices based on their yield and interest rate sensitivity (Duration) over 3 and 12 months. The estimates do not take into consideration any narrowing or widening of spread over the holding period but does indicate the level of losses that can be experienced in long duration assets for only a small change in yield.

Table 7: - Total returns from representative bond indices

INDEX	YIELD TO MATURITY %	DURATION	YIELD INCREASE %	% TOTAL RETURN, HOLDING PERIOD	
				3 MONTH	12 MONTHS
All Stock Gilts	0.41	13.4	0.5	-6.6	-6.3
All Stock Linkers	-2.36	15.4	0.5	-7.7	-7.5
Global IG Corporate	1.62	7.3	0.5	-3.2	-2.0
Global High Yield	5.58	3.8	0.5	-0.5	+3.7

Source: - ICE Indices 14th August 2020

In terms of the allocation to index linked gilts I would prefer to remain 2% underweight UK linkers with a 2% allocation to US TIPS. The real yield on TIPS has fallen over the quarter and but index linked gilt yields have fallen further so there is still a yield pick-up for holding TIPS and this market is not subject to the potential change of inflation indexation. UK Linkers remain overvalued relative to UK gilts and UK inflationary expectations. The consultation on the change to CPIH from RPI indexation closes in August. At the moment the Linker market has only priced in about 50% of the change in the market valuation. While asset managers continue to lobby for no change or compensation, Corporate Pension Fund trustees with RPI liabilities appear much more relaxed about the change. Broadly speaking there is an increasing consensus that the Chancellor will endorse the change in the Autumn Budget statement without compensation to bond holders.

Equity Markets

Table 8 below, shows the dividend yield for 2020 and the earnings growth and price / earnings ratio estimates, for 2020 and 2021 provided by Citi Research.

Table 8: - Dividend yield, Earnings growth and Price/Earnings Ratios

COUNTRY	DIVIDEND YIELD %	EARNINGS GROWTH		PRICE/EARNINGS RATIO	
FORECAST PERIOD	2020	2020	2021	2020	2021
United Kingdom	3.9	-34.8	32.3	18.2	13.8
United States	1.8	-18.5	26.9	25.2	19.9
Europe ex UK	2.8	-28.8	34.2	21.3	16.0
Japan	2.4	-11.5	28.2	19.7	15.4

Source: - Citi Research, Global Equity Strategist, July 2020

The data set out in the table of earnings growth, P/E ratios and dividends above is a better reflection than the data presented last quarter but once again I am sceptical about the optimism expressed for 2021. In aggregate the direction of the change is probably the only useful bit of information. Covid has split companies into 3 broad categories, those which have been able to carry on as normal, those which could re-open with some changes and those that can't yet fully re-open. Clearly the swing factor for earnings growth will come from those that "could" with those that "can't" unlikely to make a difference for some time. As the number of infections increases as activity starts to recover it will impact the "could" category most, thereby extending the period of below expected earnings and higher costs.

As I mentioned last time dividends are being passed or cut, to enable companies to better weather the loss of earnings during lockdown and re-opening. In the medium to long term I believe one of the changes we will see in markets is lower distributions to shareholders via the dividend and higher "cash" on company balance sheets. Having said that the dividend yield from equity, while not guaranteed like coupons on bonds, is likely to remain higher, maintaining the attractiveness of growth assets

Equity Market (Growth Assets), Recommendations

The equity markets have run out of steam since the end of the second quarter after 3 positive months, global and UK equity returns in July were negative as can be seen in table 1 above. The increase in the value of Sterling is partly responsible, regional returns were more mixed than seen in the preceding quarter. The dispersion between growth and technology stocks in particular and the rest of

the market has continued and is now extreme levels. In my last report I suggested a neutral allocation to all equity regions, I continue to believe this probably the best strategy for now.

Thus far the recovery of equity markets has been driven by the unprecedented monetary and fiscal stimulus measures and better than expected high frequency data. The risk for markets from here is the number of Covid infections is increasing as the level of activity in the economy goes up. This is leading to new restrictions on activity and a slowing of the pace of coming out of lockdown, which further weakens and extends the earnings recovery.

I still believe that over the next 12 to 18 months the Fund could be presented with the opportunity to adjust the regional allocations and maybe even go overweight Growth assets. But at the moment with the level of uncertainty maintaining a neutral or even slightly underweight position relative to the strategic benchmark may be the most prudent action.

Income Assets

As suggested above the low return from protection assets and the increased likelihood that they fail to provide as much protection as they did in the past suggests an overweight to Income assets.

I continue to favour a 2% overweight allocation and suggest that this money be used to increase the MAC allocation. My reason for this is the main opportunity in MAC comes from global high yield bonds, emerging debt, loans and the dynamic allocation between these sectors of the bond market. As can be seen in table 2 and chart 8 above spreads have narrowed significantly, but central banks remain determined to support the markets through bond purchases, an extended period of low policy rates and government bond yields. As always with this type of asset avoiding the risk of default is the key to success, but even at the current lower level of spread, sub-investment grade assets appear attractive despite the increased risk of default.

I believe Property should remain neutral overall, but over the next couple of years, I believe the uncertainty over the future use of buildings created by Covid has increased the potential volatility of the returns from this asset class. Certain types of building may need to be re-purposed, at a minimum property could see a medium term downward re-rating and the income generated by rents could have an impact beyond the short term. As a long term investor, the Fund can afford to “look through” the volatility and in low yield environment, property probably remains an attractive income asset class.

I would suggest holding the cash allocation neutral at 2%. At the end of July, the Fund was holding 6.6% in cash, however more than 3% of this figure is already promised for future investments. Given the current level of uncertainty a higher cash balance remains a good strategy for the Fund.

The asset allocation set out in table 9 below, shows the new Strategic benchmark allocations for the Derbyshire Pension Fund and my suggested relative weights as of 18th May and 17th August 2020. My suggested asset allocation weights are relative to the classification of assets and strategic benchmark ranges. These allocations represent an ideal objective for the Fund based on my expectations for economic growth and market performance, but they do not take into consideration the difficulty in reallocating between asset classes and the time needed by the In-house Team and their investment managers to find correctly priced assets for inclusion in the Fund.

Table 9: - Recommended asset allocation against the new Strategic Benchmark that came into effect on the 1st January 2019.

% ASSET CATEGORY	DERBYSHIRE STRATEGIC WEIGHT 1ST JANUARY 2019	ANTHONY FLETCHER 18TH MAY 2020	DERBYSHIRE STRATEGIC WEIGHT 1ST JANUARY 2019	ANTHONY FLETCHER 17TH AUGUST 2020
Growth Assets	**57**	**0**	**57**	**0**
UK Equity	**16**	**0**	**16**	**0**
Overseas Equity	**41**	**0**	**41**	**0**
North America	12	**0**	12	**0**
Europe ex UK	8	**0**	8	**0**
Japan	5	**0**	5	**0**
Pacific ex Japan	4	**0**	4	**0**
Emerging markets	5	**0**	5	**0**
Global Sustainable	3	**0**	3	**0**
Private Equity	4	**0**	4	**0**
Income Assets	**23**	+2	**23**	+2
Property	9	**0**	9	**0**
Infrastructure	8	**0**	8	**0**
Multi-asset Credit	6	+2	6	+2
Protection Assets	**18**	**-2**	**18**	**-2**
Conventional Gilts	6	**-3**	6	**-3**
UK index Linked	6	**-2**	6	**-2**
US TIPS	0	+2	0	+2
UK corporate bond	6	+1	6	+1
Cash	**2**	**0**	**2**	**0**

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Appendix

References

Source material was provided by, including but not limited to, the following suppliers: -

- Derbyshire Pension Fund, PEL performance services
- Citi Research,
- FTSE, Citigroup, IPD, Barclay's Global and ICE Indices
- Kames, Blackrock, M&G and JP Morgan, Asset Management
- Bank of England, UK Debt Management Office, UK OBR, UK Treasury, ONS
- US Bureau of Labour Statistics, US Commerce Dept. Executive office of the President of the United States.
- Bank of Japan, Japan MITI
- ECB, Eurostat
- Bloomberg, Markit, Trading Economics, DataStream and S&P
- Financial Times, Daily Telegraph, Wall Street Journal, New York Times, Washington Post

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Appendix 2

Investment Portfolio Valuation

July 2020

County Hall, Matlock, Derbyshire, DE4 3AH
Administered by Derbyshire County Council

DERBYSHIRE PENSION FUND

	DCC 31/07/2020 £m	DCC 31/07/2020 %
Growth Assets	**2,808**	**54.6%**
UK	789	15.3%
US	574	11.2%
Europe	431	8.4%
Japan	290	5.6%
Pacific (ex Japan)	214	4.2%
Emerging Markets	239	4.6%
Global Sustainable	111	2.2%
Private Equity	161	3.1%
Income Assets	**1,065**	**20.7%**
Infrastructure	344	6.7%
Property	406	7.9%
Direct	234	4.5%
Indirect	172	3.3%
Multi-Asset Credit	316	6.1%
Protection Assets	**927**	**18.0%**
Government	282	***5.5%***
UK	235	
Overseas	47	
Index Linked	317	***6.2%***
UK		
Overseas		
Non Government	328	***6.4%***
Cash	**340**	**6.6%**
LGPSC Regulatory Capital	**2**	**0.0%**
Total	**5,142**	**100.0%**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

UK EQUITIES Company name	Number held	Mkt price in local currency	Mkt Price GBP	Value in Sterling £
UK EQUITIES FUND				
LGIM UK EQUITY INDEX FUND				
UK EQUITIE: LGIM UK EQUITY INDEX FUND	64,187,672.92	**11.46**	**11.46**	735,590,732
UK EQUITIES TOTAL				**735,590,732**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID
NEW SECTORS
UK EQUITIES

Sector	Company Name	Number held	Mkt Price Pence	Total £
HOUSEHOLD GOODS				
UK Hous Gds Txtile	PETER GEESON 2nd PREFERRED ORDS	16,487	0.00	-
UK Household Goods Total				-
EQUITY INVESTMENT COMPANIES				
UK Investment Co's	ABERFORTH SML 1P	939,000	816.00	7,662,240
UK Investment Co's	BLACKROCK SMALLER COMPANIES TRUST PLC	830,000	1220.00	10,126,000
UK Investment Co's	MONTANARO UK SMALLER CO'S 10P	11,996,285	109.00	13,075,951
UK Investment Co's	RIVER & MERCANTILE UK MICRO	2,902,170	138.00	4,004,995
UK Investment Co's	STRATHDON INVESTMENTS PLC	20	1000.00	20,000
UK Equity Investment Companies Total				**34,889,185**
UNIT TRUSTS & OEICs				
UK Unit Trusts	LIONTRUST UK SMALLER COMPANIES FUND1	1,201,544.47	1551.70	18,644,366
UK Unit Trusts & OEICs Total				**18,644,366**

DERBYSHIRE PENSION FUND					
JULY 2020 PORTFOLIO VALUATION - BID					
US EQUITIES					
Sector	**Company Name**	**Number held**	**Mkt price USD/ CAN$**	**Mkt Price GBP**	**Value in Sterling £**
OIL & GAS PRODUCERS					
US Oil & Gas	BP PLC-SPONS ADR	47689	22.04	16.84	803,224
US Oil & Gas	CHEVRON CORP	42130	83.93	64.14	2,702,189
US Oil & Gas	CONCHO RESOURCES INC	14114	52.50	40.12	566,261
US Oil & Gas	DIAMONDBACK ENERGY INC	16685	39.86	30.46	508,242
US Oil & Gas	EOG RESOURCES INC	64191	46.84	35.80	2,297,725
US Oil & Gas	EXXON MOBILE CORP	128808	42.08	32.16	4,142,148
US Oil & Gas	MARATHON PETROLEUM CORP	59498	38.23	29.22	1,738,256
US Oil & Gas	PIONEER NATURAL RESOURCES CO	8691	96.92	74.07	643,710
US Oil & Gas Producers Total					**13,401,755**
OIL & GAS SERVICES					
US Oil & Gas Services	SCHLUMBERGER LTD	72724	18.14	13.86	1,008,143
US Forestry & Paper Total					**1,008,143**
CHEMICALS					
US Chemicals	CABOT CORP	52645	36.48	27.88	1,467,638
US Chemicals	CELANESE CORP	23009	97.21	74.29	1,709,290
US Chemicals	FMC CORP	29242	106.01	81.01	2,368,978
US Chemicals	INGEVITY CORP	22124	58.48	44.69	988,731
US Chemicals	LINDE PLC	20994	245.18	187.37	3,933,573
US Chemicals	PPG INDUSTRIES INC	32379	107.62	82.24	2,662,953
US Chemicals Total					**13,131,162**
INDUSTRIAL METALS					
US Industrial Metals	LIVENT CORP	42162	6.27	4.79	202,021
US Industrial Metals Total					**202,021**
AEROSPACE					
US Aero defence	BOEING CO/THE	9254	158.00	120.74	1,117,361
US Aero defence	LOCKHEED MARTIN CORP COM	16215	378.87	289.53	4,694,769
US Aero defence	NORTHROP GRUMMAN CORP	12692	325.01	248.37	3,152,346
US Aero defence	RAYTHEON TECHNOLOGIES CORP	68888	56.65	43.29	2,982,294
US Aerospace Total					**11,946,770**
GENERAL INDUSTRIAL					
US Div Ind	BALL CORP	46902	73.59	56.24	2,637,650
US Div Ind	DANAHER CORP	37807	203.80	155.74	5,888,212
US Div Ind	DYCOM INDUSTRIES INC	28757	42.83	32.73	941,236
US Div Ind	HONEYWELL INTERNATIONAL INC	37157	149.40	114.17	4,242,270
US Div Ind	INGERSOLL-RAND PLC	162204	31.58	24.13	3,914,540
US Div Ind	INGERSOLL-RAND PLC	162204	31.58	24.13	3,914,540
US Div Ind	KENNAMETAL INC	47830	26.95	20.60	985,068
US Div Ind	MERITOR INC	14200	22.75	17.39	246,875
US Div Ind	REXNORD CORP	61186	28.97	22.14	1,354,589
US Div Ind	STANLEY BLACK & DECKER INC	8108	153.31	117.16	949,929
US Div Ind	TRANE TECHNOLOGIES PLC	32486	111.81	85.45	2,775,773
US Div Ind	TRITON INTERNATIONAL LTD/BER	28181	31.47	24.05	677,735
US Div Ind	WABTEC CORP	31248	62.19	47.53	1,485,080
US General Industrial Total					**30,013,497**
ELECTRONIC EQUIPMENT					
US Electricity	FORTIVE CORP	75569	70.19	53.64	4,053,461
US Electricity	GENERAL ELECTRIC CO	137547	6.07	4.64	638,038
US Electricity	NVENT ELECTRIC PLC	68639	18.15	13.87	952,039

US Electronic Equipment Total					**5,643,538**
INDUSTRIAL TRANSPORT					
US Transportation	FEDEX CORP	23165	168.40	128.69	2,981,134
US Transportation	HUNT (JB) TRANSPORT SERVICES	11797	129.34	98.84	1,166,035
US Transportation	UBER TECHNOLOGIES INC	83107	30.26	23.12	1,921,824
US Industrial Transport Total					**6,068,992**
SUPPORT SERVICES					
US Support Services	GENPACT LTD	63158	39.82	30.43	1,921,926
US Support Services	TRANSUNION	5159	89.55	68.43	353,052
US Support Services	TRINET GROUP INC	38219	66.00	50.44	1,927,659
US Support Services Total					**4,202,637**
BEVERAGES					
US Beverages	COCA-COLA CO/THE	205789	47.23	36.09	7,427,577
US Beverages Total					**7,427,577**
FOOD PRODUCTION/PROCESS					
US Food Prod & Proce	MONDELEZ INTERNATIONAL INC-A	192927	55.47	42.39	8,178,209
US Food Production & Processing Total					**8,178,209**
HOUSEHOLD GOODS					
US Hous Gds Txtiles	UNDER ARMOUR INC-CLASS A	219688	10.51	8.03	1,764,477
US Hous Gds Txtiles	UNDER ARMOUR INC-CLASS C	261394	9.49	7.25	1,895,697
US Hous Gds Txtiles	VF CORP	115045	60.34	46.11	5,304,935
US Household Goods Total					**8,965,109**
PERSONAL GOODS					
US Personal Care / Hc	PROCTOR & GAMBLE CO/THE	126076	131.06	100.16	12,627,274
US Personal Goods Total					**12,627,274**
HEALTHCARE EQUIPMENT & SERVICES					
US Healthcare Equipm	ANTHEM INC	15459	273.71	209.17	3,233,546
US Healthcare Equipm	BOSTON SCIENTIFIC CORP	159248	38.57	29.48	4,693,866
US Healthcare Equipm	CENTENE CORP	36192	65.25	49.86	1,804,680
US Healthcare Equipm	EDWARDS LIFESCIENCES CORP	58445	78.41	59.92	3,502,078
US Healthcare Equipm	HCA HOLDINGS INC	21566	126.66	96.79	2,087,450
US Healthcare Equipm	IDEXX LABORATORIES INC	2983	397.75	303.96	906,714
US Healthcare Equipm	INTUITIVE SURGICAL INC	7023	685.44	523.81	3,678,740
US Healthcare Equipm	LABORATORY CRP OF AMER HLDGS	8428	192.92	147.43	1,242,536
US Healthcare Equipm	MCKESSON CORP	12780	149.72	114.42	1,462,237
US Healthcare Equipm	QUEST DIAGNOSTICS INC	12432	127.07	97.11	1,207,233
US Healthcare Equipment & ServicesTotal					**23,819,080**
PHARMACEUTICAL, BIOTECH					
US Pharm, Biotech	89BIO INC	14400	30.38	23.22	334,316
US Healthcare	AGILIENT TECHNOLOGIES INC	43002	96.33	73.62	3,165,609
US Healthcare	AKERO THERAPEUTICS INC	7200	35.11	26.83	193,184
US Healthcare	AKOUOS INC	14500	19.28	14.73	213,640
US Healthcare	ALNYLAM PHARMACEUTICALS INC	2766	145.76	111.39	308,104
US Healthcare	APELLIS PHARMACEUTICALS INC	11936	25.89	19.79	236,155
US Pharm, Biotech	ASSEMBLY BIOSCIENCES INC	7199	22.20	16.97	122,133
US Pharm, Biotech	ATRECA INC-A	14307	12.93	9.88	141,369
US Pharm, Biotech	ASTRAZENECA PLC-SPONS ADR	151499	55.77	42.62	6,456,802
US Pharm, Biotech	AVIDITY BIOSCIENCES INC	23400	28.18	21.54	503,923
US Healthcare	BAXTER INTERNATIONAL INC	60583	86.37	66.00	3,998,718
US Healthcare	BLACK DIAMOND THERAPEUTICS I	19600	27.81	21.25	416,547
US Healthcare	BLUEBIRD BIO INC	3300	60.55	46.27	152,699
US Healthcare	CONSTELLATION PHARMACEUTICAL	8700	26.87	20.53	178,646
US Pharm, Biotech	ELI LILLY & CO	70731	150.19	114.78	8,118,165
US Pharm, Biotech	FORMA THERAPEUTICS HOLDINGS	24400	34.96	26.72	651,881
US Pharm, Biotech	GENERATION BIO US	20500	19.64	15.01	307,682
US Pharm, Biotech	GLOBAL BLOOD THERAPEUTICS IN	7301	67.47	51.56	376,444

US Pharm, Biotech	GLYCOMIMETICS INC	27466	3.94	3.01	82,699
US Pharm, Biotech	G1 THERAPEUTICS INC	16294	14.67	11.21	182,669
US Pharm, Biotech	IMMUNOGEN INC	56400	4.10	3.13	176,714
US Pharm, Biotech	INCYTE CORP	5144	98.75	75.46	388,191
US Pharm, Biotech	KODIAK SCIENCES INC	5300	46.33	35.41	187,649
US Healthcare	LEGEND BIOTECH CORP-ADR	16100	35.12	26.84	432,103
US Healthcare	MADRIGAL PHARMACEUTICALS INC	3519	102.62	78.42	275,968
US Healthcare	MIRATI THERAPEUTICS INC	3263	121.71	93.01	303,494
US Healthcare	MYOKARDIA INC	6902	90.12	68.87	475,339
US Healthcare	NOVARTIS AG-SPONSORED ADR	51671	82.14	62.77	3,243,460
US Healthcare	ODONATE THERAPEUTICS INC	12709	36.38	27.80	353,330
US Healthcare	OYSTER POINT PHARMA INC	10107	22.37	17.10	172,781
US Pharm, Biotech	PFIZER INC	392465	38.47	29.40	11,537,990
US Pharm, Biotech	PPD INC	78207	29.38	22.45	1,755,919
US Pharm, Biotech	REATA PHARMACEUTICALS INC-A	1782	147.59	112.79	200,989
US Pharm, Biotech	REGENERON PHARMACEUTICALS	1967	632.03	483.00	950,056
US Pharm, Biotech	REVOLUTION MEDICINES INC	10100	24.12	18.43	186,168
US Pharm, Biotech	RIGEL PHARMACEUTICALS INC	37337	2.30	1.76	65,626
US Pharm, Biotech	ROYALTY PHARMA PLC-CL A	22525	43.07	32.91	741,390
US Pharm, Biotech	SATSUMA PHARMACEUTICALS INC	5500	23.61	18.04	99,235
US Pharm, Biotech	SEATTLE GENETICS INC	5698	166.07	126.91	723,137
US Pharm, Biotech	SYNDAX PHARMACEUTICALS	28834	14.11	10.78	310,913
US Pharm, Biotech	TCR2 THERAPEUTICS INC	15600	16.67	12.74	198,732
US Pharm, Biotech	TRICIDA INC	15035	13.38	10.22	153,733
US Pharm, Biotech	TURNING POINT THERAPEUTICS I	7371	59.32	45.33	334,145
US Pharm, Biotech	UROGEN PHARMA LTD	10204	22.05	16.85	171,944
US Healthcare	VERTEX PHARMACEUTICALS INC	4591	271.95	207.82	954,121
US Healthcare	WAVE LIFE SCIENCES LTD	11951	8.80	6.72	80,370
US Healthcare	UNITEDHEALTH GROUP INC	27172	302.63	231.27	6,284,064
US Pharmaceutical, Biotech Total					**56,898,941**
FOOD RETAIL					
US Retail Food & Drug	HOUGHTON MIFFLIN HARCOURT CO	102894	2.97	2.27	233,536
US Retail Food & Drug	HYATT HOTELS CORP-CL A	39147	47.97	36.66	1,435,077
US Retail Food & Drug	MCDONALD'S CORP	128259	194.21	148.42	19,035,596
US Retail Food & Drug	PERFORMANCE FOOD GROUP CORP	68588	28.01	21.41	1,468,143
US Food Retail Total					**22,172,351**
RETAILERS - GENERAL					
US Retailers Gen	AMAZON.COM INC	10151	3,163.86	2,417.82	24,543,309
US Retailers Gen	ETSY INC	35870	118.30	90.40	3,242,822
US Retailers Gen	ROSS STORES INC	73658	89.66	68.52	5,046,912
US Retailers Gen	TJX COMPANIES INC	189494	51.99	39.73	7,528,740
US Retailers - General Total					**40,361,783**
MEDIA					
US Media & Photo	CHARTER COMMUNICATIONS INC-A	23651	579.00	442.47	10,464,901
US Media & Photo	ELECTRONIC ARTS INC	26026	141.60	108.21	2,816,292
US Media & Photo	FACEBOOK INC	57342	253.67	193.85	11,116,011
US Media & Photo	MATCH GROUP INC	47344	106.87	81.67	3,866,587
US Media & Photo	NETFLIX INC	20317	489.26	373.89	7,596,374
US Media & Photo	NEW YORK TIMES CO-A	27067	46.13	35.25	954,181
US Media & Photo	OMNICOM GROUP	71035	53.74	41.07	2,917,273
US Media & Photo	SNAP INC-A	175105	22.41	17.13	2,998,800
US Media & Photo	WALT DISNEY COMPANY	23929	116.95	89.37	2,138,611
US Media Total					**44,869,029**
TRAVEL & LEISURE					
US Hotels Leisure	JETBLUE AIRWAYS CORP	85165	10.34	7.90	672,959
US Travel & Leisure Total					**672,959**
TELECOMS					

Telecoms	T-MOBILE US INC	17783	107.38	82.06	1,459,269
US Telecoms Total					**1,459,269**
ELECTRICITY					
US Electricity	DUKE ENERGY CORP	86344	84.73	64.75	5,590,832
US Electricity	EDISON INTERNATIONAL	85199	55.64	42.52	3,622,669
US Electricity	EXELON CORP	159957	38.60	29.50	4,718,431
US Electricity	FIRSTENERGY CORP	179298	28.99	22.15	3,972,196
US Electricity	SOUTHERN CO/THE	17186	54.60	41.73	717,091
US Electricity Total					**18,621,219**
BANKS, RETAIL					
US Banks Retail	BANK OF AMERICA CORP	592777	24.87	19.01	11,266,115
US Banks - Retail Total					**11,266,115**
NON-LIFE INSURANCE					
US Insurance	AMERICAN INTERNATIONAL GROUP	80607	32.13	24.55	1,979,204
US Insurance	ASSURANT INC	33645	107.47	82.13	2,763,216
US Insurance	ASSURED GUARANTY LTD	79000	21.84	16.69	1,318,520
US Insurance	ATHENE HOLDING LTD-CLASS A	63511	32.25	24.65	1,565,257
US Insurance	HARTFORD FINANCIAL SVCS GRP	77491	42.31	32.33	2,505,540
US Insurance	MARSH & MCLENNAN COS INC COM	20196	116.51	89.04	1,798,190
US Insurance	PROGRESSIVE CORP	44859	90.32	69.02	3,096,282
US Insurance	RENAISSANCERE HOLDINGS LTD	10500	180.41	137.87	1,447,628
US Insurance	TRUPANION INC	41295	50.57	38.65	1,595,870
US Non-Life Insurance Total					**18,069,707**
REAL ESTATE					
US Real Estate	AMERICAN TOWER CORP	33996	261.38	199.75	6,790,585
US Real Estate	ALEXANDRIA REAL ESTATE EQUIT	26330	177.41	135.58	3,569,735
US Real Estate	DOUGLAS EMMETT INC	79400	29.13	22.26	1,767,535
US Real Estate	EQUINIX INC	11063	785.09	599.97	6,637,421
US Real Estate	SUN COMMUNITIES INC	7115	149.90	114.55	815,049
US Real Estate Total					**19,580,325**
GENERAL FINANCIAL					
US Special Finance	AMERICAN EXPRESS CO	22392	93.30	71.30	1,596,546
US Special Finance	ARES MANAGEMENT CORP - A	98817	39.90	30.49	3,013,086
US Special Finance	BLACKROCK INC	2056	575.02	439.43	903,469
US Special Finance	CHARLES SCHWAB CORP	137656	33.14	25.33	3,486,219
US Special Finance	EQUITABLE HOLDINGS INC	170061	20.46	15.64	2,658,994
US Special Finance	THE BLACKSTONE GROUP INC-A	65944	53.25	40.69	2,683,502
US Special Finance	EQUIFAX INC	5269	162.56	124.23	654,559
US Special Finance	FLEETCOR TECHNOLOGIES INC	17269	258.56	197.59	3,412,209
US Special Finance	GLOBAL PAYMENTS INC	61186	177.84	135.91	8,315,503
US Special Finance	HAMILTON LANE INC-CLASS A	29760	72.11	55.11	1,639,968
US Special Finance	IHS MARKIT LTD	93800	80.69	61.66	5,784,017
US Special Finance	LPL FINANCIAL HOLDINGS	7000	79.08	60.43	423,031
US Special Finance	ONEMAIN HOLDINGS INC	49153	28.70	21.93	1,078,050
US Special Finance	PAYPAL HOLDINGS INC	34813	196.14	149.89	5,218,127
US Special Finance	S&P GLOBAL INC	11918	350.18	267.61	3,189,347
US Special Finance	TD AMERITRADE HOLDING CORP	47474	35.88	27.42	1,301,713
US Special Finance	THERAPEUTICS ACQUISITION-A	37100	14.16	10.82	401,462
US Special Finance	VISA INC CL A SHS	37868	190.39	145.50	5,509,644
US Special Finance	VOYA FINANCIAL INC	39509	49.40	37.75	1,491,523
US Special Finance	WEX INC	10373	158.36	121.02	1,255,327
US General Financial Total					**54,016,298**
SOFTWARE					
US Software & Comp S	ADOBE SYSTEMS INC	5440	444.40	339.61	1,847,481
US Software & Comp S	ALPHABET INC - CL A SHARES	19162	1,487.86	1,137.02	21,787,627

US Software & Comp S	BLUCORA INC	6134	11.77	8.99	55,173
US Software & Comp S	GUIDEWIRE SOFTWARE INC	12436	117.60	89.87	1,117,622
US Software & Comp S	MICROSOFT CORP	199452	205.06	156.71	31,255,495
US Software & Comp S	Q2 HOLDINGS INC	20223	94.05	71.87	1,453,488
US Software & Comp S	SALESFORCE.COM INC	34511	194.85	148.90	5,138,839
US Software & Comp S	SCIENCE APPLICATIONS INTERNATIONA	16797	79.98	61.12	1,026,645
US Software & Comp S	SERVICENOW INC	6041	439.03	335.51	2,026,796
US Software & Comp S	SLACK TECHNOLOGIES INC-CL A	19727	29.53	22.57	445,176
US Software & Comp S	SPLUNK INC	7199	209.63	160.20	1,153,274
US Software & Comp S	SPOTIFY TECHNOLOGY SA	7789	257.54	196.81	1,532,969
US Software & Comp S	SS&C TECHNOLOGIES HOLDINGS	19058	57.49	43.93	837,291
US Software & Comp S	SVMK INC	74976	23.96	18.31	1,372,828
US Software & Comp S	VERISIGN INC	10816	211.53	161.65	1,748,420
US Software & Comp S	WORKDAY INC-CLASS A	13963	180.92	138.26	1,930,511
US Software Total					**74,729,636**
TECHNOLOGY HARDWARE					
US IT Hardware	ADVANCED MICRO DEVICES	93743	77.42	59.16	5,546,245
US IT Hardware	APPLE INC	96478	425.18	324.92	31,347,878
US IT Hardware	CORNING INC	127791	31.00	23.69	3,027,394
US IT Hardware	KLA-TENCOR CORP	19153	199.67	152.59	2,922,514
US IT Hardware	LAM RESEARCH CORP	4103	377.16	288.23	1,182,590
US IT Hardware	LATTICE SEMICONDUCTOR CORP	125127	31.10	23.77	2,973,846
US IT Hardware	LUMENTUM HOLDINGS INC	35302	92.82	70.93	2,504,078
US IT Hardware	MARVELL TECHNOLOGY GROUP LTD	135867	36.46	27.86	3,785,626
US IT Hardware	MICRON TECHNOLOGY INC	69469	50.05	38.25	2,657,065
US IT Hardware	TAIWAN SEMICONDUCTOR-SP ADR	44023	78.87	60.27	2,653,374
US IT Hardware	TERADYNE INC	32189	88.94	67.97	2,187,820
US IT Hardware	TEXAS INSTRUMENTS INC	37765	127.51	97.44	3,679,940
US Technology Hardware Total					**64,468,372**
TOTAL UNITED STATES					**573,821,769**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

EUROPEAN EQUITIES Company name	Number held	Mkt price in local currency	Mkt Price GBP	Value in Sterling £
EUROPEAN				
PASSIVE TRACKER FUND				
EUROPEAN UBS LIFE EUROPE EX-UK EQUITY T	127,335,613	**338.77**	**3.39**	431,374,856
EUROPEAN EQUITIES TOTAL				**431,374,856**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

OTHER EQUITIES		Company name	Number held	Mkt price in local currency	Mkt Price GBP	Value in Sterling £
JAPAN						
Investment Companies						
Japan	GB00BYSRMH16	CC Japan Income & Growth Trust	5,000,000	**114.00**	**114.00**	5,700,000
Japan	GB0001740025	JPMorgan JAP IT 25P	3,981,500	**508.00**	**508.00**	20,226,020
Japan	GB0003165817	JPMF japs smoc	2,109,500	**427.00**	**427.00**	9,007,565
Japan	GB0008022849	Schroder Japan Growth Fund 10p ords	4,985,000	**161.00**	**161.00**	8,025,850
J Investment Companies Total						**42,959,435**
Unit Trusts & OEICs						
Japan	GB0006011133	Baillie Gifford OGF - Japanese B Acc Shares	4,524,639.67	**1,694.00**	**1,694.00**	76,647,396
Japan	GB00B9M3QZ64	Barings Jap Growth Trst-IGBA	5,282,832.62	**239.20**	**239.20**	12,636,536
Japan	GB00B3RS8478	Invesco Japan FD-UKNTACC	4,579,026.99	**165.87**	**165.87**	7,595,232
Japan	GB0030879471	JPMorgan Jap Fd A Acc	3,000,000.00	**568.10**	**568.10**	17,043,000
Japan	GB0007650640	Schroder UT Tokyo Ac	11,000,000.00	**321.30**	**321.30**	35,343,000
J Unit Trusts Total						**149,265,164**
Life Policies						
Internatio	0	LGIM Japan Equity Index Fund	26,141,158.640	**1.89**	**1.89**	49,341,437
International Life Policies						**49,341,437**
Investment Entities						
Japan	LU0278933410	Aberdeen Global - JAP Smaller Cos Fund D£	1,662,639.78	**11.12**	**11.12**	18,487,390
Japan	IE0034388797	JO Hambro - Japan Fd GBP-A	15,000,000.00	**1.97**	**1.97**	29,595,000
J Investment Entities Total						**48,082,390**
JAPAN TOTAL						**289,648,426**
OTHER ASIA						
Investment Companies						
Asian	GB00B0P6J834	ABERDEEN ASIAN INCOME FUND ORDS	2,840,000	**181.00**	**181.00**	5,140,400
Asian	GB00BBM56V29	ABERDEEN NDIT 25P	4,876,000	**254.00**	**254.00**	12,385,040
Asian	GB0002945029	ASIA DRAGON TRUST 20P	6,131,500	**399.00**	**399.00**	24,464,685
OA Investment Companies Total						**41,990,125**
Unit Trusts & OEICs						
Asian	GB0030184088	Stewart Investors Asia Pacific & Japan Sustainabi	5,250,000	**1,464.16**	**1,464.16**	76,868,400
Asian	GB0030879695	JPMorgan Asia Fund A Ac	20,000,000	**263.20**	**263.20**	52,640,000
Asian	GB0007646747	Schroder Instl PAC Fd Ac	2,000,000	**1,544.00**	**1,544.00**	30,880,000
OA Unit Trusts Total						**160,388,400**
Investment Entities						
Asian	IE00B3BC9S63	Barings Australia Fund-IUSDA $	109,543.282	**136.67**	**104.44**	11,441,052
OA Investment Entities Total						**11,441,052**
OTHER ASIA TOTAL						**213,819,577**
EMERGING MARKETS						
Investment Companies						
Internatio	GG00B45L2K95	ABERDEEN EMERGING MARKETS	2,788,425	**535.00**	**535.00**	14,918,074
Internatio	GB00B3SXM832	BLACKROCK FRONTIERS INV TRUST	2,950,000	**90.00**	**90.00**	2,655,000
Internatio	GB0003418950	JP Morgan EMER IT25P	1,673,500	**1,040.00**	**1,040.00**	17,404,400
Int'l Investment Companies Total						**34,977,474**
Unit Trusts & OEICs						
Internatio	GB0030187438	Stewart Investors Global Emerging Markets Funf	3,000,000	**750.27**	**750.27**	22,508,100
Latin Ame	GB0001531861	Thd ndle Lnamer Gwth	3,500,000	**230.70**	**230.70**	8,074,500
Int'l Unit Trusts Total						**30,582,600**
Life Policies						
Internatio	0	LGIM World Emerging Markets Index Fund	36,576,132.890	**3.62**	**3.62**	132,268,441
International Life Policies						**132,268,441**
Investment Entities						
Latin Ame	LU0053687314	JPMorgan LNAMER A U$	86,085.904	**39.74**	**30.37**	2,614,369
Internatio	LU0781734594	POLUNIN FUNDS-DEVEL CNTY-B	47,502.659	**1,052.17**	**804.07**	38,195,383
LatAm Investment Entities Total						**40,809,753**
EMERGING MARKETS TOTAL						**238,638,267**
OTHER EQUITIES TOTAL						**742,106,270**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

GLOBAL SUSTAINABLE FUNDS	Company name	Number held	Mkt price in local currency	Mkt Price GBP	Value in Sterling £
GLOBAL SUSTAINABLE FUNDS					
GLOBAL SUSTAINABLE FUNI	Baillie Gifford positive Change Fund B	21,595,663.46	**276.90**	**2.77**	59,798,392
GLOBAL SUSTAINABLE FUNI	RBC Global Equity Focus Fund	395,114.71	**128.69**	**128.69**	50,847,313
UK EQUITIES TOTAL					**110,645,705**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

OTHER EQUITIES Company name	Number held	Mkt price in local currency	Value in Sterling £
PRIVATE EQUITY			
Quoted Private Equity			
UK Invesl APAX GLOBAL ALPHA LTD	3,000,000	158.60	4,758,000
UK Invesl HARBOURVEST GLOBAL PRIVATE	925,000	1528.00	14,134,000
UK Invesl HGCAPITAL TRUST PLC	7,053,150	246.00	17,350,749
UK Invesl ICG ENTERPRISE TRUST PLC	181,795	788.00	1,432,545
UK Invesl NB PRIVATE EQUITY PARTNERS Ltd (A)	1,500,000	11.50	13,182,450
UK Invesl PANTHEON INTERNATIONAL PLC	345,000	2030.00	7,003,500
UK Invesl PRINCESS PRIVATE EQUITY HOLDING LTD	500,000	8.72	3,924,828
UK Invesl STANDARD LIFE PRIVATE EQUUITY	900,000	303.00	2,727,000
UK Invesl SCHRODER UK PUBLIC PRIVATE	5,000,000	25.10	1,255,000
UK Quoted Private Equity Total			**65,768,072**
Unquoted Private Equity			
UK Uncla ADAM STREET PARTNERS (FEEDER) 2017 FU	30,000,000	0.59	13,480,520
UK Uncla BAIRD CAPITAL PARTNERS EUROPE FUND L	4,300,000	0.03	118,787
UK Uncla CAPITAL DYNAMICS GLOBAL SECONDARIES	20,000,000	0.63	9,641,161
UK Uncla CAPITAL DYNAMICS MID-MARKET DIRECT FI	25,000,000	0.94	21,089,836
UK Uncla CAPITAL DYNAMICS LGPS COLLECTIVE PE \	20,000,000	0.48	9,509,956
UK Uncla CAPITAL DYNAMICS CPEP LGPS	25,000,000	0.14	3,500,000
UK Uncla CATAPULT GROWTH FUND UNITS	3,000,000	0.14	410,368
UK Uncla EAST MIDLANDS VENTURE	3,000,000	0.07	212,682
UK Uncla EPIRIS FUND II	25,000,000	0.25	6,158,685
UK Uncla GRAPHITE CAPITAL PARTNERS FUND 1X A	11,250,000	0.26	2,878,298
UK Uncla GRAPHITE CAPITAL PARTNERS FUND 1X C	11,250,000	0.26	2,878,302
UK Uncla MOBEUS EQUITY PARTNERS IV LP	10,000,000	0.51	5,127,489
UK Invesl PANORAMIC ENTERPRISE CAPITAL UNITS	1,428,486	1.02	1,451,066
UK Invesl PANORAMIC GROWTH FUND 2 LP	10,000,000	0.34	3,431,922
UK Invesl PARTNERS GROUP GLOBAL VALUE 2008	7,500,000	0.32	2,178,654
UK Invesl STAR CAPITAL STRATEGIC ASSETS III LP	12,500,000	0.43	4,822,582
UK Uncla VESPA CAPITAL II LLP	10,000,000	0.83	8,282,218
UK Unquoted Private Equity Total			**95,172,528**
PRIVATE EQUITY TOTAL			**160,940,600**
INFRASTRUCTURE			
UK Infrastructure Quoted			
Closed-er FORESIGHT SOLAR FUND LTD	4,000,000	107.50	4,300,000
Closed-er GREENCOAT UK WIND PLC	11,875,000	146.20	17,361,250
Closed-er HICL INFRASTRUCUTRE CO LTD	6,060,872	167.80	10,170,143
Closed-e INTERNATIONAL PUBLIC PARTNERSHIP LTD	20,462,823.00	163.20	33,395,327.14
Closed-e 3I INFRASTRUCTURE PLC	2,249,999.00	290.00	6,524,997.10
Closed-e RENEWABLES INFRASTRUCTURE GR	8,111,111.00	133.00	10,787,777.63
UK Infrastructure Quoted Total			**82,539,495**
UK Infrastructure Unquoted			
UK Uncla DALMORE CAPITAL 3 LP	25,000,000	0.97	24,338,162
UK Uncla EQUITIX FUND 1 LTD P'SHIP	7,500,000	1.72	12,885,077
UK Uncla Equitix Fund IV Ltd P'ship	25,000,000	1.28	31,911,793
UK Uncla FIRST STATE EDIF II	20,000,000	1.00	17,960,433
UK Uncla IMPAX NEW ENERGY INVESTORS II UNITS	10,000,000	0.01	131,074
UK Uncla JP Morgan Infrastructure Investment Fund UK L	110,000,000	0.96	80,599,015
UK Uncla MEIF 5 Co-Invest LP	12,600,000	0.58	6,537,858
UK Uncla MEIF 6 Co-Invest LP	28,000,000	0.00	252
UK Uncla Macquarie European Infrastructure Fund 5 LP	14,400,000	1.05	13,604,280
UK Uncla Macquarie European Infrastructure Fund 6 SCSI	56,000,000	0.32	16,097,654
UK Uncla Macquarie Green Infrastructure Fund (Euro)	59,000,000	0.04	2,060,607
UK Uncla PIP Multi Strategy Infrastructure LP	25,000,000	0.83	20,707,590
UK Uncla SL CAPITAL INFRASTRUCTURE 1LP	15,000,000	1.14	17,107,660
UK Uncla SL Capital Infratructure II SCSP	25,000,000	0.78	17,451,331
UK Infrastructure Total			**261,392,785**
INFRASTRUCTURE TOTAL			**343,932,280**
ALTERNATIVES TOTAL			**504,872,880**

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

	Number held	Mkt Price in local currenc (Clean) use Calc & IL Valuation	Mkt Price in local currenc) (Dirty) use for Non IL Valuation	Mkt Price pence GBP	Total £ GBP
UK GILTS					
TSY 3.75% 7/9/2020	10,322,000	100.35	101.87	101.87	10,515,263
TSY 1.75% 7/9/2022	13,490,000	103.84	104.54	104.54	14,103,061
TSY 4% 7/3/2022	10,995,000	106.46	108.08	108.08	11,883,568
TSY 2.25% 7/9/2023	15,400,000	107.30	108.21	108.21	16,663,879
TSY 5% 7/3/2025	5,500,000	123.61	125.63	125.63	6,909,895
TSY 2% 7/9/2025	7,000,000	110.96	111.77	111.77	7,824,095
TSY 1.5% 7/22/2026	5,650,000	109.59	109.64	109.64	6,194,768
TSY 4.25% 7/12/2027	18,000,000	131.54	132.20	132.20	23,795,619
TSY 4.75% 7/12/2030	13,162,000	147.78	148.52	148.52	19,548,565
TSY 4.25% 7/6/2032	12,370,000	147.00	147.66	147.66	18,266,023
TSY 4.5% 7/9/2034	16,373,000	157.19	159.01	159.01	26,035,200
TSY 4.25% 7/3/2036	11,400,000	157.62	159.34	159.34	18,164,850
TSY 1.75% 7/9/2037	11,800,000	120.25	120.96	120.96	14,272,874
TSY 4.75% 7/12/2038	7,934,000	174.61	175.35	175.35	13,912,329
TSY 4.25% 7/9/2039	4,050,000	167.58	169.30	169.30	6,856,641
TSY 3.25% 1/22/2044	8,000,000	157.19	157.30	157.30	12,583,838
TSY 4.25% 7/12/2046	3,900,000	187.66	188.32	188.32	7,344,476
001 UKGB Total					**234,874,944**
US GOVERNMENT BONDS					
T 2.75% 31/8/2023	26,191,000	108.05	109.22	83.47	21,860,650
T 2.25% 15/11/2024	21,000,000	108.84	109.33	83.55	17,545,959
T 2.75% 15/11/2042	7,500,000	133.16	133.75	102.21	7,666,115
004 USGB Total					**47,072,724.09**
NON GOVERNMENT BONDS					
LGPS Central Global Active Corp B	3,223,092	101.71	101.71	101.71	327,820,696
Non Govt Bonds Total					**327,820,696**
MULTI ASSET CREDIT					
AMP Capital Infrastructure Debt Fu	17,000,000	0.88	0.88	0.88	13,498,672
Barings Global Private Loan Fund	40,000,000	0.52	0.52	0.52	20,666,142
Barings Global Private Loan Fund 2	40,000,000	0.90	0.90	0.90	36,082,910
Barings Global Private Loan Fund 3	50,000,000	0.36	0.36	0.36	17,931,521
CQS Credit Multi Asset Fund Class	105,489	1,018.17	1,018.17	1,018.17	107,406,165
CVC Credit PARTNERS European I	76,000,000	0.21	0.21	0.21	14,327,593
Janus Henderson Multi Asset Credi	98,434,501	1.07	1.07	1.07	105,602,797
Multi Asset Credit Total					**315,515,800**
UK INDEX LINKED					
TREAS 4.125% IL STK 22/7/2030	6,510,000	389.68	389.97	389.97	25,387,107
TREAS 2% IL STK 26/1/2035	8,000,000	308.61	308.68	308.68	24,694,655
002 UKGIL Total					**50,081,762**

INDEX LINKED (3 monthers)

	Number held	Clean Price	Index Ratio	Gross	Accrued Interest	Total
UK INDEX LINKED (3monthers)						
TREAS 0.125% IL STK 22/3/2024	9,230,000	111.0870	1.205480	12,360,184.37	4,201.15	12,364,386
TREAS 1.25% IL STK 22/11/2027	7,400,000	134.8950	1.505830	15,031,541.40	18,349.18	15,049,891
TREAS 0.125% IL STK 22/3/2029	5,325,000	130.5880	1.230870	8,559,237.35	2,423.74	8,561,661
TREAS 1.25% IL STK 22/11/2032	2,777,000	162.5100	1.345870	6,073,780.36	6,885.90	6,080,666
TREAS 0.75% IL STK 22/3/2034	11,465,000	159.7570	1.258380	23,048,664.32	31,310.67	23,079,975
TREAS 1.125% IL STK 22/11/2037	5,580,000	185.9150	1.444960	14,990,097.40	12,452.65	15,002,550
TREAS 0.625% IL STK 22/3/2040	5,600,000	181.7550	1.349660	13,737,217.38	12,744.57	13,749,962
TREAS 0.625% IL STK 22/11/2042	5,950,000	193.4230	1.375440	15,829,483.00	7,376.87	15,836,860
TREAS 0.125% IL STK 22/3/2044	11,470,000	181.6250	1.205470	25,112,818.16	5,220.72	25,118,039
TREAS 0.125% IL STK 22/3/2046	8,730,000	188.4990	1.133610	18,654,643.88	3,973.57	18,658,617
TREAS 0.75% IL STK 22/11/2047	6,500,000	220.4130	1.406540	20,151,280.57	9,670.52	20,160,951
TREAS 0.125% IL STK 10/08/2048	5,300,000	198.0650	1.063460	11,163,612.86	-127.40	11,163,485
TREAS 0.5% IL STK 22/3/2050	5,000,000	220.2210	1.369410	15,078,641.98	9,103.26	15,087,745
UK INDEX LINKED (3monthers) TOTAL						**199,914,788**

US INDEX LINKED	Number held	Clean Price	Index Ratio	Gross $	Accrued Interest $	Total $	Total £
TII0.125% 15/1/2023	7,000,000	103.125000	1.111180	8,021,330.63	451.77	8,021,782	6,130,246
TII3.625% 15/4/2028	4,045,000	137.289063	1.585780	8,806,379.59	44,069.50	8,850,449	6,763,513
TII1.750% 15/1/2028	5,550,000	121.835938	1.224290	8,278,519.86	5,014.61	8,283,534	6,330,277
TII2.5% 15/1/2029	7,000,000	131.078125	1.194620	10,961,198.48	9,035.33	10,970,234	8,383,453
TII2.125% 15/2/2040	4,095,000	155.460938	1.186660	7,554,426.36	40,640.63	7,595,067	5,804,150

DERBYSHIRE PENSION FUND
JULY 2020 PORTFOLIO VALUATION - BID

	Number held	Mkt Price in local currency (Clean) use	Mkt Price in local currency (Dirty)	Mkt Price pence GBP			Total £ GBP
TII0.75% 15/2/2042	20,300,000	128.015625	1.135090	29,497,778.92	71,105.77	29,568,885	22,596,542
TII0.625% 15/2/2043	10,000,000	125.671875	1.115580	14,019,703.03	29,189.56	14,048,893	10,736,164
0045 USGB IL Total							**66,744,345**

TOTAL BONDS	1,242,025,060
Index linked-total	**316,740,895**
Conventional-total	**281,947,668**
Non gov-total	**643,336,497**

DERBYSHIRE PENSION FUND

JULY 2020 PORTFOLIO VALUATION - BID

					Valuation to 30/6/20
Real Property					**£**
Property		Southampton Property			7,100,000
Property		Retail Unit Tamworth			8,250,000
Property		15-17 Jockeys Field London			11,900,000
Property		D'Arblay House, London			15,750,000
Property		Bristol Odeon Development			5,000,000
Property		Quintins Centre, Hailsham			6,300,000
Property		Caledonia House, London			24,400,000
Property		Chelsea Fields Ind Est, London			13,900,000
Property		Planet Centre, Feltham			14,200,000
Property		Hill St, Mayfair			15,550,000
Property		Birmingham - Travelodge developm't			13,700,000
Property		Saxmundham, Tesco developm't			9,650,000
Property		Roundhay Road, Leeds			6,150,000
Property		Premier Inn, Rubery, Birmingham			5,950,000
Property		South Normanton Warehouse, Alfreton			15,800,000
Property		Loddon Centre, Basingstoke			13,900,000
Property		Parkway, Bury St Edmunds			9,300,000
Property		Waitrose, York			13,550,000
Property		Link 95, Haywood Manchester			10,350,000
Property		Car Park, Welford Rd Leicester			12,900,000
Total Real Property		*TOTAL BOOK COST at 31,*			**233,600,000**
Property Managed Funds			**Number held**	**Mkt price**	
Property	**Pence**	Assura PLC	6,000,000	78.9000	4,734,000
Property	**GBP**	Aviva Pooled Property Fund - class	629,696	15.9148	10,021,488
Property	**GBP**	Aviva Pooled Property Fund - class	509,387	16.0370	8,169,058
Property	**GBP**	Bridges Property Alternatives Func	10,000,000	0.6433	6,432,755
Property	**GBP**	Bridges Property Alternatives Func	10,000,000	0.1909	1,909,326
Property	**EUR**	Fidelity Eurozone Select Real Esta	4,486	5853.0180	23,637,491
Property	**GBP**	Hearthstone Residential Fund 1 LF	25,000,000	0.8067	20,168,633
Property	**GBP**	Igloo Regeneration P'ship Property	4,644,493	0.0323	150,082
Property	**EUR**	Invesco Real Estate-European Fur	44,569	112.6170	4,518,242
Property	**Pence**	Target Healthcare REIT Ltd	4,085,000	111.2000	4,542,520
Property	**GBP**	M&G PP UK Property Fund (Inc)	27,124	685.8700	18,603,538
Property	**EUR**	M&G European Property Fund SIC	25,000,000	1.0214	22,987,045
Property	**GBP**	Threadneedle Pensions Property F	1,647,730	5.9491	9,802,513
Property	**Pence**	Tritax Big Box Indirect Pooled Fun	10,000,000	151.3000	15,130,000
Property	**GBP**	Unite UK Student Accommodation	15,584,567	1.3590	21,179,427
Total Property Funds					**171,986,118**

Regulatory Capital	LGPS Central	**0.00**		2,000,000
Cash	*Updated to 30 July 2020*	**Mellon USD**	**Exch rate**	
Cash	Northern Trust	*UK*		17,864,445
Cash		*Wellington*		2,535,988
Cash	Cash - Lloyds bank Superfund	*20553355*		3,988,000
	Adjustments for timing differences	*RBC Purch trade 30.7.20, Settle 4.8.20*		-10,000,000
		Sales-various trades 29 & 31 July settling in Aug		2,466,647
Cash	Cash Temporary Loans	183,500,000		
	Santander 95 Day Notice	10,000,000		
	Santander 180 Day Notice	10,000,000		
	Aberdeen Standard Life	30,000,000		
	Federated Prime Rate	30,000,000		
	Deutsche Global MMF	30,000,000		
	Insight MMF	30,000,000		
	Certs of Deposit	0		
	Treasury Bills	0		323,500,000
Total Cash			Total Cash	**340,355,080**

Agenda Item No. 4 (b)

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

9 September 2020

Report of the Director of Finance & ICT

STEWARDSHIP REPORT

1 Purpose of the Report

To provide the Pensions & Investments Committee with an overview of the stewardship activity carried out by Derbyshire Pension Fund's (the Fund) external investment managers in the quarter ended 30 June 2020.

2 Information and Analysis

This report attaches the following two reports to ensure that the Pensions & Investments Committee is aware of the engagement activity being carried out by LGIM and by LGPS Central Limited (the Fund's pooling company):

- Q2 2020 Legal & General Investment Management (LGIM) ESG Impact Report (Appendix 1)
- Q1 2020/21 LGPS Central Limited Quarterly Stewardship Report (Appendix 2).

LGIM manages around £1bn of assets on behalf of the Fund through passive products covering: UK Equities; Japanese Equities; and Emerging Market Equities. It is expected that LGPS Central Limited will manage a growing proportion of the Fund's assets going forward as part of the LGPS pooling project.

These two reports provide an overview of the investment managers' current key stewardship themes and voting and engagement activity over the last quarter.

3 Other Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal and human rights, human resources, equality and diversity, health, environmental, transport, property and prevention of crime and disorder considerations.

4 Officer's Recommendation

That Committee notes the stewardship activity of LGIM & LGPS Central Limited.

Peter Handford

Director of Finance & ICT

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Not to be distributed to retail clients.**

ESG Impact Report

Q2 2020

Active ownership means using our scale and influence to bring about real, positive change to create sustainable investor value.

Legal & General
INVESTMENT MANAGEMENT

Our mission

To use our influence to ensure that:

1

Companies integrate environmental, social and governance (ESG) factors into their culture and everyday thinking.

2

Markets and regulators create an environment in which good management of ESG factors is valued and supported.

Our focus

To use our influence to ensure that:

Holding boards to account

To be successful, companies need to have people at the helm who are well equipped to create resilient long-term growth. By voting and engaging directly with companies, we encourage management to control risks and benefit from emerging opportunities.

We seek to protect and enhance our clients' assets by engaging with companies and holding management to account for their decisions. Voting is an important tool in this process, and one which we use extensively.

Creating sustainable value

We believe it is in the interest of all stakeholders for companies to build sustainable business models that are also beneficial to society. We work to prevent market behaviour that destroys long-term value creation.

LGIM wants to safeguard and grow our clients' assets by ensuring that companies are well positioned for sustainable growth. Our investment process includes an assessment of how well companies incorporate relevant ESG factors into their everyday thinking.

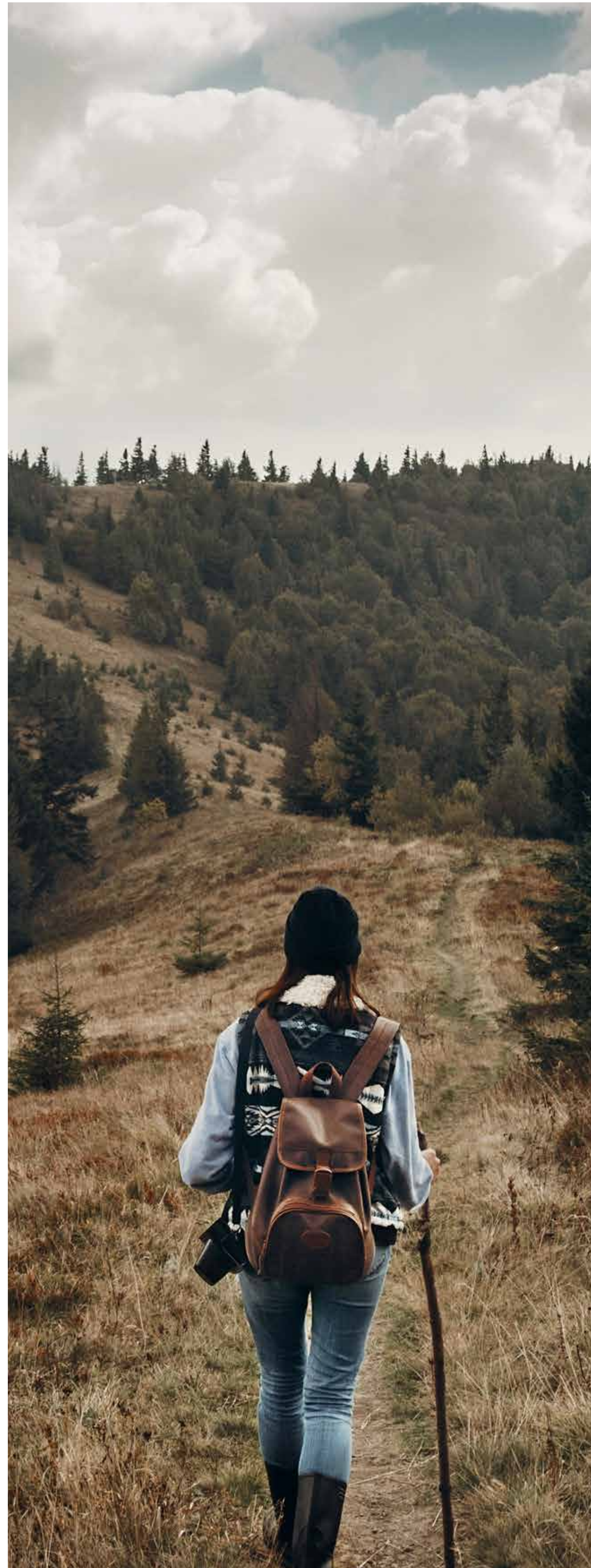
We engage directly and collaboratively with companies to highlight key challenges and opportunities, and to support strategies that can seek to deliver long-term success.

Promoting market resilience

As a long-term investor for our clients, it is essential that markets are able to generate sustainable value. In doing so, we believe companies should become more resilient to change and therefore aim to benefit the whole market.

We aim to use our scale and influence to ensure that issues impacting the value of our clients' investments are recognised and appropriately managed. This includes working with key decision-makers such as governments and regulators, and collaborating with asset owners to bring about positive change.

Action and impact



LGIM's contribution to the PRI's response to COVID-19

In May, LGIM's Investment Stewardship team was invited by the United Nations-supported Principles of Responsible Investment (PRI) investor network to participate in a webinar entitled 'COVID-19 and ESG in the 2020 AGM Season'.

The webinar was organised on the back of collaborative work undertaken between the PRI, the Business & Human Rights Resource Centre, California State Teachers' Retirement System (CalSTRS) and Algemene Pensioen Groep (APG), to propose questions that investors could put forward to their investee holdings during this very particular annual general meeting (AGM) season. The focus was mainly on social aspects involving companies during the pandemic and their reactions to it. The Investment Stewardship team was asked to provide a corporate governance perspective to the webinar, which attracted a significant amount of participants, over 1,000 views (529 live attendees plus 492 views of the recording of the webinar).

In the webinar we explained our approach during this AGM season, highlighting that we have not modified our voting policies, but that on the contrary, we underscored that it is exactly in a time of crisis when the core tenets of corporate governance come into play and matter the most. We gave the example of overboarding, where non-executive directors have multiple positions at different boards, and the inability in times of crisis for directors to be present, up-to-speed and able to attend and contribute to multiple meetings held by multiple companies within a brief period of time.

Following on the webinar we contributed to the guidance document '2020 AGM Season, Investor Questions in Light of COVID-19', which covers three broad themes: business continuity; employee health and wellbeing; and alignment with long-term value creation.

A question of rank

At the beginning of the year, LGIM was rated highly among the world's 75 largest asset managers for our approach to responsible investment, according to an independent report by the non-governmental organisation, ShareAction.

Asset Manager	Overall Responsible Investment Rating	Ranking By Theme (of 75)		
		Climate Change	Bio-diversity	Human Rights
Robeco	A	2	1	1
BNP Paribas Asset Management	A	3	2	4
Legal & General Investment Management	A	1	4	5
APG Asset Management	A	16	14	2
Aviva Investors	A	10	13	11

Adapted from ShareAction, August 2020:
https://shareaction.org/research-resources/point-of-no-returns/

This was followed by three thematic reports which explored in more depth the actions and policies of asset managers with regards to human rights, biodiversity and climate change. LGIM continued to score very favourably throughout the series of reports, including being ranked top for our climate change strategy.

We now understand more about areas for improvement; for example, we are currently developing an engagement strategy around biodiversity.

In late June, we joined forces with other investors, writing to the Brazilian government to call for a curb on deforestation.

Our campaign was covered widely in the media – including by prestigious outlets such as *Reuters*, the *New York Times* and *The Financial Times*.

Blogs

Keeping clients informed about ESG matters is important to us, so we often address key topics – in the second quarter members of the team shared their thoughts in these blogs:

- **Methane: Carbon's shadier sibling** - Why tacking methane emissions must be a priority for companies and policymakers
- **Time to be bold and green** - Policymakers must put the climate emergency at the heart of their COVID-19 stimulus packages
- **Strengthening the foundations for sustainable investment** - A defining moment for non-financial disclosures
- **Divestment damages: Quantifying the impact of ESG exclusions** - The perils of ESG exclusions are often exaggerated – but so are their benefits
- **We are not alone: Biodiversity is key to a sustainable future** - Biodiversity matters for many reasons; we believe investors should take note
- **Japan's AGM season: A year like no other** - COVID-19 has only amplified the importance of issues related to ESG and resilience, so we will remain committed to our stewardship policies in Japan
- **Japan's AGM season: Looking to next year and beyond** - We will support reforms that ensure AGMs in Japan deliver accountability more inclusively

Active ownership report coverage

Our ninth Active Ownership report was published in April and provides an overview of the important work our team carried out on behalf of our clients in 2019. Within three days of being published, the report had received coverage in over 60 national and international news sources.

Notably, the Financial Times led with the importance of stakeholder capitalism in light of the COVID-19 crisis, referencing the team's letter to businesses in March urging caution on sensitive issues around capital allocation and executive pay.

Finding the greenest generation

In October 2019, LGIM's defined contribution pensions business conducted a survey of just under 1,000 respondents across three generations: Baby Boomers, Generation X and Millennials. All our respondents had a private-sector DC pension (not necessarily managed by LGIM). We sought to understand if their attitudes to key ESG issues were shaped by generation and gender, and how savers wanted their preferences integrated into their pensions.

Some views translated across generations, for example, the idea that ESG information can improve engagement with pension savings. There were also stark differences. 'Boomers' were more than twice as likely as Millennials to prioritise investment performance over climate-change considerations, and 45% of Millennials would divest from fossil fuels irrespective of the performance impact.

This is not to suggest that those from earlier generations did not care about ESG factors, but their priorities were different, because their experience as a generation was different. For example, nearly 75% of all the women surveyed over the age of 39 would divest from companies in their pension with a poor governance and pay record. This is a group of people who are likely to have been affected by the gender pay gap during their own working lives, and is a good example of when gender and generational experience intersect to shape the preferences of our respondents.

Notably, more than half of those surveyed across all generations said they would prefer their asset manager to engage with poor-performing companies in the first instance, before divesting, with over 55% expecting their companies to be less invested in the laggards by default. In this vein, LGIM supports the newly-launched Make My Money Matter campaign, acknowledging that if you have a pension, you have positive power.

This supports our view that the industry needs to focus on creating transparent communications on the ESG issues which resonate with members, in order to engage them.

From 'material' to 'significant' votes: LGIM's commitment to vote transparency

As a long-term and engaged investor, LGIM takes our responsibility to exercise the voting rights of our clients' assets seriously. We direct the vote of a considerable proportion of a company's shares by exercising the shareholder rights of a significant number of our clients with one consistent voice across all of our active and index funds. This improves the effectiveness of voting as a means to support our engagement activities and bringing about change in the market as a whole.

As regulations on vote reporting have recently evolved, with the introduction of the concept of the 'significant vote' by the EU Shareholder Rights Directive II, LGIM wants to ensure we continue to help our clients in fulfilling their reporting obligations. We also believe that transparency with the public over our voting activity is critical in order for clients and interested parties to hold us to account.

The full report and podcast are available here: https://update.lgim.com/dc-esg

For many years, LGIM has regularly produced case studies and/or summaries of LGIM's vote positions for what we deemed were 'material votes'. We are evolving our approach in line with the new regulation and are committed to providing our clients access to 'significant vote' information.

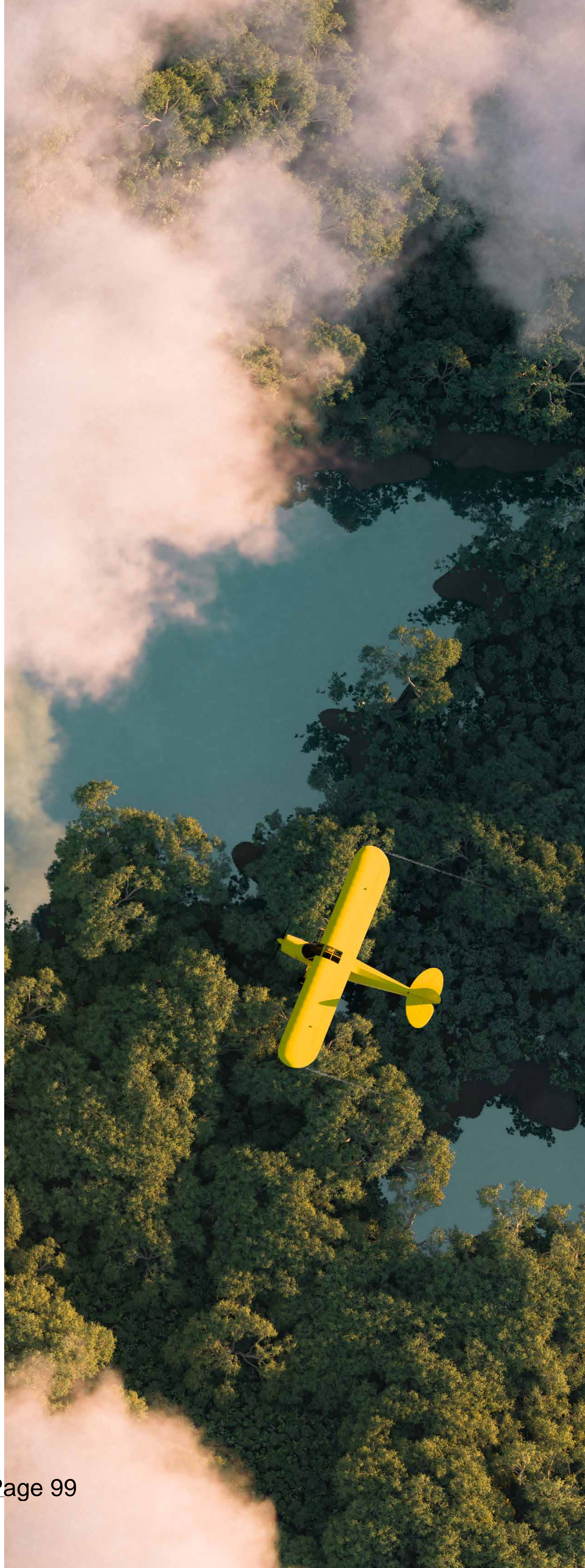
In determining significant votes, LGIM's Investment Stewardship team takes into account the criteria provided by the Pensions & Lifetime Savings Association consultation (PLSA). This includes, but is not limited to:

- A high profile vote which has a degree of controversy such that there is high client and/or public scrutiny
- Significant client interest for a vote: directly communicated by clients to the Investment Stewardship team at LGIM's annual stakeholder roundtable event, or where we note a significant increase in requests from clients on a particular vote
- A sanction vote as a result of a direct or collaborative engagement
- A vote linked to an LGIM engagement campaign, in line with the Investment Stewardship team's five-year ESG priority engagement themes

We will provide information on significant votes in the format of detailed case studies in our quarterly ESG Impact Report and Active Ownership publications.

If you require information on specific votes, please note that we publicly disclose our votes for the major markets on our website. The reports are published at the end of each month and can be used by clients for their external reporting requirements. The voting disclosures can be found by selecting 'Voting Report' on the following page:

https://www.lgim.com/uk/en/capabilities/corporate-governance/policies-and-voting-disclosures-uk-en/



The pandemic's impact on UK voting season

Companies continue to face challenges posed by the COVID-19 pandemic and social distancing rules, impacting this voting season.

The companies which held their annual general meeting (AGM) in April and May were less impacted because their accounts had already been audited and signed off. However, those companies with AGMs set to happen later into the voting season were affected by delays.

The Financial Conduct Authority (FCA) allowed companies an additional two months to publish audited financial reports. Therefore, in total they will have up to six months from their financial year-end to publish audited statements of accounts. The Institute of Chartered Secretaries and Administrators (ICSA) and the Financial Reporting Council (FRC) provided companies with guidance on options for companies to consider in relation to holding their AGM which included postponement of AGMs and holding hybrid AGMs.

LGIM wrote to the chairs of the FTSE 350 companies, lending our support to the actions they must take to safeguard the future of the company and its employees. We suggested that companies should consider holding a separate meeting later in the year to allow shareholders the opportunity to question the board if there was no process to enable this at their AGM.

During the first half of the year, approximately 45 companies elected to postpone their AGM. This number may increase in the second half as more companies will have been impacted by delays to audits.

Executives remain in the hot seat

As in most years, executive pay continued to be the main reason for companies to experience high amounts of dissent from shareholders. Individual directors were also the target of shareholder dissatisfaction. For WM Morrison (34.8% votes against) and Informa (35.1% votes against) this was primarily due to the issue of pension payments to executive directors. LGIM supported Informa's pay because they engaged with us to inform us that they would be conducting a review of remuneration later this year, once a new chair had been appointed. The only company to lose a vote on its remuneration report was Tesco plc (67.3% vote against) not because of pensions, but because it removed Ocado from its relative total shareholder return peer group. Both Intertek (42.9% votes against) and Pendragon (41.3% votes against) came very close to losing the vote on their remuneration policy.

Until the end of May, 29 directors had received significant votes (>20%) against their re-election. Ten of these directors received in excess of 30% votes against their re-election. Guy Wollaert at PureCircle nearly lost his seat with 47.5% votes against his re-election.[1]

A declaration of independence

During Q2 2020, which was the busiest quarter for UK AGMs, LGIM voted against at least one resolution at 56% of shareholder meetings held (AGMs and extraordinary general meetings). LGIM voted against 153 directors during the quarter, with the largest number of votes against being triggered due to a lack of independence and/or non-independent directors serving on a board committee reserved for independent directors, as set out in the UK Code of Corporate Governance.

The second biggest cause for concern was over-boarding. LGIM expects non-executive directors not to serve on more than five boards (with a chairman's role counting as two board roles).

The next largest cause of votes against the management was on executive remuneration, where we opposed 28% of remuneration-related votes. We voted against the approval of 76 remuneration policies. The two main triggers were increases to the quantum of executive compensation, following proposals to increase their bonus potential and companies failing to meet our policy and that of the Investment Association on post-exit shareholding requirements, which is the shareholding we

1. Company voting data provided by each individual company.

The full report and podcast are available here: https://update.lgim.com/dc-esg

expect a director to maintain after they have departed from the company. As part of our drive to ensure income equality within an organisation, LGIM took a stance to no longer promote increases to short-term variable pay in 2018. We have taken a strong stance on post-exit shareholding requirements to encourage the stewards of the companies that we invest our clients' assets in to focus on building a sustainable long-term business which benefits all stakeholders.

Case study*

Company name: Barclays		
Market cap: £19.42 billion**	Sector: Financial	ESG Score: 58(-)

What is the issue?

At the end of March, Barclays plc published its ESG report and issued a statement, outlining the ambitious target of aligning the entire business to the goals of the Paris Agreement through plans to shrink its carbon footprint to net zero by 2050. LGIM endorsed this proposal, which was voted on by shareholders at the 2020 AGM on 7th May alongside a shareholder resolution on the same topic.

What did LGIM do?

LGIM voted for resolution 29, proposed by Barclays and for resolution 30, proposed by ShareAction.

LGIM has long considered climate change to be a key risk facing financial institutions such as Barclays. For the past two years we have had extensive discussions with the company on its need to have a strategic approach to climate change. An important catalyst to these discussions was the filing of a shareholder resolution by NGO ShareAction and other co-filers in December 2019.

Since the beginning of the year, LGIM has played a role in private discussions with and between the Barclays board, ShareAction, the Investor Forum and other large investors to secure an outcome that the company, investors and the shareholder proponents are able to support.

The resolution proposed by Barclays sets out its long-term plans and has the backing of ShareAction and co-filers. We are particularly grateful to the Investor Forum for the significant role it played in coordinating this outcome.

What was the outcome?

The hard work is just beginning. Our focus will now be to help Barclays on the detail of their plans and targets, more detail of which is to be published this year. We plan to continue to work closely with the Barclays board and management team in the development of their plans and will continue to liaise with ShareAction, Investor Forum, and other large investors, to ensure a consistency of messaging and to continue to drive positive change.

Why is this a significant vote?

Since the beginning of the year there has been significant client interest in our voting intentions and engagement activities in relation to the 2020 Barclays AGM. We thank our clients for their patience and understanding while we undertook sensitive discussions and negotiations in private. We consider the outcome to be extremely positive for all parties: Barclays, ShareAction and long-term asset owners such as our clients.

LGIM's ESG scores

The ESG scores capture minimum standards on environmental, social and governance metrics – as well as companies' overall levels of transparency. Scores shown as at end of March 2020 (compared to end of March 2019). LGIM's scores for over 2000 listed companies, as well as a guide to our methodology can be found at: https://www.lgim.com/uk/en/capabilities/corporategovernance/assessing-companies-esg/

*Case study shown for illustrative purposes only. **Source: Refinitiv as at 12/8/2020.

A tumultuous voting season in continental Europe

The 2020 AGM season in Europe (ex-UK) has not been a quiet one, involving interesting developments, such as activists requesting the removal of an entire board (Lagardère), or an audit scandal in Germany (Wirecard).

Whilst there was criticism that virtual AGMs have limited shareholders' ability to directly challenge boards, it has not stopped LGIM from using its voice under our renewed voting policies, casting one vote against at least 79% of European companies.

Case study*

Company name: Lagardère		
Market Cap: £1.97bn**	Sector: Publishing	ESG Score: 64 (▼3)

What is the issue?	Activist Amber Capital, which owned 16% of the share capital at the time of engagement, proposed 8 new directors to the Supervisory Board (SB) of Lagardère, as well as to remove all the incumbent directors (apart from two 2019 appointments). This was due to the opinion that the company strategy was not creating value for shareholders, that the board members were not sufficiently challenging management on strategic decisions, and for various governance failures. The company continues to have a *commandite* structure; a limited partnership, which means that the managing partner has a tight grip on the company, despite only having 7 % share capital and 11% voting rights.
Why is it an issue?	LGIM engages with companies on their strategies, any lack of challenge to these, and with governance concerns. The company strategy had not been value-enhancing and the governance structure of the company was not allowing the SB to challenge management on this.
What did LGIM do?	Where there is a proxy contest, LGIM engages with both the activist and the company to understand both perspectives. LGIM engaged with both Amber Capital, where we were able to speak to the proposed new SB Chair, and also Lagardère, where we spoke to the incumbent SB Chair. This allowed us to gain direct perspectives from the individual charged with ensuring their board includes the right individuals to challenge management.
What was the outcome?	LGIM voted in favour of five of the Amber-proposed candidates, and voted off six of the incumbent Lagardère SB directors. Even though shareholders did not give majority support to Amber's candidates, some of its proposed candidates received 47% support, a clear indication that many shareholders have concerns with the board. LGIM will continue to engage with the company to understand its future strategy and how it will add value to shareholders over the long term, as well as to keep the structure of SB under review.
Why is this a significant vote?	LGIM noted significant media and public interest on this vote given the proposed revocation of the company's board.

*Case study shown for illustrative purposes only. The above information does not constitute a recommendation to buy or sell any security.
**Source: Refinitiv as at 12/8/2020.

Case study*

Company name: Wirecard		
Market Cap: €201.8m**	**Sector: Technology / Financials**	**ESG Score: 58 (▲2)[2]**

What is the issue?

Early in the research process, our proprietary ESG Active View tool raised red flags about German fin-tech company Wirecard's governance. In particular, the Financial Times had reported suggestions of accounting irregularities at Wirecard.

The underlying logic of the proposed bond deal raised further concerns for our active fixed income team. The company planned to use the proceeds of its bond issue to repay some bank loans. The suggestion that banks wanted this exposure off their balance sheet required additional investigation.

Finally, our active fixed income team noted that Wirecard had just one rating (Baa3 at Moodys). Any issuer with only one rating raises concerns; even more so when that rating is below BBB/Baa2.

What did LGIM do?

LGIM met the company management during a bond road show. A fixed income ESG analyst, a fixed income telecoms, media, and technology analyst and an expert from our Investment Stewardship team worked together to assess the deal, with a focus on corporate governance concerns. The company management's responses to the accounting allegations were considered unsatisfactory, with some of the responses offered by management even more concerning than the allegations themselves.

As a result of this robust research process, none of LGIM's active funds invested in Wirecard.

Given our concerns, LGIM's Investment Stewardship team, at the company's 2019 AGM, cast a vote against the discharge of all individual members of the management and supervisory boards from any and all of their actions during the past fiscal year.

What was the outcome?

The company announced on 25 June 2020 that it filed for insolvency after admitting that the €1.9 billion of cash on its balance sheet did not exist. Its former CEO Markus Braun was arrested on suspicion of false accounting and market manipulation.

Many questions remain including regarding the role of the German regulator BaFin, and the auditors EY. LGIM's Investment Stewardship team will continue to actively engage to seek to lift market standards in Germany.

For more information, our active fixed income team wrote a blog on the topic 'Neunundneunzig red flags: how we avoided Wirecard'.[3]

Why is this a significant vote?

LGIM's vote of no confidence is a rare and significant step for us as part of our vote escalation policy. Given the importance of the scandal, we consider this vote, cast in 2019, to be a significant vote.

*Case study shown for illustrative purposes only. The above information does not constitute a recommendation to buy or sell any security.
**Source: Refinitiv as at 12/8/2020.

2. The LGIM ESG score encompasses a wide range of themes. As a result, no single issue is designed to dominate our scoring framework. Wirecard performed well on some key themes within the LGIM ESG score including shareholder rights, climate and board diversity. During index construction, companies are compared against their sector peers. Although the company received a 58 (slightly positive score), across our ESG Score integrated Future World index range, the company is either flat or marginally underweight.

3. https://www.lgimblog.com/categories/markets-and-economics/fixed-income/neunundneunzig-red-flags-how-we-avoided-wirecard/

Voting season in the US

From tech darling to ESG case study: Spotlight on Amazon*

Amazon has matured from a tech darling to a corporate-governance case study. There was a tremendous focus on May's annual meeting, despite the company's jaw-dropping financial performance and consumers globally flocking to the "everything store" in the midst of a pandemic.

The market attention was significant leading up to the AGM, with:

- 12 shareholder proposals on the table – the largest number of any major US company this proxy season
- Diverse investor coalitions submitting and rallying behind the proposals, including global, different types of investors and first time co-filers/engagers
- Substantial press coverage – with largely negative sentiment related to the company's governance profile and its initial management of COVID-19
- Multiple state treasurers speaking out and even holding an online targeted pre-annual meeting investor forum entitled 'Workplace & Investor Risks in Amazon.com, Inc.'s COVID-19 Response'

Anecdotally, the Stewardship team received more inquires related to Amazon than any other company this season.

No distance from the 'Social' in ESG

In addition to facing a full slate of proxy proposals, in the two months leading up to the annual meeting, Amazon was on the front lines of a pandemic response. The company was already on the back foot owing to the harsh workplace practices alleged by the author of a seminal article in the New York Times published in 2015, which depicted a bruising culture. The news of a string of workers catching COVID-19, the company's response, and subsequent details, have all become major news and an important topic for our engagements leading up to the

*Case study shown for illustrative purposes only.

proxy vote. Our team has had multiple engagements with Amazon over the past 12 months. The topics of our engagements touched most aspects of ESG, with an emphasis on social topics:

- **Governance**: Separation of CEO and board chair roles, plus the desire for directors to participate in engagement meetings
- **Environment**: Details about the data transparency committed to in their 'Climate Pledge'
- **Social**: Establishment of workplace culture, employee health and safety

The allegations from current and former employees are worrying. Amazon employees have consistently reported not feeling safe at work, that paid sick leave is not adequate, and that the company only provides an incentive of $2 per hour to work during the pandemic. Also cited is an ongoing culture of retaliation, censorship, and fear.

We discussed with Amazon the lengths the company is going to in adapting their working environment, with claims of industry-leading safety protocols, increased pay, and adjusted absentee policies. However, some of their responses seemed to have backfired. For example, a policy to inform all workers in a facility if COVID-19 is detected has definitely caused increased media attention.

Targeting our proxy votes

This year was an unusual backdrop in which to cast our proxy votes. Of 12 shareholder proposals, we voted to support 10. We look into the individual merits of each individual proposal, and there are two main areas which drive our decision-making: disclosure to encourage a better understanding of process and performance of material issues (resolutions 5, 6, 7, 8, 10, 13, 15 and 16) and governance structures that benefit long-term shareholders (resolutions 9 and 14).

The detail for each proposal and LGIM's vote as well as the rationale behind the vote and the vote result can be seen on our website in our usual voting reports.

Making Amazon amazing

Despite shareholders not giving majority support to the raft of shareholder proposals, the sheer number and focus on these continues to dominate the landscape for the company. Our engagement with the company continues as we push it to disclose more and to ensure it is adequately managing its broader stakeholders, and most importantly, its human capital.

Voting season in Japan

An unusual year

Given the impact of the COVID-19 pandemic on reporting and audits, Japanese companies that were unable to report audited financial statements by their AGM were given the option of either postponing or adjourning their meeting[4].

For companies experiencing pandemic-imposed audit challenges, our suggestion has been to postpone their AGM and hold a meeting later in the year.

We also called on companies to cooperate to allow auditors to carry out their duties without compromising their quality. In our view, a postponed AGM where investors have access to the audited accounts is a much better option than running the risk of a flawed audit.

While technology is starting to change the traditional physical form of AGMs, many long-standing issues – such as the highly condensed AGM season – will remain after the pandemic. We wrote a blog to share our view on reforms that can be implemented to make AGMs more inclusive.

Bolstering voting policies

For over a decade, we have been a strong advocate for good corporate governance in Japan and globally. Board independence and diversity are examples of matters that are more relevant than ever, as boards strive to navigate these uncertain times and emerge more innovative and resilient than before. We have, for example, voted against the most senior member of the board or the nomination committee chair of Japanese companies when:

- There are no women on the board[5]
- Less than one-third of the board is independent

Some investors have relaxed their return on equity (ROE) expectations this year. LGIM, however, has neither historically nor currently applied a voting policy based on ROE. This is because we believe this metric does not fundamentally address the issues for Japanese boards and their ability to be successful for the long term in this globally challenging environment.

Notable AGMs

We voted in favour of the shareholder proposal put to Mizuho Financial Group that called on the group to align its investments with the goals of the Paris Agreement. Whilst the proposal did not pass, it received support of more than a third of votes, sending a clear message that we believe will not go unnoticed by Mizuho's management and companies across Japan.

We voted against the re-election of senior members of the board at Mitsubishi Electric due to serious concerns related to culture and labour management. We acknowledge that culture is a difficult topic to engage on, and we thank the companies that have been open to discuss the important issue. We look forward to further dialogue where we expect to hear about how companies are using key performance metrics and involving the board to promote a healthy corporate culture.

As a long-term investor, LGIM will continue our engagement with Japanese companies to support them to act on the climate emergency and other key ESG issues.

4. A quarter of companies had announced delays to their preliminary earnings reports which is followed by an external audit. Under the adjournment option, investors would have needed to cast their votes without the opportunity to consult the business report and audited financial statements. The meeting would have been reconvened later in the year as a formality to confirm the audited financial statements, but there will be no voting. We therefore were not in favour of this option.
5. In 2020 this was applicable to the TOPIX 100 but the scope will be expanded over time.

Sustainability engagements

Sustained efforts on sustainability

As the coronavirus crisis shines a spotlight on the importance of resilience and long-term planning, we are continuing our efforts to encourage companies to improve their climate change strategies. With a growing number of industry voices raising the possibility that the pandemic has brought forward peak oil demand[6], we were encouraged by several developments in the energy sector.

After unveiling earlier its target to be a 'net zero emissions' company this year, oil major BP has now revised its long-term price assumptions (now including an ambitious $100/ton carbon price) which will help align capital expenditure with the Paris Agreement on climate. Alignment was one of the key requirements in the successful shareholder proposal that LGIM had co-filed at the company last year; LGIM are one of the investors leading engagements with BP as part of the multi-trillion Climate Action 100+ investor coalition.

European oil majors Royal Dutch Shell, Equinor, Eni and Total have announced net zero emissions targets, which cover not just their operations, but, importantly also the use of their products (by far the largest source of emissions for the industry). Notably, Shell has signalled its intention to gradually no longer serve corporate customers which also do not have net zero targets. As there are important differences between the announced strategies of the majors (whether they imply a peak in oil and gas production and/or growth of renewable energy, whether they rely on carbon capture etc.), we will continue to push companies to harmonise and raise their ambitions. Importantly, we will also continue to work to narrow the ambition gap in the sustainability objectives of energy companies on different sides of the Atlantic, as illustrated by ExxonMobil.

"We listened and we learned. The board supported the resolution and we acted on your advice. I personally continue to value and benefit from our ongoing engagement with Climate Action 100+ and the investors it represents."

Bernard Looney
CEO, BP[7]

One important tool at our disposal is our shareholder vote. In Australia, we supported proposals for Paris-aligned emission targets at oil companies Santos and Woodside Petroleum, which received significant support from around 50% of shareholders.

6. https://www.theguardian.com/business/2020/jun/21/even-oil-giants-now-foresee-end-of-gasoline-age-shell-bp-profitability-pandemic
7. https://www.bp.com/en/global/corporate/news-and-insights/speeches/2020-annual-general-meeting-group-chief-executive.html
8. https://www.ft.com/content/a7084118-b501-49c8-821d-c82668b2709b
9. https://www.lgimblog.com/categories/esg-and-long-term-themes/methane-carbon-s-shadier-sibling/
10. https://www.bbc.co.uk/news/business-52851185

We also supported a similar proposal at mining giant Rio Tinto. The company is currently facing a media backlash following the destruction of an aboriginal heritage site during a mine expansion in Western Australia. We have expressed our disappointment at Rio Tinto's handling of the incident – both publicly, in the press[8], and privately, during a call with the company's chair – and expect Rio to demonstrate accountability and institute changes to prevent recurrences. We have also reaffirmed the importance of land use rights in maintaining the social licence to operate with Rio's peers operating in the region.

Carbon dioxide gathers most of the attention in a climate context, but its lesser-known (and more powerful) greenhouse gas sibling – methane – is rising on the investor agenda. We tackled the issue in a recent blog[9] and in a webinar available to watch here.

We also recommended that the European Commission increase the stringency of its methane regulations, an approach we will also be pursuing with key regulators in the US. Policy advocacy remains another important tool in promoting a sustainable future: over the past few months we have repeatedly lent our voice to calls for governments – from the UK to the EU - to implement measures for a green recovery.[10]

Case study*

Company name: ExxonMobil		
Market Cap: $190.1 billion (USD)**	**Sector: Oil and gas**	**ESG Score: 25 (▼2)**

What is the issue?	The company's refusal to disclose and set targets for its total carbon emissions places it at odds with its peers, and is a source of concern as the energy transition accelerates and uncertainty increases over the long-term prospects of the fossil fuel industry. The company has also resisted efforts from shareholders to appoint an independent chair, which we believe provides better accountability and oversight.
What did LGIM do?	In June 2019, under our annual 'Climate Impact Pledge' ranking of corporate climate leaders and laggards, we announced that we will be removing ExxonMobil from our Future World fund range, and will be voting against the chair of the board. Ahead of the company's annual general meeting in May 2020, we also announced we will be supporting shareholder proposals for an independent chair and a report on the company's political lobbying. Due to recurring shareholder concerns, our voting policy also sanctioned the reappointment of the directors responsible for nominations and remuneration.
What was the outcome?	Our voting intentions were the subject of over 40 articles in major news outlets across the world, including Reuters, Bloomberg, Les Échos and Nikkei, with a number of asset owners in Europe and North America also declaring their intentions to vote against the company. At the AGM, circa 30% of shareholders supported the proposals for independence and lobbying. We believe this sends an important signal, and will continue to engage, both individually and in collaboration with other investors, to push for change at the company.
Why is this a significant vote?	We voted against the chair of the board as part of LGIM's 'Climate Impact Pledge' escalation sanction.

*Case study shown for illustrative purposes only. **Source: Refinitiv as at 12/8/2020.

Public policy update

Over the past quarter LGIM has actively engaged on, and closely following, a wide variety of policy and regulatory developments around the world.

United Kingdom

LGIM has been engaging with government, regulators, indexes and industry associations on various ESG topics. A few examples include:

- How the investment industry can support the governments net zero target by 2050
- Mandatory TCFD reporting across the investment chain
- The development of useable responsible investment frameworks (i.e. the Investment Associations Responsible Investment Framework)
- The possible use of 'sustainable' product labels

LGIM has also been very engaged with the government's response to COVID-19 and has been working closely with the Financial Reporting Council and the Investment Association in this regard. LGIM has been actively calling on the UK government to use this as an opportunity to integrate 'sustainable and green' factors into its economic recovery plans. We have also been working collaboratively with associations and industry to signal how important the UK's response is to achieving net-zero and where the government should focus investment. LGIM is supportive and has been actively engaged on the Pension Scheme Bill and the Department for Work and Pensions (DWP) guidance on 'Aligning your pension scheme with the TCFD recommendations'.

European Union

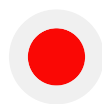
At a European Union level, we have continued to closely follow the important and in-depth technical work of the Commission's action plan on sustainable finance and 'European Green Deal'. Non-financial disclosures are the bedrock of the efficient and sustainable allocation of capital. Given their importance, over the past few months LGIM has focused on the review of the 'Non-Financial Reporting Directive' (NFRD). The review aims to gather feedback as to the quality of disclosures historically, how disclosures can be standardised, the principle of materiality, assurance, digitalisation, location and where efficiencies can be made. At LGIM, as a long-term investor with universal coverage, we have been pushing for relevant, comparable, consistent, and verifiable non-financial information across markets so that we can price environmental, social, and governance (ESG) risks and opportunities accurately. We will closely monitor the review of the NFRD as it progresses through the Commission.

LGIM has also been actively engaging in the COVID-19 response, working with other investors and informal alliances calling for a sustainable economic recovery and stimulus packages that are aligned with the 'Green Deal'.

LGIM has been working with other investors and through the Institutional Investors Group on Climate Change (IIGCC) wrote to EU heads of state and government, highlighting our support for the proposed EU net zero emissions target. In addition, and given the significant of methane emissions contribution to climate change, we wrote to senior officials in the European Commission (through the IIGCC) pressing for a robust methane policy as part of implementing the 'Green Deal'.

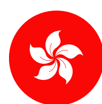
United States

In the United States we have been working together with Legal & General Investment Management America (LGIMA) to engage with the Securities Exchange Commission (SEC) on several important points. One recent example was that LGIM, working as part of a group of institutions, wrote to the SEC to encourage the introduction of new set of rules that would see companies disclosing more consistent and reliable data on 11 areas including management of the response to COVID-19, human capital management process and supply chain risks. There have been some promising signals coming from the SEC Investment Advisory Committee recently, encouraging the SEC to take ESG disclosures seriously or risk the US falling behind. This has been an ongoing issue for us and we will continue to push for over the coming months.



Japan

LGIM has been engaging on seeking an exemption for asset managers to the amendment to the 'Foreign Exchange and Foreign Trade Act'. The amendment requires foreign investors to file a ‘pre-acquisition notification’ to the government if they intend to acquire 1% or more of a listed company in a restricted sector. LGIM has also been engaging on the revisions to the new Japanese Stewardship Code.



Hong Kong

In Hong Kong the LGIM team is engaged with the Securities and Futures Commission on their 'Green & Sustainable Finance' workstream.

Globally

Along with 100 investors and driven by the Investor Alliance for Human Rights, LGIM has written to policymakers around the world calling for the introduction of new requirements that would mandate companies to disclose their human rights due diligence.

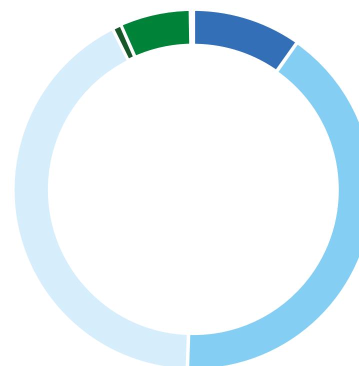
Regional updates

UK - Q2 2020 voting summary

Proposal category	For	Against	Abstain
Antitakeover Related	221	0	0
Capitalisation	1083	37	0
Directors Related	2190	153	1
Remuneration-related	408	159	0
Reorganisation and Mergers	21	3	0
Routine/Business	1177	24	0
Shareholder Proposal - Compensation	1	0	0
Shareholder Proposal - Corporate Governance	0	0	0
Shareholder Proposal - Directors Related	12	0	0
Shareholder Proposal - General Economic Issues	0	0	0
Shareholder Proposal - Health/Environment	1	0	0
Shareholder Proposal - Other/Miscellaneous	0	1	0
Shareholder Proposal - Routine/Business	0	0	0
Shareholder Proposal - Social/Human Rights	0	0	0
Shareholder Proposal - Social	0	0	0
Total	5114	377	1
Total resolutions	5492		
No. AGMs	294		
No. EGMs	33		
No. of companies voted on	312		
No. of companies where voted against management on at least one resolution	174		
% of companies with at least one vote against	56%		

Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds

Votes against management



- Antitakeover Related - 0
- Capitalisation - 37
- Directors Related - 154
- Remuneration-related - 159
- Reorganisation and Mergers - 3
- Routine/Business - 24
- Shareholder Proposal - Compensation - 0
- Shareholder Proposal - Corporate Governance - 0
- Shareholder Proposal - Directors Related - 0
- Shareholder Proposal - General Economic Issues - 0
- Shareholder Proposal - Health/Environment - 0
- Shareholder Proposal - Other/Miscellaneous - 1
- Shareholder Proposal - Routine/Business - 0
- Shareholder Proposal - Social/Human Rights - 0
- Shareholder Proposal - Social - 0

Number of companies voted for/against abstentions

138	174

- No. of companies where supported management
- No. of companies where voted against management (including abstentions)

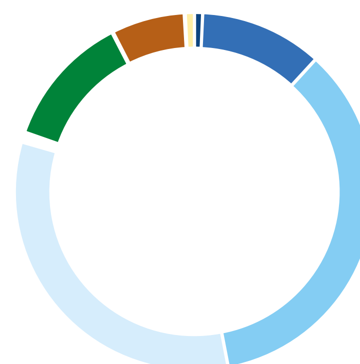
LGIM voted against at least one resolution at 56% of UK companies over the quarter

Europe - Q2 2020 voting summary

Proposal category	For	Against	Abstain
Antitakeover Related	17	8	0
Capitalisation	610	121	0
Directors Related	1840	385	1
Remuneration-related	703	356	0
Reorganisation and Mergers	44	10	0
Routine/Business	1628	129	4
Shareholder Proposal - Compensation	4	1	0
Shareholder Proposal - Corporate Governance	13	0	0
Shareholder Proposal - Directors Related	47	72	0
Shareholder Proposal - General Economic Issues	0	0	0
Shareholder Proposal - Health/Environment	3	1	0
Shareholder Proposal - Other/Miscellaneous	11	9	0
Shareholder Proposal - Routine/Business	7	0	0
Shareholder Proposal - Social/Human Rights	0	0	0
Shareholder Proposal - Social	0	0	0
Total	4927	1092	5
Total resolutions	6024		
No. AGMs	215		
No. EGMs	104		
No. of companies voted on	310		
No. of companies where voted against management on at least one resolution	244		
% of companies with at least one vote against	79%		

Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds

Votes against management



- Antitakeover Related - 8
- Capitalisation - 121
- Directors Related - 386
- Remuneration-related - 356
- Reorganisation and Mergers - 10
- Routine/Business - 132
- Shareholder Proposal - Compensation - 1
- Shareholder Proposal - Corporate Governance - 0
- Shareholder Proposal - Directors Related - 72
- Shareholder Proposal - General Economic Issues - 0
- Shareholder Proposal - Health/Environment - 1
- Shareholder Proposal - Other/Miscellaneous - 9
- Shareholder Proposal - Routine/Business - 0
- Shareholder Proposal - Social/Human Rights - 0
- Shareholder Proposal - Social - 0

Number of companies voted for/against abstentions

66 | 244

- No. of companies where supported management
- No. of companies where voted against management (including abstentions)

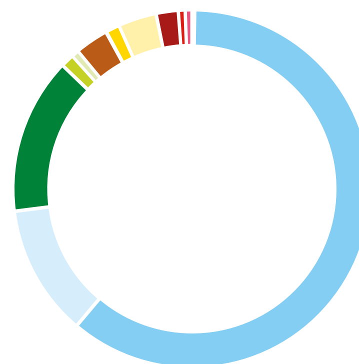
LGIM voted against at least one resolution at 79% of European companies over the quarter

North America - Q2 2020 voting summary

Proposal category	For	Against	Abstain
Antitakeover Related	59	1	0
Capitalisation	54	4	0
Directors Related	3975	1189	0
Remuneration-related	451	232	0
Reorganisation and Mergers	6	0	0
Routine/Business	320	275	1
Shareholder Proposal - Compensation	5	23	0
Shareholder Proposal - Corporate Governance	6	13	0
Shareholder Proposal - Directors Related	68	59	0
Shareholder Proposal - General Economic Issues	0	1	0
Shareholder Proposal - Health/Environment	6	24	0
Shareholder Proposal - Other/Miscellaneous	5	68	0
Shareholder Proposal - Routine/Business	0	39	0
Shareholder Proposal - Social/Human Rights	4	12	0
Shareholder Proposal - Social	8	12	0
Total	4967	1952	1
Total resolutions	6920		
No. AGMs	532		
No. EGMs	3		
No. of companies voted on	534		
No. of companies where voted against management on at least one resolution	516		
% of companies with at least one vote against	97%		

Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds

Votes against management



- Antitakeover Related - 1
- Capitalisation - 4
- Directors Related - 1189
- Remuneration-related - 232
- Reorganisation and Mergers - 0
- Routine/Business - 276
- Shareholder Proposal - Compensation - 23
- Shareholder Proposal - Corporate Governance - 13
- Shareholder Proposal - Directors Related - 59
- Shareholder Proposal - General Economic Issues - 1
- Shareholder Proposal - Health/Environment - 24
- Shareholder Proposal - Other/Miscellaneous - 68
- Shareholder Proposal - Routine/Business - 39
- Shareholder Proposal - Social/Human Rights - 12
- Shareholder Proposal - Social - 12

Number of companies voted for/against abstentions

- No. of companies where supported management
- No. of companies where voted against management (including abstentions)

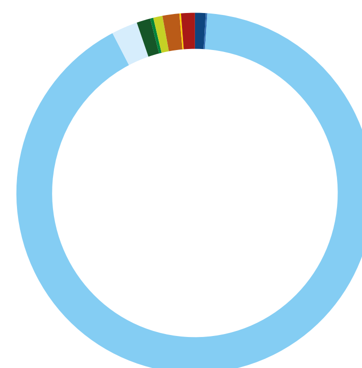
LGIM voted against at least one resolution at 97% of North American companies over the quarter

Japan - Q2 2020 voting summary

Proposal category	For	Against	Abstain
Antitakeover Related	0	7	0
Capitalisation	1	1	0
Directors Related	3744	657	0
Remuneration-related	161	17	0
Reorganisation and Mergers	78	9	0
Routine/Business	281	2	0
Shareholder Proposal - Compensation	1	6	0
Shareholder Proposal - Corporate Governance	2	0	0
Shareholder Proposal - Directors Related	18	11	0
Shareholder Proposal - General Economic Issues	0	0	0
Shareholder Proposal - Health/Environment	42	1	0
Shareholder Proposal - Other/Miscellaneous	0	0	0
Shareholder Proposal - Routine/Business	22	9	0
Shareholder Proposal - Social/Human Rights	0	0	0
Shareholder Proposal - Social	0	0	0
Total	4350	720	0
Total resolutions	5070		
No. AGMs	405		
No. EGMs	2		
No. of companies voted on	406		
No. of companies where voted against management on at least one resolution	290		
% of companies with at least one vote against	71%		

Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds

Votes against management



- Antitakeover Related - 7
- Capitalisation - 1
- Directors Related - 657
- Remuneration-related - 17
- Reorganisation and Mergers - 9
- Routine/Business - 2
- Shareholder Proposal - Compensation - 6
- Shareholder Proposal - Corporate Governance - 0
- Shareholder Proposal - Directors Related - 11
- Shareholder Proposal - General Economic Issues - 0
- Shareholder Proposal - Health/Environment - 1
- Shareholder Proposal - Other/Miscellaneous - 0
- Shareholder Proposal - Routine/Business - 9
- Shareholder Proposal - Social/Human Rights - 0
- Shareholder Proposal - Social - 0

Number of companies voted for/against

- No. of companies where supported management
- No. of companies where voted against management

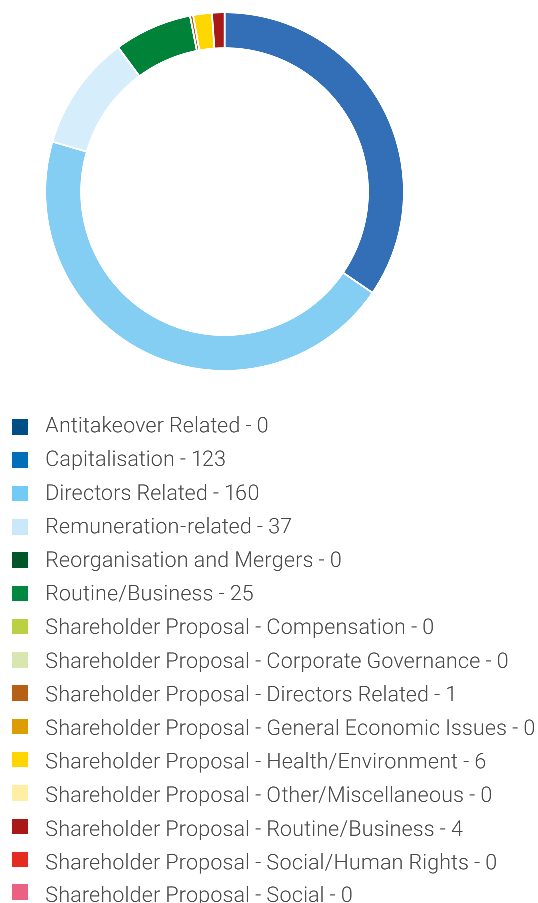
LGIM voted against at least one resolution at 71% of Japanese companies over the quarter

Asia Pacific - Q2 2020 voting summary

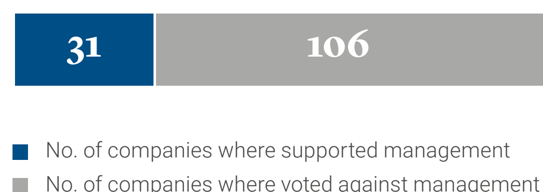
Proposal category	For	Against	Abstain
Antitakeover Related	1	0	0
Capitalisation	163	123	0
Directors Related	388	160	0
Remuneration-related	33	37	0
Reorganisation and Mergers	29	0	0
Routine/Business	300	25	0
Shareholder Proposal - Compensation	0	0	0
Shareholder Proposal - Corporate Governance	0	0	0
Shareholder Proposal - Directors Related	0	1	0
Shareholder Proposal - General Economic Issues	0	0	0
Shareholder Proposal - Health/Environment	0	6	0
Shareholder Proposal - Other/Miscellaneous	0	0	0
Shareholder Proposal - Routine/Business	1	4	0
Shareholder Proposal - Social/Human Rights	0	0	0
Shareholder Proposal - Social	2	0	0
Total	925	348	0
Total resolutions	1273		
No. AGMs	127		
No. EGMs	21		
No. of companies voted on	137		
No. of companies where voted against management on at least one resolution	106		
% of companies with at least one vote against	77%		

Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds

Votes against management



Number of companies voted for/against



- No. of companies where supported management
- No. of companies where voted against management

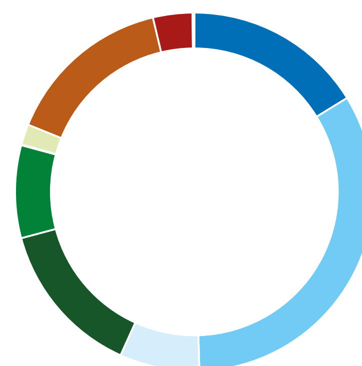
LGIM voted against at least one resolution at 77% of Asia Pacific companies over the quarter

Emerging markets - Q2 2020 voting summary

Proposal category	For	Against	Abstain
Antitakeover Related	5	0	0
Capitalisation	2120	507	0
Directors Related	3600	881	160
Remuneration-related	98	225	0
Reorganisation and Mergers	1598	440	0
Routine/Business	5808	261	0
Shareholder Proposal - Compensation	15	2	0
Shareholder Proposal - Corporate Governance	0	56	2
Shareholder Proposal - Directors Related	93	472	2
Shareholder Proposal - General Economic Issues	0	0	0
Shareholder Proposal - Health/Environment	0	0	0
Shareholder Proposal - Other/Miscellaneous	0	0	0
Shareholder Proposal - Routine/Business	9	111	0
Shareholder Proposal - Social/Human Rights	0	0	0
Shareholder Proposal - Social	2	5	0
Total	13348	2960	164
Total resolutions	16472		
No. AGMs	944		
No. EGMs	258		
No. of companies voted on	975		
No. of companies where voted against management on at least one resolution	650		
% of companies with at least one vote against	67%		

Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds. The abstentions were due to technical reasons which prevented us from voting. Where we have the option to vote, it is our policy to not abstain.

Votes against management



- Antitakeover Related - 0
- Capitalisation - 507
- Directors Related - 1041
- Remuneration-related - 225
- Reorganisation and Mergers - 440
- Routine/Business - 261
- Shareholder Proposal - Compensation - 2
- Shareholder Proposal - Corporate Governance - 58
- Shareholder Proposal - Directors Related - 474
- Shareholder Proposal - General Economic Issues - 0
- Shareholder Proposal - Health/Environment - 0
- Shareholder Proposal - Other/Miscellaneous - 0
- Shareholder Proposal - Routine/Business - 111
- Shareholder Proposal - Social/Human Rights - 0
- Shareholder Proposal - Social - 5

Number of companies voted for/against abstentions

- No. of companies where supported management
- No. of companies where voted against management (including abstentions)

LGIM voted against at least one resolution at 67% of emerging markets companies over the quarter

Global voting summary

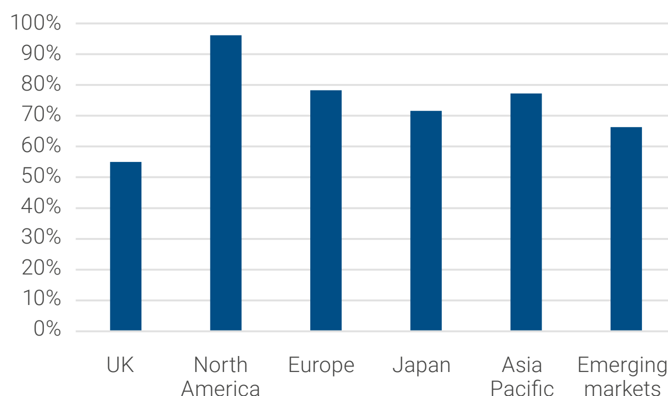
Voting totals

Proposal category	For	Against	Abstain	Total
Antitakeover Related	303	16	0	319
Capitalisation	4031	793	0	4824
Directors Related	15737	3425	162	19324
Remuneration-related	1854	1026	0	2880
Reorganisation and Mergers	1776	462	0	2238
Routine/Business	9514	716	5	10235
Shareholder Proposal - Compensation	26	32	0	58
Shareholder Proposal - Corporate Governance	21	69	2	92
Shareholder Proposal - Directors Related	238	615	2	855
Shareholder Proposal - General Economic Issues	0	1	0	1
Shareholder Proposal - Health/Environment	52	32	0	84
Shareholder Proposal - Other/Miscellaneous	16	78	0	94
Shareholder Proposal - Routine/Business	39	163	0	202
Shareholder Proposal - Social/Human Rights	4	12	0	16
Shareholder Proposal - Social	12	17	0	29
Total	33631	7449	171	41251
No. AGMs	2517			
No. EGMs	421			
No. of companies voted on	2674			
No. of companies where voted against management on at least one resolution	1980			
% of companies with at least one vote against	74%			

Number of companies voted for/against abstentions

- No. of companies where supported management
- No. of companies where voted against management (including abstentions)

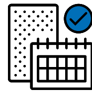
% of companies with at least one vote against (includes abstentions)



Source for all data LGIM. The votes above represent voting instructions for our main FTSE pooled index funds

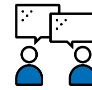
Global engagement summary

Engagement statistics:



83

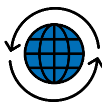
Total number of engagements during the quarter



72

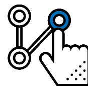
Number of companies engaged

Number of engagements on:



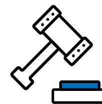
18

Environmental topics



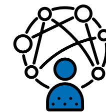
34

Other topics (e.g. financial and strategy



70

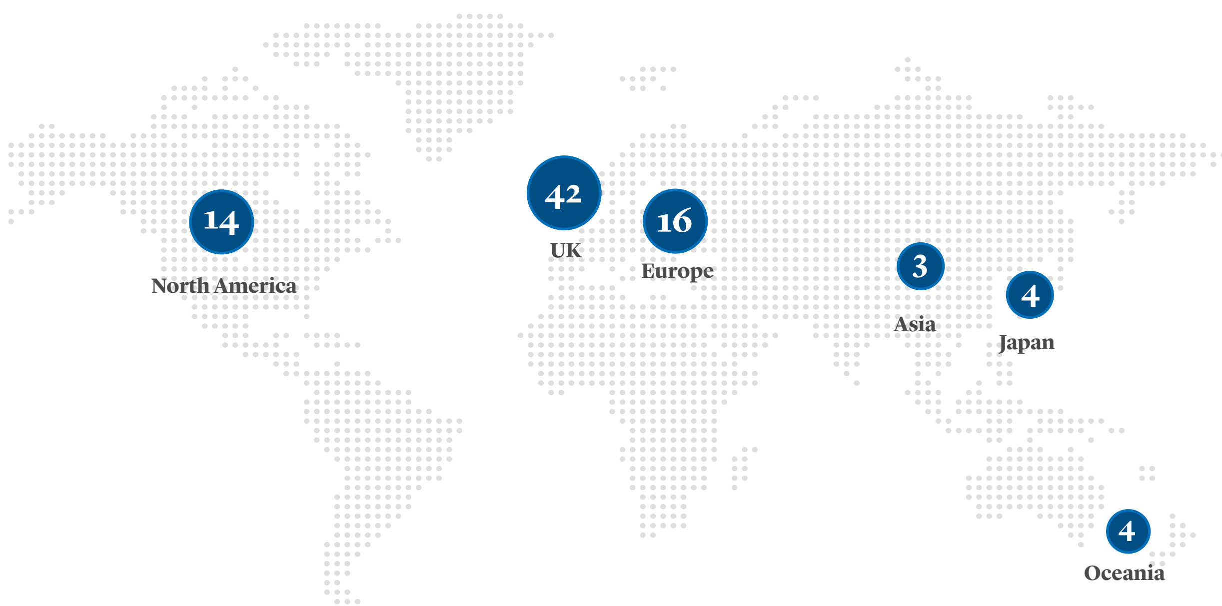
Governance topics



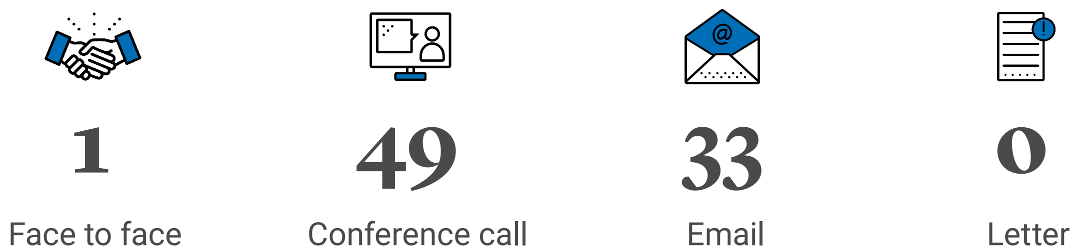
20

Social topics

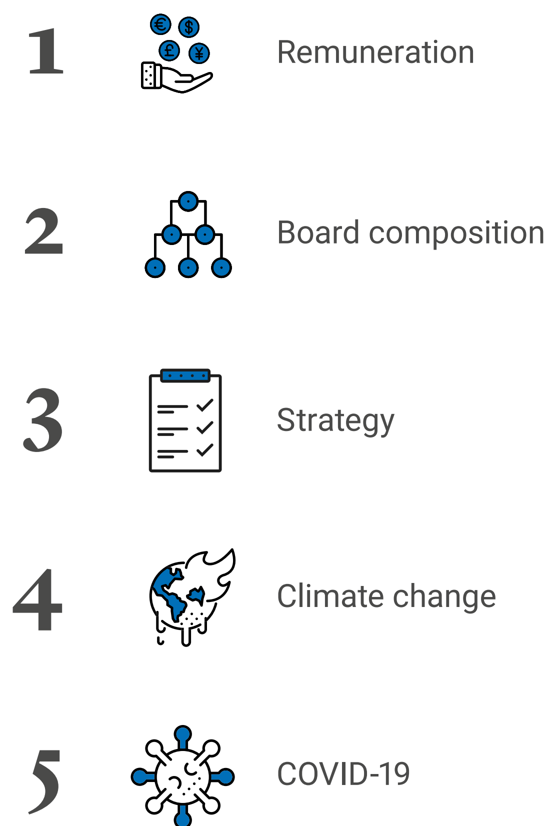
Breakdown of our engagements by market:



Engagement type:

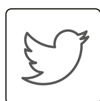


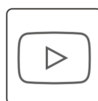
Top five engagement topics:



Contact us

For further information about LGIM, please visit lgim.com or contact your usual LGIM representative





Important notice

Past performance is not a guide to future performance. The value of an investment and any income taken from it is not guaranteed and can go down as well as up, you may not get back the amount you originally invested.

Views expressed are of Legal & General Investment Management Limited as at August 2020.

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Legal & General
INVESTMENT MANAGEMENT

LGPS Central Limited

Quarterly Stewardship Update

FIRST QUARTER, 2020-21 (APRIL - JUNE 2020)

LGPS Central Limited is authorised and regulated by the Financial Conduct Authority

Responsible Investment & Engagement

LGPS Central's approach

LGPS Central's approach to Responsible Investment & Engagement carries two objectives:

OBJECTIVE #1

Support investment objectives

OBJECTIVE #2

Be an exemplar for RI within the financial services industry, promote collaboration, and raise standards across the marketplace

These objectives are met through three pillars:

This update covers LGPS Central's stewardship activity. Our stewardship efforts are supplemented by global engagement and voting services provided by EOS at Federated Hermes (EOS). For more information please refer to LGPS Central's Responsible Investment & Engagement Framework and UK Stewardship Code Compliance Statement.

ADDITIONAL DISCLOSURES

- *Responsible Investment & Engagement Framework*
- *Stewardship Code*
- *Voting Principles*
- *Voting Disclosure*
- *Voting Statistics*

Signatory of: PRI Principles for Responsible Investment

LGPS ADVISORY BOARD CODE OF TRANSPARENCY

01 Engagement and Stewardship Themes

This quarter, the COVID 19 health pandemic has caused radical disruption to markets, companies and investors alike. While the situation is highly disruptive, our view that engagement is a key tool which helps us enhance the long-term value of assets we manage on behalf of Partner Funds has not faltered, rather it has been reinforced.

The health pandemic has also brought home the point, in stark terms, that the "S" in ESG carries material risks. We think it is a fair assumption that companies who actively engage their stakeholders and are attuned to stakeholders' views are more likely to tackle the crisis well and be more resilient to future crisis. In engagement with companies, both directly, in collaboration and through our stewardship provider, we are cognisant of the unprecedented challenges that the health pandemic poses to individual companies and to sectors. At the same time, core expectations that we express for management of risks and opportunities on our four Stewardship Themes (see below) are, in our view, still reasonable and timely to uphold. Companies have largely been receptive and welcoming of engagement, which in some respects has been more efficient when carried out via virtual means. Below, we give examples of ongoing or new engagements which relate to the four Stewardship Themes that have been identified in collaboration with our Partner Funds. The bulk of our engagement effort is centred around these themes which allows us the opportunity to build knowledge, relationships (with peer investors and companies) and to help influence and build best practice industry standards relevant to each theme. We regularly cover issues that fall outside of the stewardship themes, such as fair remuneration, board composition, diversity, and human rights, and have included two examples in this update.

Our Stewardship Themes over the next three-year period are:

- Climate change
- Plastic
- Fair tax payment and tax transparency
- Technology and disruptive industries

This quarter our engagement set[1] comprised 672 companies with 1,578 engagement issues[2]. The high number of engagement issues reflects the fact that April – June is Annual General Meeting (AGM) season for key markets and we or our partners frequently raise multiple issues with companies around the time of an AGM. These issues are not necessarily tied in with ongoing engagements or with specific engagement objectives. Against 481 specific engagement objectives set by our stewardship provider, there was achievement of some or all engagement objectives on 175 occasions. Most engagements were conducted through letter issuance or remote company meetings at Chair, Board or senior management levels.

[1] This includes engagements undertaken directly, in collaboration, and via our contracted stewardship provider.

[2] There can be more than one engagement issue per company, for example board diversity and climate change.

CLIMATE CHANGE

This quarter our climate change engagement set comprised 203 companies with 252 engagements issues[3]. There was engagement activity on 228 engagement issues and achievement of some or all engagement objectives on 89 occasions.

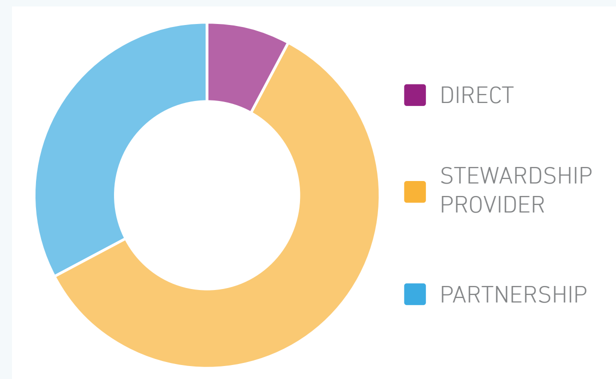
Against the backdrop of the ongoing health pandemic, the climate crisis comes into renewed focus as a "twin crisis" that may unfold over a longer time horizon but is no less urgent to tackle from a long-term economic perspective. As an engager we take a holistic, whole-market outlook whereby we engage fossil fuel companies but also the banks that provide their finance, the auditors who audit their accounts, and all the companies on the demand side. We continue to engage companies on their approach to, and use of, lobbying that shapes climate policies and we engage directly at policy level. Over the last quarter LPGS Central joined more than 100 global investors asking policy makers in the EU to plan and execute recovery from COVID 19 that is aligned with climate commitments, and ultimately with the goals of the Paris Agreement.

Together with Mercy Investment Services (US investor), we co-filed a shareholder proposal asking Honeywell Inc. to provide a report on its direct and indirect lobbying activities and the Board's decision-making process and oversight of lobbying payments. We are concerned that undisclosed indirect lobbying through trade associations poses reputational risks when the lobbying contradicts Honeywell's public positions, resulting in a values misalignment. As an example, Honeywell is committed to "reducing global greenhouse gases" and has signed an agreement to work with the United Nations Environment Programme to combat climate change. This contradicts advocacy by the Chamber of Commerce (Chamber) which Honeywell is a member of. The Chamber has lobbied several regressive positions in its detailed policy engagement, e.g. on the role of coal in the "energy mix" and is one of the most powerful and oppositional trade groups globally in terms of climate policy influence. LGPS Central attended Honeywell's AGM virtually which allowed for limited interaction regarding the shareholder proposal, however the proposal we co-filed received more than 45% support which sends a very clear signal to the Company. We engaged Honeywell following the AGM regarding the vote result and how they can continue to strengthen their lobbying disclosure. The Company is receptive to investor feedback concerning disclosure best practices and we expect these conversations to continue into the next proxy season.

During the last quarter we continued engagement with audit committees of companies with high exposure to climate change risks. The initiative is a satellite to the Climate Action 100+ (CA100+) engagement project and supports the overall goals of CA100+. In November 2019, letters went to three oil and gas majors – BP, Shell and Total – asking for assurances that key financial disclosures to shareholders take due account of all risks, including climate change. If climate risk is not considered, the longevity and value of assets held by these companies may be over-estimated, which could lead to capital being misdirected. The investor group, led by Sarasin & Partners, published a statement on 22 June 2020 welcoming a recent announcement by BP that the company will lower long-term oil and gas price assumptions used in financial statements to reflect a decarbonising world. We commend BP for this move and the statement also positively acknowledges the fact that Shell and Total have similarly lowered their oil and gas price assumptions used in their 2019 audit accounts.

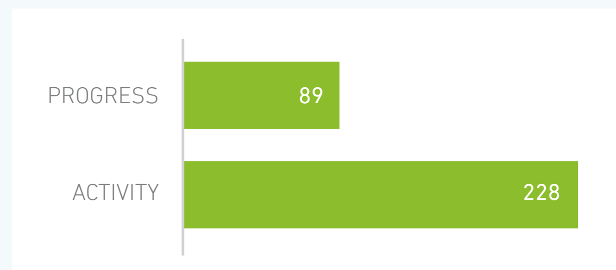
The companies in question are willing to engage on the subject and this positive momentum is now harnessed in order to further the engagement.

ENGAGEMENT VOLUME BY ***TYPE***



- 252 engagements in progress
- Majority of engagements undertaken via CA100+
- Continued focus on companies' financial disclosures taking account of climate risk

ENGAGEMENT VOLUME BY ***OUTCOME***



[3] There can be more than one climate-related engagement issue per company.

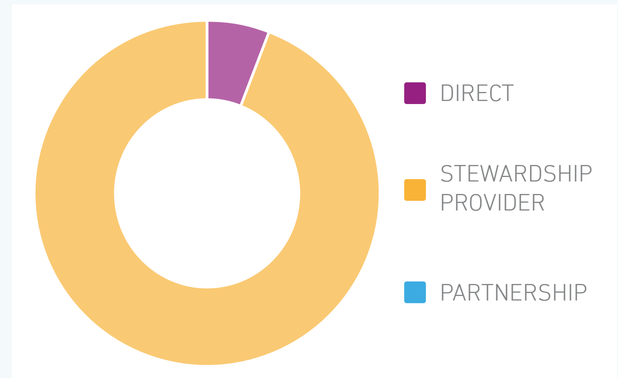
PLASTIC

This quarter our single-use plastics engagement set comprised 15 companies with 17 engagements issues. There was engagement activity on 16 engagements and achievement of some or all engagement objectives on six occasions.

We view development of industry standards as a critical component to efficient engagement with companies and sectors. LGPS Central is collaborating with Investor Forum and peer investors, Marine Scotland, the British Plastics Federation and the British Standards Institute to create the first industry specification to prevent plastic pellet pollution. The new specification will set out measures to prevent plastic pellet leakage, which poses serious threat to the ecosystem and to people's health, and to help companies demonstrate good practice in pellet loss prevention measures across their supply chains. The project was formally launched on World Environment Day (5 June) and will allow companies the ability to demonstrate best practice while giving investors a means for engagement and to hold companies to account on this issue.

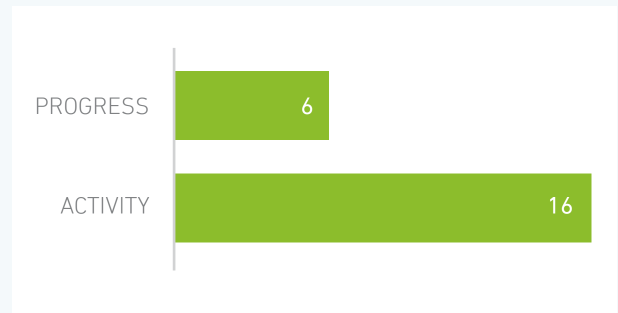
During the last quarter, our stewardship provider EOS at Federated Hermes (EOS) published *Investor Expectations for Global Plastics Challenges*. The expectation is that companies move from treating single-use plastic as an externalised risk, to considering it as a resource requiring responsible management to avoid acute environmental pollution, potential human health impacts and substantial greenhouse gas emissions. EOS is communicating the newly launched expectations to companies in vulnerable sectors, including chemicals, consumer goods and retail sectors. As an example, EOS engaged on our behalf with a US food and retail staples Company that has adopted a time-bound ambitious target for reducing plastic packaging waste, including own-brand and branded product packaging. It is encouraging that the Company applies UK plastics legislation across the group, though progress varies significantly due to local recycling infrastructure. At its 21 distribution centres in North America it has achieved a rate of over 98% recycling. This could likely help the company reach its goal under the UK Plastics Pact of making 100% of plastic packaging reusable, recyclable or compostable by the year 2025. The Company is also engaging suppliers on how products are delivered to them.

*ENGAGEMENT VOLUME BY **TYPE***



- 17 engagements during the quarter
- Launch of project to establish unique industry specification to prevent plastic pellet pollution
- EOS publishes *Investor Expectations for Global Plastics Challenges*

*ENGAGEMENT VOLUME BY **OUTCOME***



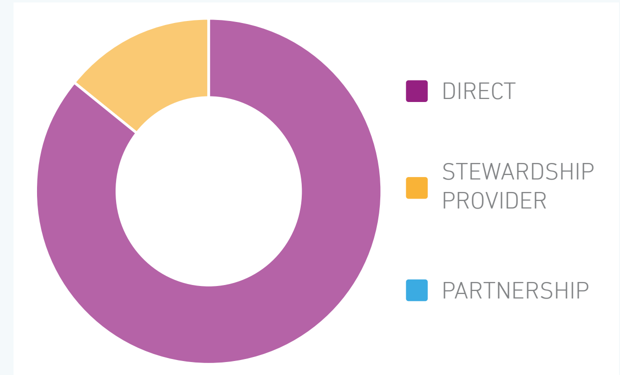
FAIR TAX PAYMENT AND TAX TRANSPARENCY

This quarter our tax transparency engagement set comprised seven companies with seven engagements issues. There was engagement activity on three engagements and achievement of some or all engagement objectives on two occasions.

While many countries are providing various forms of tax relief to businessess during the health pandemic, the investor interest and scrutiny on companies' responsible tax behaviour and their willingness to pay ther fair share of tax will only increase. As a global community, we are poorly prepared to handle any crisis, including health pandemics and the ongoing climate crisis, without funding through tax. We contributed to a consultation on Fair Trade Mark's (FTM) report "The Essential Elements of Global Corporate Standards for Responsible Tax Conduct" which seeks to identify common, international norms for responsible tax conduct.

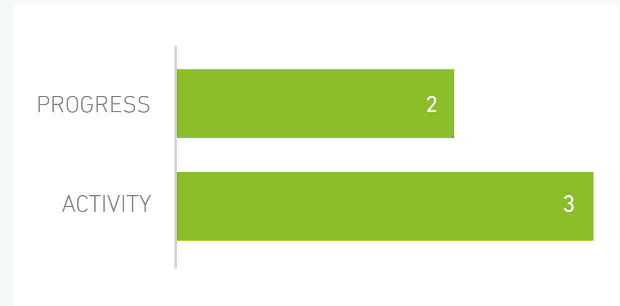
We engaged the CEO and CFO of an international mining Company together with five fellow European investors on responsible tax behaviour. We were assured that the Company values dialogue with all key stakeholders including communities in which it operates mines, host country governments, and investors. The Company engages with host countries to ensure these countries receive a fair share of the economic activities of its operations. In many emerging markets, the Company seeks to achieve a broad economic contribution through taxes paid, through employment of locals in the workforce and by means of specific targeted support such as health and education initiatives. Since the beginning of 2019, the Company has decentralised its management structure and is seeking to simplify the corporate structure. The Company made clear that it is not seeking to shift revenues from higher to lower tax jurisdictions but rather to avoid paying large amounts of taxes to jurisdictions that are not host countries to its mining operations. There is an awareness that many host countries where the company operates need more revenues, hence the company seeks dialogue with host-country stakeholders to explain its various contributions (taxes, royalties etc.). During COVID 19, the company has not used furlough schemes and has not taken advantage of delaying paying taxes or other business support measures as it has, through focussed management, been able to continue its mining activities throughout the pandemic. We were pleased to note that the company, after a recent merger, is now working to set up a tax policy which will be reviewed by the board and is expected to be made available on its website shortly.

ENGAGEMENT VOLUME BY TYPE



- Seven engagements during the quarter
- Collaboration with peer European investors to engage a selection of companies across vulnerable sectors
- Contribution to Fair Tax Mark project seeking to identify common, international norms for responsible tax conduct

ENGAGEMENT VOLUME BY OUTCOME

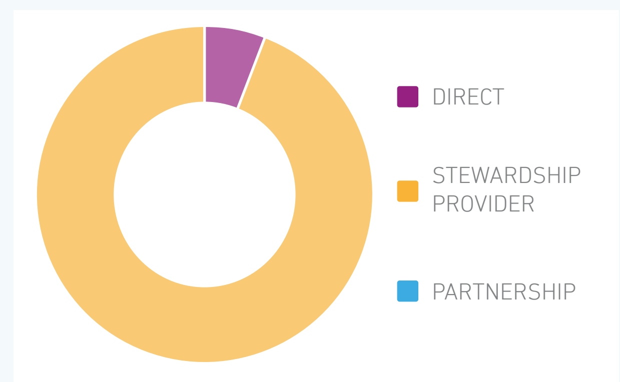


TECHNOLOGY AND DISRUPTIVE INDUSTRIES

This quarter our technology and disruptive industries engagement set comprised 32 companies with 54 engagements issues. There was engagement activity on 51 engagement issues and achievement of some or all engagement objectives on nine occasions.

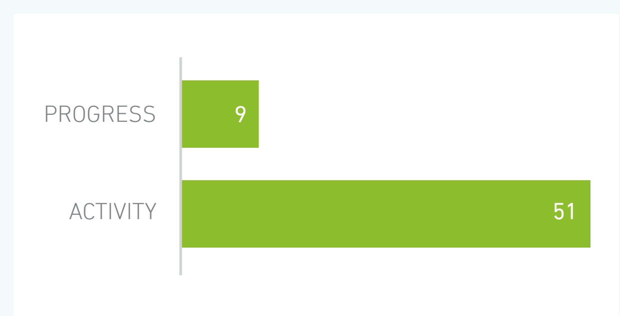
Our attention to social media companies through engagement on social media content control continues and has been amplified by other stakeholders voicing concern about hate speech and disinformation on social media platforms. These concerns have been magnified in the current COVID-19 pandemic when people require robust, factual information but where misinformation and conspiracy theories are evident. During the AGM season we voted for shareholder proposals that ask Facebook and Alphabet to ensure better oversight of human rights risk. In order to further ongoing, collaborative engagement with Alphabet, we voted for a shareholder proposal requesting the establishment of a Human Rights Risk Oversight Committee. The proposal got very strong support, roughly 45% of the independent votes cast for. In our view, human rights risks are embedded in the Company's business model and its technologies, but the Company lacks comprehensive, company-wide policies, processes and due diligence systems to manage them. The Company argues that the current board structure allows for regular assessment of human rights risks, including through the audit committee. We are concerned, however, that the three-member audit committee does not have enough resources or expertise to provide such oversight. Alphabet states that it adheres to the UN Guiding Principles for Business and Human Rights, and we view it as appropriate and necessary that it establishes a Board Committee to carry out this oversight ensuring such adherence. This shareholder proposal reiterates the message in a letter sent to Alphabet in November 2019 by 80 investors, including LGPS Central, requesting a dialogue on human rights risks. The Company denied this request. It is our view that investors need to keep pressure on the Company to improve transparency, accountability and board oversight on material risks including human rights, in order to provide long-term value creation.

ENGAGEMENT VOLUME BY TYPE



- 54 engagements in progress
- Broader stakeholder concern over hate speech and misinformation amplify ongoing engagements around social media content control
- Escalation of engagements through shareholder proposals

ENGAGEMENT VOLUME BY OUTCOME



Examples of engagement outside of stewardship themes

DIVERSITY

LGPS Central has been a member of the 30% Investor Club since inception of the Company. Diversity continues to be on our radar as a key element of good governance, though we see varying degrees of uptake across markets of a more balanced representation of gender, culture, ethnicity etc. at board and management levels of companies. Japanese boards have one of the lowest proportions of female representation in major markets and therefore it is highly welcome that the 30% Investor Club opened a 30% Investor Club Chapter in Japan in May last year. Together with fellow 30% Investor Club members, and led by Royal London Asset Management, we have reached out to two Japanese companies to encourage better diversity and to seek more disclosure on diversity-related policies and targets. Also, we are proposing to these companies that they consider membership in the newly established 30% Investor Club in Japan. Encouragingly one of the companies promptly accepted our proposal for a dialogue and we understand that for these companies, the issue of diversity is relatively new as a topic for discussion with investors.

BROADER SUSTAINABILITY, INCLUDING BIODIVERSITY, LAND-USE AND RIGHTS OF INDIGENOUS PEOPLES

In September 2019, we signed a PRI investor statement alongside more than 250 other investors, calling on companies to take action to prevent deforestation in the Amazon region in Brazil. The situation in Brazil is still very concerning. Provisional legislative measures are being considered due to COVID 19 to legalise private occupation of public lands/forests in the Amazon and to reduce requirements for environmental licensing, amongst others. During the last quarter, we joined an investor coalition led by Norwegian investor Storebrand, to seek dialogue with policymakers in Brazil and to raise these concerns from a long-term investment perspective. We recognise the crucial role that tropical forests play in tackling climate change, protecting biodiversity and ensuring ecosystem services, which again has an impact on economic development and the stability and well-functioning of capital markets. After letters were sent to Brazilian embassies across Europe, US and Japan, the coalition has engaged at the highest political levels, including with the Vice President, the Governor of the Brazilian Central Bank and members of the Brazilian Congress.

02 Voting

POLICY

For UK listed companies, we vote our shares in accordance with a set of bespoke UK Voting Principles. For other markets, we consider the recommendations and advice of our third-party proxy advisor, EOS at Federated Hermes.

COMMENTARY

The 2020 voting season saw many companies in the US and Europe opt for virtual shareholder meetings against the backdrop of COVID 19. While the virtual format posed fresh challenges for companies and investors alike, it is clear that the attention to material ESG issues remains high on investors' agenda and many ESG-related shareholder proposals got very strong or even majority support. LGPS Central attended and asked questions at three virtual shareholder meetings; Honeywell Inc, Citigroup Inc and Glencore. On our behalf, EOS attended and asked questions at 22 shareholder meetings, including Deutsche Bank, BP, Google owner Alphabet, Novartis, Amazon and Facebook.

Between April and June 2020, we:

- Voted at 1,794 meetings (25,366 resolutions) globally
- Opposed one or more resolutions at 1,079 meetings
- Voted with management by exception at 209 meetings and abstained at 23 meetings
- Supported management on all resolutions at the remaining 483 meetings.

A full overview of voting decisions for securities held in portfolios within the company's Authorised Contractual Scheme (ACS) – broken down by market, issues and reflecting number of votes against and abstentions – can be found here.

LAPFF issued alerts for 24 companies on 77 resolutions during this quarter. We voted in alignment with LAPFF recommendations in the majority (59) of cases.

EXAMPLES OF VOTING DECISIONS

At the AGM of **Tencent Holdings Ltd** (Chinese multinational conglomerate holding company specialising in various Internet-related services and products, entertainment, artificial intelligence and technology), we voted against the Chair of the Nominations Committee, Charles Searle. This was to express concerns over low diversity on the board as well as Searle's lack of independence. Searle represents Naspers' interest (Tencent's biggest investor) yet sits on Tencent's audit committee. While we have concerns regarding board diversity, we welcome progress made by the company in appointing its first female director since 2004 last year. We voted for, by exception, re-election of board member Martin Lau. Although Lau sits on more than six boards, Tencent is a minority shareholder at all of them with publicly available information on strategic partnerships. This is considered justified

and manageable. Also, Lau is one of the longest serving executive directors since 2005, has delivered good results for the company over the years and is respected by investors. During this turbulent time, his leadership is needed. We voted against two resolutions that will allow the company to increase capital by more than 10% without pre-emption rights, without justifying any exceptional circumstance. Our concern is that this will excessively dilute existing shareholders' rights. These two resolutions received 30% votes against.

At **Glencore's** AGM we voted against Peter Coates, Chair of Health, Safety, Environment and Communities Committee, as we did at last year's AGM. We are concerned about the Company's poor health and safety performance, over and above our ongoing concern related to Coates' history of advocacy that we view as contrary to the goals of the Paris Agreement and not aligned with Glencore's stated climate ambition and strategy. Approximately 4% of shareholders voted against Peter Coates at the AGM. We voted for the Chair of the Board and the Chair of the Nominations Committee by exception given COVID 19, but the underlying concerns remain on lack of gender diversity, which has gone down to 22% from 25% in 2019. Because of the health pandemic, Glencore hosted a virtual webinar for shareholders at the end of May which we attended, but which we found somewhat lacking in in-depth interaction. We welcome Glencore's recent projection that it will reduce downstream emissions by 30% by 2035 by virtue of not investing into new thermal coal production. Alongside CA100+ investors we are seeking more disclosure on how capital investment plans, methodologies and assumptions align with the goals of the Paris Agreement, as well as disclosure on short-, medium and long-term carbon reduction targets across all scopes. With the CA100+ investor coalition we have agreed to a meeting with the Chair of Glencore in Q3 to discuss these and more issues including succession planning, remuneration and lobbying.

At the AGM of **Facebook**, we voted in favour of four shareholder proposals which all related to the governance of the company. The founder-CEO Mark Zuckerberg owns 13% of the Company but controls a majority of the votes. This is due to the dual class share structure and one of the shareholder proposals calls for the company to initiate and adopt a recapitalisation plan for all outstanding stock to have one vote. The proposal received 27% support. Zuckerberg is both CEO of Facebook and Chair of the board. We are concerned about the inherent lack of independent oversight that this duality entails. A proposal to split the roles of CEO and Chair was also raised last year and continues to get strong minority shareholder support – this time, 20% of shareholders voted for. The third shareholder proposal we supported seeks a change in the Company's constitution so that if a director in a contested election does not receive a majority of the votes cast, he or she is removed from office. This improves shareholder rights and makes the directors accountable to shareholders. As many as 25% of shareholders voted for the proposal at the AGM. The last shareholder proposal we supported requests that the Board nominate a director candidate who is both independent and an expert in human rights. While in most cases we would not support the election of a director whose sole attribute as a board member is expertise on one subject matter, in this case we view it as appropriate to support the proposal which connects directly to our engagement regarding the management of objectionable content. The proposal received approximately 4% support.

At the AGM of **Chevron**, we voted in favour of a shareholder resolution asking the Company to set out a report on risks related to its petrochemical operations in areas prone to severe storms, flooding and sea-level rise. This resolution received 46% support, which sends a clear signal to Chevron that shareholders expect the company to assess and disclose risks linked to climate-change induced weather phenomena, which will ultimately ensure better management of those risks. We also voted in favour of a proposal calling on the company to outline its lobbying around climate change, an expectation that we continue to express to companies across sectors. This proposal received more than 50 per cent support from shareholders and was passed by the AGM. While in the US market shareholder resolutions are only advisory and do not legally bind the Company, it is very unusual for companies not to act on proposals which receive majority support. As has been the case several times in previous years, a resolution was put to the AGM asking that Chevron adopt a policy for an independent chair. We voted for this resolution, consistent with our Voting Principles and the way in which we have discharged similar resolutions at other companies. The oversight provided by an independent Chair is clearly welcomed by many shareholders and attracted more than 26% support.

At the AGM of **Carnival Corporation & Plc** we opposed the approval of the directors' remuneration policy. Carnival Corp and Carnival Plc operate under a Dual-Listed (DLC) structure with primary listings in the US and the UK and two separate but identical boards. The Company's Board and remuneration structures are more in line with those of a US company as most of the operations and executives of Carnival Corp & Plc are located in the US. Under the proposed policy, the CEO can receive up to USD6 million or 400% of base salary in an annual bonus. The most material part of the Carnival pay policy is a combination of highly complex long-term incentive plan awards. In the LGPS Central Voting Principles we advocate for remuneration policies that are simple, transparent, and understandable. In addition, there are multiple incentive plans in place simultaneously. As per the LGPS Central Voting Principles, companies should avoid having more than one active incentive plan.

LGPS CENTRAL LIMITED'S

Partner Organisations

LGPS Central currently contributes to the following investor groups:

LGPS Central Limited

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All information is prepared as of **18.08.2020**.

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Registered Office: Mander House, Mander Centre, Wolverhampton, WV1 3NB

Agenda Item No. 4 (c)

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

9 September 2020

Report of the Director of Finance & ICT

RESPONSIBLE INVESTMENT FRAMEWORK AND CLIMATE STRATEGY

1 Purpose of the Report

To seek approval for Derbyshire Pension Fund's (the Fund) proposed Responsible Investment Framework and Climate Strategy.

2 Information and Analysis

Responsible Investment

In accordance with the LGPS (Management and Investment of Funds) Regulations 2016, the Fund's Investment Strategy Statement (ISS) must set out the administering authority's policy on how environmental, social and corporate governance (ESG) considerations are taken into account in the selection, non-selection, retention and realisation of investments. The Investment Strategy Statement must also cover the authority's policy on the exercise of rights (including voting rights) attached to its investments.

Previously, the Fund's approach to the integration of ESG factors into investment decisions and the Fund's approach to voting, was included in the Fund's ISS, supported by a standalone Voting Policy. A Responsible Investment Framework (RI Framework) has now been developed to set out the Fund's approach to Responsible Investment which includes the integration of ESG considerations into the investment process and Fund stewardship (engagement and voting) and governance activities.

Climate Change

A report outlining the Fund's approach to incorporating the implications of climate change into the Fund's investment process was presented to Committee in August 2017. In 2019, the Fund commissioned a Climate Risk Report from LGPS Central Limited which was received in February 2020 and was structured around the Taskforce for Climate-related Disclosures (TCFD) four thematic areas of: governance; strategy; risk management and metric targets.

The Climate Risk Report also included: an assessment of financially material climate-related risks and opportunities within the Fund's investment portfolio; climate scenario analysis; and carbon risk metrics. The Climate Risk Report was presented to Committee in March 2020, together with a copy of the Fund's first TCFD report, which has subsequently been uploaded to the Fund's website.

In recognition of the potential material effect of climate change, and the response to climate change, on the assets and liabilities of the Fund, a separate Climate Strategy has been developed for the Fund.

The Fund's revised ISS, which is being considered separately by this Committee, contains links to the proposed RI Framework and Climate Strategy.

Training
Members of this Committee and of Derbyshire Pension Board have taken part in training sessions covering the ISS, and the proposed RI Framework and Climate Strategy as part of the process of formulating these strategies.

The responsible investment training covered:

- the definition of RI
- LGPS RI regulations
- a three pillar approach to RI
- the spectrum of capital (investment approaches ranging from traditional investment to philanthropy)
- the West Midlands Pension Fund Global Sustainable Framework
- LGPS Central Pool beliefs
- LGPS Central Ltd stewardship
- Engagement versus divestment
- the Local Authority Pension Fund Forum

The climate change training covered:

- what is climate change
- fossil fuel consumption and carbon dioxide emissions
- energy sources and usage
- climate change risks and opportunities
- the Paris Agreement
- the Fund's carbon metrics
- regional benchmark carbon metrics
- the quality of carbon emissions scores & the significance of Scope 3 emissions (indirect emissions that occur in the value chain of the reporting company, including both upstream and downstream emissions)
- the impact of carbon emissions scores on investment decisions

- the Institutional Investors Group of Climate Change draft Net Zero Framework
- net zero implications
- other LGPS pension funds' climate strategies
- key climate strategy questions & the Fund's proposed strategy

RI Framework
The Fund believes that responsible investment can enhance long-term performance. Effective management of financially material ESG risks should support the requirement to protect investment returns over the long term and companies with strong ESG business practices have the potential to create additional value for shareholders.

Responsible investment has relevance both before (i.e. investment selection) and after an investment decision (i.e. on-going stewardship through engagement and voting activity) and is a core part of the Fund's fiduciary duty. It is distinct from 'ethical investment', which is an approach to selecting investments on the basis of ethical beliefs (beliefs about what is morally right and wrong).

The Committee recognises its responsibility to act in the best interest of the Fund's employers and scheme members, whilst seeking to protect local tax payers and employers from unsustainable pension costs.

The RI Framework is consistent with LGPS Central Limited's Responsible Investment & Engagement Framework, which was developed in collaboration with the eight LGPS funds (Partner Funds) within the LGPS Central Pool. In order for the Partner Funds to invest together via the LGPS Central Pool, the agreement of a common approach to responsible investment is important.

The Fund's RI Framework is based on three core pillars: manager selection; stewardship (engagement and voting); and transparent disclosure. A copy of the Fund's proposed Responsible Investment Framework is set out at Appendix 1.

Climate Strategy
The Fund's Climate Risk Report, high level climate change risk analysis from the Fund's actuary, Hymans Robertson, guidance on implementing the TCFD recommendations for assets owners from the TCFD, together with additional internal research into climate risk metrics and the output of the recent member training sessions, have been utilized to develop the proposed Climate Strategy which is attached as Appendix 2.

The Climate Strategy sets out the Fund's approach to addressing the risks and opportunities related to climate change. It includes the introduction of targets to reduce the carbon emissions of the Fund's investment portfolio and to increase investment in low carbon and sustainable investments. The

targets will be reviewed at least every five years. A material increase in the targets in the five year period to 2030, and in each subsequent five year period, is expected, in line with the stated ambition of achieving a portfolio of assets with net zero carbon emissions by 2050. Progress against the targets will be reported every two years.

Consultation
The Fund will consult with its stakeholders, including scheme employers, the local pension board and members of the pension fund, on the proposed RI Framework and Climate Strategy. The results of the consultation will be reported to Committee in December 2020.

Approval is sought for the Director of Finance & ICT, in conjunction with the Chair of the Committee, to consider the results of the consultation in the meantime, and to determine if any revisions to the proposed RI Framework and Climate Strategy are necessary following the consultation.

3 Other Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal and human rights, human resources, equality and diversity, health, environmental, transport, property and prevention of crime and disorder.

4 Background Papers

Files held by the Investment Section.

5 Officer's Recommendations

That the Committee:

I. Approves the proposed Responsible Investment Framework and Climate Strategy, subject to the outcome of the consultation with the Fund's stakeholders.

II. Delegates the consideration of the results of the consultation, and the determination of whether any revisions to the proposed RI Framework and Climate Strategy are necessary following the consultation, to the Director of Finance & ICT in conjunction with the Chair.

Peter Handford

Director of Finance & ICT

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Appendix 1

Responsible Investment Framework

Draft – September 2020

County Hall, Matlock, Derbyshire, DE4 3AH
Administered by Derbyshire County Council

lgps

1. Introduction

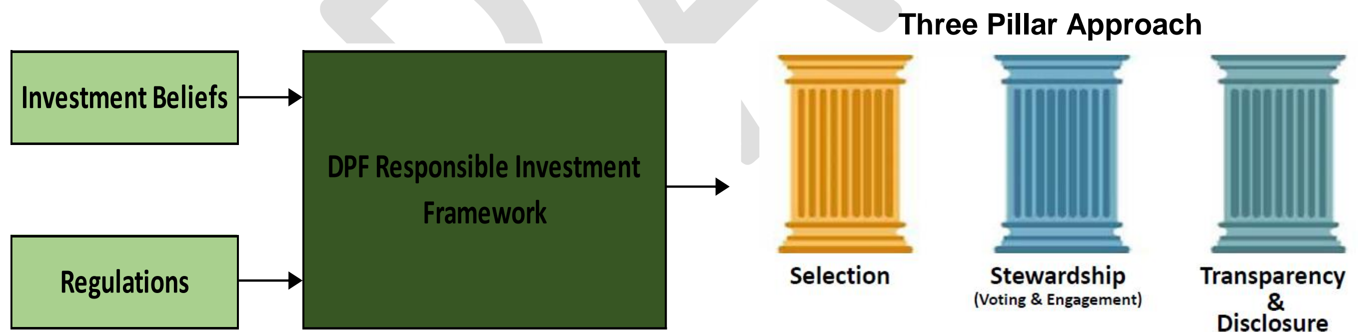
This Responsible Investment Framework (RI Framework) sets out Derbyshire Pension Fund's (the Fund) approach to responsible investment (RI) which includes the integration of environmental, social and governance (ESG) considerations into the investment process and Fund stewardship and governance activities.

The Pensions and Investments Committee (the Committee) is responsible for reviewing and approving the Fund's policies and strategies, including the RI Framework. The RI Framework works in tandem with the Fund's Climate Strategy, Investment Strategy Statement and Funding Strategy Statement aligning with the Fund's investment beliefs and fiduciary duty.

The Committee will review the Responsible Investment Framework at least every three years, or at such time as the Commiteee determines it is appropriate to review the Fund's approach to RI.

Responsibility for the implementation of the Framework resides with the Head of Pension Fund and the Investments Manager.

The Fund takes a three pillar approach to the implementation of Responsible Investment as set out below:



2. Responsible Investment

Responsible investment is an approach to investment that aims to incorporate ESG factors into investment decisions, to better manage risk and generate sustainable, long term returns.[1] It has relevance both during the selection of an investment and after an investment decision has been made, through on-going stewardship activity which covers considered voting and engagement with investee companies.

Responsible investment is a core part of the Fund's fiduciary duty. It is distinct from

[1] PRI Principles for Responsible Investment

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‘ethical investment’, which is an approach to selecting investments on the basis of ethical beliefs (beliefs about what is morally right and wrong).

Effective management of financially material ESG risks should support the requirement to protect investment returns over the long term. The Fund’s investment team seeks to understand relevant ESG factors alongside conventional financial considerations within the investment process, and the Fund’s external investment managers are expected to do the same. Non-financial factors may be considered to the extent that they are not detrimental to the investment return.

ESG factors include:

Environmental	**Social**	**Governance**
Climate Change (including physical risk and transition risk)	Working Conditions (including slavery & child labour)	Executive Pay
Resource Depletion	Health & Safety	Bribery & Corruption
Waste & Pollution	Employee Relations	Board Diversity
Deforestation	Community Relations	Tax Strategy
		Political Lobbying
		Disclosure & Transparency

The Fund’s Strategic Asset Allocation Benchmark includes an allocation to Global Sustainable Equities. Sustainable investment managers are regarded as managers who invest in companies with a long term approach to sustainability where the effective management of environmental, social and governance risks and opportunities is an integral part of the strategy to create a sustainable business. Companies with strong ESG business practices have the potential to create additional value for shareholders.

Within the Global Sustainable Equities allocation, the Fund will consider impact investment managers who invest in companies which aim to contribute to a more sustainable world, by seeking to effect positive social and enivironmental change, while generating investment returns.

The Committee recognizes its responsibility to act in the best interest of the Fund’s employers and scheme members, whilst seeking to protect local tax payers and employers from unsustainable pension costs.

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3. Investment Beliefs

The Fund's investment beliefs as set out in the Fund's Investment Strategy Statement are as follows:

- A long term approach to investment will deliver better returns
- The long term nature of LGPS liabilities allows for a long term investment horizon
- Asset allocation is the most important factor in driving long term investment returns
- Liabilities influence the asset structure; funds exist to meet their obligations
- Risk premiums exist for certain investments; taking advantage of these can help to improve investment returns
- Markets can be inefficient, and mispriced for long periods of time; therefore there is a place for active and passive investment management
- Diversification across investments with low correlation improves the risk/return profile
- Secure and growing income streams underpin the ability to meet future liabilities
- Responsible investment can enhance long term investment performance
- Investment management costs should be minimized where possible but net investment returns after costs are the most important factor

4. Regulations & Statutory Guidance

The Responsible Investment Framework works in tandem with the Fund's Investment Strategy Statement. The Framework and Investment Strategy Statement have been developed in accordance with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, statutory guidance, and best practice.

5. Engagement & Collaboration

The Fund adopts a strategy of engagement with companies to influence behaviour and enhance value, rather than adopting a divestment approach, believing that this is more compatible with the administering authority's fiduciary duties and supports responsible investment.

Engagement allows the Fund to use its influence as an active owner, with other like-minded investors, to improve ESG practices in investee companies, influence that would be lost through a divestment approach. It is recognised that change takes time, as a long term investor the Fund takes a long term approach to its stewardship activities.

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6. Remuneration and Cost Management

Executive remuneration and investment management costs are important, particularly in low-return environments. Fee arrangements with fund managers and the remuneration policies of investee companies should be aligned with the Fund's long-term interests.

7. Climate Change

The Committee recognises that financial markets will be impacted by climate change and by the response of climate change policy makers. Risks and opportunities related to climate change are likely to be experienced across the whole of the Fund's portfolio. The current understanding of the potential risks posed by climate change, together with the development of climate- related measurements and disclosures, are still at an early stage, and there is considerable variability in the quality and comparability of carbon emission estimates. It is recognised that it will take time for companies to adapt to the changing regulatory and market positions.

Reflecting the potential material effect of climate change, and the response to change climate, on the assets and liabilities of the Fund, a separate Climate Strategy has been developed, a copy of which can be found on the Fund's website at [link]

8. LGPS Central Limited

The Fund is part of the LGPS Central Pool (the Pool) with the LGPS funds of Cheshire, Leicestershire, Nottinghamshire, Shropshire, Staffordshire, West Midlands and Worcestershire (the eight Partner Funds). The Pool has been established in accordance with Government requirements for the pooling of LGPS investment assets. LGPS Central Limited has been established to manage investments on behalf of the Pool, and received authorization from the Financial Conduct Authority in January 2018. The Company launched its first sub-funds within an Authorised Contractual Scheme collective investment vehicle in April 2018, and has launched several additional sub-funds since that date.

LGPS Central Limited has developed a Responsible Investment & Engagement Framework (LGPSC Framework) incorporating the investment beliefs and responsible investment beliefs of the eight Pension Funds within the LGPS Central Pool which will be applied to both internally and externally managed investment mandates. The LGPSC Framework contains the following beliefs:

- Long-termism: A long-term approach to investment will deliver better returns and the long-term nature of LGPS liabilities allows for a long-term investment horizon.
- Responsible Investment: Responsible Investment is supportive of risk adjusted returns over the long-term, across all asset classes. Responsible investment should be integrated into the investment process of the Company and its investment managers.

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- Diversification, risk management and stewardship: Diversification across investments with low correlation improves the risk return profile. A strategy of engagement, rather than exclusion, is more compatible with fiduciary duty and more supportive of responsible investment, because the opportunity to influence companies through stewardship is waived in a divestment approach. Even well-diversified portfolios face systematic risk. Systematic risk can be mitigated over the long-term through widespread stewardship and industry participation.
- Corporate governance and cognitive diversity: Investee companies and asset managers with robust governance structures should be better positioned to handle the effects of shocks and stresses of future events. There is clear evidence showing that decision-making and performance are improved when company boards and investment teams are composed of cognitively diverse individuals.
- Fees and remuneration: The management fees of investment managers and the remuneration policies of investee companies are of significance for the Company's clients, particularly in a low-return environment. Fees and remuneration should be aligned with the long-term interests of our clients, and value for money is more important than the simple minimisation of costs.
- Risk and opportunity: Risk premia exist for certain investments; taking advantage of these can help to improve returns. There is risk, but also opportunity in holding companies that have weak governance of financially material ESG issues. Opportunities can be captured so long as they are aligned to the Company's objectives and strategy, and so long as there is a sufficient evidence base upon which to make an investment decision.
- Climate change: Financial markets could be materially impacted by climate change and by the response of climate policy makers. Responsible investors should proactively manage this risk factor through stewardship activities, using partnerships of like-minded investors where feasible.

In collaboration with the eight Partner Funds, LGPS Central Limited has identified four themes that will be given particular attention in its ongoing stewardship efforts. The four themes, which will be reviewed after three years, are: Climate change; Single-use plastics; Fair tax payment and tax transparency; and Technology and disruptive industries. The Partner Funds and LGPS Central Limited believe that identifying material core themes helps direct engagement and sends a clear signal to companies of the areas that the Partner Funds and LGPS Central Limited are likely to be concerned with during engagement meetings.

LGPS Central Limited also supports the Fund through the annual preparation of a Climate Risk Report which supports the Fund in the preparation of the Fund's Climate Related Disclosure Report prepared in alignment with the recommendations of the Taskforce on Climate-related Financial Disclosures.

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9. Implementation

The Fund aims to put its Responsible Investment Strategy into practice through actions both before (selection) and after the investment decision (stewardship).

As a largely externally-managed pension fund, the identification and assessment of RI factors is also the responsibility of individual investment managers appointed by the Fund.

The Fund aims to be transparent to its stakeholders through regular, high quality disclosure.

9.1 Selection

ESG factors are integrated into the Fund's investment decision making process where those factors are financially material within the context of the investment mandate. As part of the investment manager due diligence process, the Fund obtains a copy of the potential investment manager's RI or stewardship policies which sets out how RI factors are integrated into the investment manager's investment process.

9.2 Investment Manager Monitoring

Existing investment managers are monitored on a regular basis to review the integration of ESG risks into the portfolio management, and to understand their engagement activities.

9.3 Company Engagement and Engagement through Partnership

The Fund's strategy is to engage with its investee companies either on its own or through partnerships on a range of financially material ESG investment factors to protect and increase shareholder value. These partnerships include:

- The Local Authority Pension Fund Forum (LAPFF): a voluntary association of the majority of Local Authority pension funds based in the UK with combined assets of over £300bn. Membership of LAPFF provides the Fund with independent research and advice on RI risks of companies to inform further stakeholder engagement; advice on the governance practices of companies; and a forum to engage with companies to improve governance practices
- LGPS Central Limited: the Fund's pooled investment operator
- Hermes EOS: Hermes EOS is engaged by LGPS Central Limited to expand the scope of its engagement programme, especially to reach non-UK companies

The Fund will develop an Annual Responsible Investment Stewardship Plan, and hold constructive dialogue with investee companies on RI issues (either on its own or through partnerships), and where practicable, participate in the development of public policy on RI issues.

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9.4 Voting

The Fund places great importance on the exercise of voting rights. The Fund's voting policy covers the Fund's directly held investments in the United Kingdom and North America. The Committee has appointed Institutional Shareholder Services (ISS), a specialist third party voting service provider to make recommendations on casting votes in respect of the Fund's directly held UK listed investments. Voting is carried out in line with recommendations from ISS, whose voting principles cover four key tenets on: accountability; stewardship; independence; and transparency. The Fund also periodically receives voting alerts from the LAPFF on certain resolutions. If the voting alert from the LAPFF conflicts with the voting service recommendation, due consideration is given to all the arguments before the vote is cast.

The Fund has appointed Wellington Management (Wellington) in a discretionary capacity to manage its directly held North American investments, including voting in line with local practice. Wellington have policies and procedures to ensure that they collect and analyse all relevant information for each meeting, applying their proxy voting guidelines accurately and executing votes in a timely manner.

A significant proportion of the Fund's assets are managed through pooled products, where the voting activity is carried out by external investment managers. These principally relate to funds managed Legal & General Investment Management (LGIM).

Voting activity is carried out in accordance with LGIM's voting policy, and is based on a set of corporate governance principles. Previous engagement with an investee company also determines the manner in which voting decisions are made and cast. Voting activity is combined with direct engagement with the investee company to ensure that the investee company fully understands any issues and concerns that LGIM may have and to encourage improvement. LGIM utilises the voting invormation services of ISS and Institutional Voting Information Services (IVIS) to conduct thorough analysis and research on investee companies.

The Fund expects an increasing proportion of its assets to be managed by LGPS Central Limited going forward, as assets are transitioned into its pooled products. LGPS Central Limited's Responsible Investment & Engagement Framework will be applied to both internally and externally managed investment mandates.

Copies of LGIM's and LGPS Central Limited's Stewardship Reports are presented to the Committee on a quarterly basis.

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9.5 UK Stewardship Code

The Fund is a Tier 1 signatory to the Financial Reporting Council's (FRC) UK Stewardship Code 2012. A copy of the Fund's statement of compliance with the code can be found on the Fund's website at: FRC

The UK Stewardship Code has recently been updated (2020 Code); the updated code came into effect on 1 January 2020. The 2020 Code consists of 12 Principles for Asset Managers and Asset Owners, with a focus on the activities and outcomes of stewardship, not just policy statements.

Organisations that want to become signatories to the 2020 Code will be required to produce an annual Stewardship Report explaining how they have applied the 2020 Code in the previous twelve months. To be included in the first list of signatories, organisations must submit a final report to the FRC by 31 March 2021. The Fund intends to fully comply with the 2020 Code.

10. Transparency and Disclosure

The Fund aims to keep its stakeholders aware of RI activities through:

- Making its Responsible Investment Framework, together with the supporting Climate Strategy, public documents
- Reporting to Committee on the stewardship activities (including voting decisions) of the Fund's principle investment managers on a quarterly basis
- Providing a summary of the Fund's RI activities in the annual report
- Reporting annually using the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD)
- Reporting on progress against the RI Stewardship engagement goals every two years

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Appendix 2

Climate Strategy

Draft – September 2020

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Administered by Derbyshire County Council

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1. Introduction

This Climate Strategy sets out Derbyshire Pension Fund's (the Fund) approach to addressing the risks and opportunities related to climate change.

The Fund supports the ambitions of the Paris Agreement[1] and aims to achieve a portfolio of assets with net zero carbon emissions by 2050.

The Pensions and Investments Committee (the Committee) is responsible for reviewing and approving the Fund's policies and strategies, including the Climate Strategy. The Climate Strategy works in tandem with the Fund's Responsible Investment Framework, Investment Strategy Statement and Funding Strategy Statement.

The development of a separate Climate Strategy reflects the potential material effect of climate change, and the response to climate change, on the assets and liabilities of the Fund.

The Committee will review the Climate Strategy at least every three years, or at such time as the Committee determines it is appropriate to review the Fund's approach to addressing the risks and opportunities related to climate change.

Responsibility for the identification and management of climate-related risks, together with the implementation of the Fund's Climate Strategy, resides with the Head of Pension Fund and the Investments Manager.

2. Climate Change

Human activities are estimated to have caused approximately 1.0°C of global warming above pre-industrial levels. Most of this warming has occurred in the last 35 years, with the five warmest years on record taking place since 2010. The observed global mean surface temperature has risen from around 1950 onwards. Over 97% of climate scientists (Source: NASA) agree that this trend is the result of greenhouse gas (GHG) emissions which are being trapped in the atmosphere and creating a 'greenhouse effect' – a warming that occurs when the atmosphere blocks heat radiating from Earth towards space. These climate scientists have observed that these climactic changes are primarily the result of human activities including electricity and heat production, agriculture and land use change, industry, and transport.

This is causing more frequent and more extreme weather events and world governments have started to respond. The signatories to the 2015 Paris Agreement committed to keeping the global temperature rise this century to well below 2.0°C compared with pre-industrial levels and to aiming to limit the increase to 1.5°C (Article 2(1)a). The Paris Agreement commits signatories to the establishment of Nationally Determined

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[1] Paris Agreement – To hold the increase in the global temperature to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5°C above pre-industrial levels – ratified by 189 parties.

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Contributions (NDCs), which are intended to be individually equitable and collectively sufficient to achieve Article 2(1)a. It is estimated that under current global policies (and assuming successful implementation), the world is heading towards a warming of 3.2°C.

The low-carbon transition is already underway, with a number of governments and institutions around the world intensifying their climate change policies, and corporates responding in turn.

Investors are exposed globally to the risks and opportunities presented by climate change adaption and mitigation. Investors have an important role to play in the transition to a low carbon economy, influencing company behaviours and encouraging the development of better climate-related disclosures. However, investors cannot effect material change alone. Governments, policy makers, consumers, companies and investors all have a role to play in the transition to a low carbon economy.

If policy and corporate action does not progressively transition towards the net zero goal, it will be extremely challenging for investors to achieve a portfolio of assets that has net zero emissions in 2050.

The Fund recognises that:

- Human activities have caused a change in the earth's climate which presents material risks to human and eco-systems and to global economies
- A global co-ordinated policy response and a change in consumer behaviour will be required to limit the damaging rise in global temperatures
- Climate change is a long term financial material risk for the Fund, across all asset classes, and has the potential to impact the funding level of the Fund through impacts on employer covenant, asset pricing, and longer-term inflation, interest rates and life expectancy

The Fund believes that:

- The risks and opportunities of climate change should be considered as part of asset allocation decisions, manager selection decisions and individual investment decisions
- Diversification across asset classes, regions and sectors is an important risk management tool to reduce climate-related risks
- In order to fully integrate climate-related risk into the Fund's investment processes, the consistency, comparability and quality of climate-related data, including the identification and measurement of companies' Scope 3 emissions will need to improve
- The low-carbon transition is already underway, but the pathway is unclear, and the transition will not occur by focussing only on the suppliers of energy; the demand for energy must also be addressed

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- It is possible for a company to shift its business model in order to trive in the transition to a low carbon future; such a shift is more likely with the support and stewardship of responsible investors

3. Climate-related Objectives

The Fund aims to have access to the best possible information available on the risk and opportunities presented by climate change. This includes impacts to the Fund's investment strategy, or funding strategy, as a result of transition risks, physical risks and opportunities.

The Fund aims to ensure that its investment portfolio will be as resilient as possible to climate-related risks over the short, medium and long term. For an effective first line of defence, the Fund aims to integrate climate-related factors into the investment process, including the selection of investment managers.

The Fund intends to decarbonise its portfolio through its selection of investments and investment managers, with the aim of being carbon neutral by 2050.

4. Collaboration and Transparency

The Fund aims to collaborate with like-minded organisations to support the ambitions of climate-related initiatives and aims to be fully transparent with its stakeholders through regular public disclosure, aligned with best practice.

- The Fund supports the Paris Agreement on Climate Change
- The Fund will actively participate in selected initiatives that lend support to the Fund's Climate Strategy, including working with other like-minded investors to engage with high-emitting companies
- The Fund supports the Taskforce on Climate-related Financial Disclosures (TCFD) and adopts its recommendations for the Fund's climate disclosures

5. Strategic Actions

5.1 Measurement & Observation

The Fund recognises that the tools and techniques for assessing climate-related risks in investment portfolios are an imperfect but evolving discipline. The Fund aims to use the best available information to assess climate-related threats to investment performance.

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The Fund will make regular measurements and observations on climate-related risks and opportunities relevant to the Fund. This will include:

- Identification of the most material climate-related risks to the Fund
- Economic assessment of the Fund's asset allocation against plausible climate-related scenarios
- A suite of carbon metrics for the Fund's listed equity portfolio to allow the Fund to assess progress in responding to climate-related risks and opportunities, including: carbon intensity; weight in companies with fossil fuel reserves; weight in companies with thermal coal reserves; and weight in companies with clean technology. A more complete analysis of all of the Fund's assets classes will be carried out when reliable carbon-related data becomes available for non-listed equity assets
- Assessment of progression against the Fund's carbon footprint and low carbon & sustainable investment targets

Methodologies for assessing the impact of future climate-related scenarios, including the possibility of measuring against alignment with the Paris Agreement, remain at an early stage of development, and the Fund will support efforts to develop more reliable and comparable methodologies.

The Fund recognises that there is currently significant variability in the relevance, consistency, comparability and quality of companies' climate-related disclosures. The Fund supports adoption, and encourages disclosure, in line with the recommendations of the TCFD.

5.2 Asset Allocation & Targets

Where there is a credible evidence base, the Fund will integrate climate-related factors into asset class reviews, subject to the requirements of the Investment Strategy Statement and Funding Strategy Statement.

The Fund believes that portfolio-wide 'top down' targets are an important means to set direction and appropriate ambition for an investment strategy towards net zero, and to monitor whether that strategy is achieving expected outcomes. However, a focus on just a single top down portfolio emissions reduction target can incentivise a shift of assets within a portfolio from high to already lower carbon assets and sectors, rather than driving additional 'real world' emissions reductions from increasing investments in climate solutions that contribute to the achievement of the net zero goal. As a result, the Fund will aim to:

- reduce the carbon footprint (Scope 1 & 2) of the Fund's listed equity portfolio by at least **30%** relative to the weighted benchmark in 2020 by the end of 2025; and
- invest at least **30%** of the Fund portfolio in low carbon & sustainable investments by the end of 2025.

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The Fund will review the carbon footprint and low carbon & sustainable investment targets on, at least, a five yearly basis thereafter. The Fund expects to see a material increase in the targets in the five year period to 2030, and in each subsequent five year period, on the journey to a carbon neutral portfolio, taking into account the contemporary development of carbon-related data metrics and availability of suitable products across all asset classes.

5.3 Manager Selection and Monitoring

The Fund will assess material climate-related risk and opportunities, alongside other relevant investment factors, as part of the investment manager selection process.

As a largely externally-managed pension fund, the identification and assessment of climate-related risks is also the responsibility of individual investment managers appointed by the Fund. Existing investment managers are monitored on a regular basis to review the integration of climate-related risks into the portfolio management, and to understand their engagement activities.

5.4 Stewardship

The Fund's annual Responsible Investment Stewardship Plan will include a section on climate-related stewardship plans. This will set clear goals of engagement with investee companies and investment managers to manage risks and opportunities within the Fund's investment portfolio, focusing on those risks and opportunities which will have the greatest impact.

The Fund will collaborate with other like-minded investors where possible and the Fund will participate in selected collaborative initiatives where these support the Fund's climate-related objectives.

The Fund will make full use of its voting rights and will co-file or support climate-related shareholder resolutions where these support the Fund's climate-related objectives.

6. Transparency & Disclosure

The Fund will:

- prepare a TCFD Report every two years
- report on the progression against the Fund's carbon footprint and low carbon & sustainable investment targets every two years
- report on a suite of carbon metrics in the Fund's annual report
- disclose the stewardship reports of the Fund's key investment managers on a quarterly basis
- report on progress against the RI Stewardship Plan engagement goals every two years

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Agenda Item No. 4 (d)

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

9 September 2020

Report of the Director of Finance & ICT

STRATEGIC ASSET ALLOCATION BENCHMARK AND INVESTMENT STRATEGY STATEMENT

1 Purpose of the Report

To seek approval for a new Strategic Asset Allocation Benchmark for Derbyshire Pension Fund (the Fund/Pension Fund) and a revised Investment Strategy Statement.

2 Information and Analysis

Strategic Asset Allocation Benchmark

At the last formal actuarial valuation at the end of March 2019, the funding level of the Pension Fund was 97%. This was an improvement on the funding level of 87% at the formal valuation at the end of March 2016.

The funding level of the Pension Fund is the ratio of assets to liabilities at the valuation date. The funding level provides a high-level snapshot of the funding position at a particular date.

At 31 March 2019, the assets of the Fund were valued at £4,929m and the past service liabilities were estimated to be £5,092m. The investment and membership experience of the Fund from March 2016 to March 2019 had a positive impact on the funding level.

Despite the recent turbulence in markets related to the Covid-19 pandemic, investment returns have generally been positive since March 2019. The experience related to the liabilities of the Fund over that period is more difficult to estimate, in the absence of an interim funding update. However, conversations with the Fund's actuary indicate that the current funding level is likely to be in the region of 95%.

Following the receipt of the formal March 2019 actuarial valuation, the Fund's Strategic Asset Allocation Benchmark (SAAB) has been reviewed, taking into consideration the improvement in the funding level . The following changes are proposed:

Asset Class	Current SAAB	Proposed Intermediate SAAB	Proposed Final SAAB	Final Change
UK Equities	16.0%	14.0%	12.0%	(4.0%)
North American Equities	12.0%	6.0%	-	(12.0%)
European Equities	8.0%	4.0%	-	(8.0%)
Japanese Equities	5.0%	5.0%	5.0%	-
Asia Pacific Ex-Japan Equities	4.0%	2.0%	-	(4.0%)
Emerging Market Equities	5.0%	5.0%	5.0%	-
Global Sustainable Equities	3.0%	16.0%	29.0%	26.0%
Private Equity	4.0%	4.0%	4.0%	-
Growth Assets	**57.0%**	**56.0%**	**55.0%**	**(2.0%)**
Infrastructure	8.0%	9.0%	10.0%	2.0%
Multi-Asset Credit	6.0%	6.0%	6.0%	-
Direct Property	5.0%	6.0%	6.0%	1.0%
Indirect Property	4.0%	3.0%	3.0%	(1.0%)
Income Assets	**23.0%**	**24.0%**	**25.0%**	**2.0%**
Conventional Bonds	6.0%	6.0%	6.0%	-
Index-Linked Bonds	6.0%	6.0%	6.0%	-
Corporate Bonds	6.0%	6.0%	6.0%	-
Cash	2.0%	2.0%	2.0%	-
Protection Assets	**20.0%**	**20.0%**	**20.0%**	**-**
Total	**100.0%**	**100.0%**	**100.0%**	**-**

The proposed final SAAB includes a modest 2% switch from Growth Assets to Income Assets reflecting the improvement in the Fund's funding position, whilst acknowledging that the Fund is open to new members and continues to accrue additional future pension liabilities.

Whilst the final SAAB continues to assume that some of the Fund's equity allocations are managed on a regional basis, these are reduced and targeted at those regions were the Fund's In-House Investment Management Team believe that they offer portfolio diversification. It is proposed that the current equity allocations in respect of North America, Europe and Asia Pacific Ex-Japan are consolidated and switched into Global Sustainable Equities.

The Fund introduced a 3% allocation to Global Sustainable Equities in October 2018. The allocation targets investment in global companies that are sustainable in financial, environmental, social and governance terms and, where appropriate, that provide solutions to sustainability challenges.

The Fund has worked with other members of the LGPS Central Pool over the last twelve to eighteen months to build its knowledge of the asset class, and made its first allocation to the asset class in April 2020 through a collaborative West Midlands Pension Fund Global Sustainable Equity Framework Agreement. The IIMT believe that the asset class is well aligned with the

Fund's Responsible Investment Framework and Climate Strategy, and offers attractive long-term risk adjusted returns.

The proposed 2% increase in Income Assets is allocated to Infrastructure, taking the asset class weighting to 10%. Infrastructure is an attractive asset class for the pension fund, offering equity like returns, predictable long-term cash flows which are often linked to inflation, and returns with a low correlation to other major asset classes.

Whilst the overall Property allocation is unchanged at 9%, it is recommended that the Direct Property allocation is increased by 1%, offset by a 1% reduction in the Indirect Property allocation. The IIMT believes that this will allow the Fund's Discretionary Direct Property Manager to actively source additional opportunities, whilst reducing the investment management fees payable by the Fund.

Given the quantum of the proposed changes between the current and final SAAB, the IIMT recommends that an intermediate SAAB is also approved to allow the IIMT to manage the transition risk towards the final SAAB. The intermediate SAAB is expected to come into effect at the beginning of Q4 2020-21, with the final SSAB expected to come into effect by 1 January 2022 at the latest.

(i) Investment Strategy Statement

The Fund's SAAB is included in the Fund's Investment Strategy Statement. LGPS Regulations require an administering authority to prepare an Investment Strategy Statement in accordance with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the 2016 Regulations). The Fund's Investment Strategy Statement was last revised in October 2018.

Under the 2016 Regulations, the Investment Strategy Statement must be reviewed, and if necessary revised, following a material change in the factors which are judged to have a bearing on the stated investment policy, and at least every three years. Given the proposed changes to the Fund's SAAB set out in this report, a revised Investment Strategy Statement has been prepared, a copy of which is set out at Appendix 1.

In addition to the changes in the SAAB, the Investment Strategy Statement has been updated for the following:

- Extending the Fund's hedging policy to include both Income Assets and Protection Assets (previously just Protection Assets) to reduce the Fund's overseas currency exposure. The Fund continues to regard the currency exposure associated with investing in overseas equities as part of the return on overseas equities; and

- Reference to the Fund's standalone Responsible Investment Framework and Climate Strategy, both of which are supplementary to the Investment Strategy Statement.

The Investment Strategy Statement must cover:

- A requirement to use a wide variety of investments;
- The authority's assessment of the suitability of particular investments and types of investment;
- The authority's approach to risk, including how it will be measured and managed;
- The authority's approach to pooling investments, including the use of collective investment vehicles and shared services;
- The authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and
- The authority's policy on the exercise of rights (including voting rights) attached to its investments.

The Investment Strategy Statement must also set out the maximum percentage of the total value of all investments of fund money that it will invest in particular investments or classes of investment and the authority is required to consult such persons as it considers appropriate regarding the proposed contents of its investment strategy.

The Fund's independent investment adviser, Anthony Fletcher, has reviewed the revised Investment Strategy Statement and the proposed changes to the SAAB and a copy of the advisor's review is set out at Appendix 2.

(ii) Consultation

It is intended to consult with scheme employers, the local pension board and other stakeholders on the revised Investment Strategy Statement. The results of the consultation will be reported to Committee in December 2020.

Approval is sought for the Director of Finance & ICT, in conjunction with the Chair of the Committee, to consider the results of the consultation in the meantime, and for the Director of Finance & ICT and the Chair to determine if any revisions to the proposed Investment Strategy Statement are necessary following the consultation, in able to allow the new investment strategy. to be adopted at the beginning of Q4 2020-21.

3 Other Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal and human rights, human resources, equality and

diversity, health, environmental, transport, property and prevention of crime and disorder.

4 Background Papers

Files held by the Investment Section.

5 Officer's Recommendations

That the Committee:

(i) Approves the revised Investment Strategy Statement set out in this report, including the proposed changes to the Strategic Asset Allocation Benchmark, subject to the outcome of the consultation with the Fund's stakeholders.

(ii) Delegates the consideration of the results of the consultation, and the determination of whether any revisions to the proposed Investment Strategy Statement are necessary following the consultation, to the Director of Finance & ICT in conjunction with the Chair.

Peter Handford

Director of Finance & ICT

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Appendix 1

Investment Strategy Statement

Draft – September 2020

County Hall, Matlock, Derbyshire, DE4 3AH
Administered by Derbyshire County Council

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Derbyshire Pension Fund

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Introduction

This is the Investment Strategy Statement (the ISS) of Derbyshire Pension Fund (the Fund), which is administered by Derbyshire County Council. The ISS is drawn up in compliance with Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the Regulations) and has been prepared following consultation with such persons as Derbyshire County Council considered appropriate.

The ISS will be reviewed following any material change in the factors which are judged to have a bearing on the stated investment policy and at least every three years as required by the Regulations.

The primary objective of the Fund is to ensure that over the long term the Fund will be able to meet all benefit payments as and when they fall due. These payments will be met by contributions resulting from the funding strategy or asset returns and income resulting from the investment strategy. The funding and investment strategies are, therefore, inextricably linked; the Funding Strategy Statement can be found on the Fund's website at: [link]

Fund Governance

Derbyshire County Council is an administering authority for the Local Government Pension Scheme in accordance with Local Government Pension Scheme Regulations 2013. The Pensions and Investments Committee (the Committee) is responsible for discharging Derbyshire County Council's statutory function as the administering authority for the Fund.

The Committee is responsible for determining the Fund's investment policy, monitoring performance and overall stewardship of the Fund. Members of the Committee act in a similar manner to trustees and take advice from Anthony Fletcher, the Fund's Independent Adviser and from the Director of Finance & ICT and the Fund's in-house investment managers.

A proportion of the Fund's investments are managed on an active basis by the Fund's in-house Investment Team, and by LGPS Central Limited, a company established to manage investments on behalf of eight LGPS pension funds across the Midlands. Where the appropriate skills are not available internally, or through LGPS Central Limited, external managers are used.

In 2015, Derbyshire Pension Board was established to assist the administering authority to ensure the effective and efficient governance and administration of the Local Government Pension Scheme.

Full details of the Fund's governance arrangements, including the governance arrangements for the LGPS Central Pool, are contained in the Governance Policy and Compliance Statement which is published on the Fund's website: [link]

Investment Objectives

The Committee has agreed a long term investment strategy that aims to maximise the returns from investments within acceptable levels of risk, contributes to the Fund having sufficient assets to cover the accrued benefits, and enables employer contributions to be kept as stable as possible.

The investment strategy takes into account the following beliefs:

- A long term approach to investment will deliver better returns
- The long term nature of LGPS liabilities allows for a long term investment horizon
- Asset allocation is the most important factor in driving long term investment returns
- Liabilities influence the asset structure; funds exist to meet their obligations
- Risk premiums exist for certain investments; taking advantage of these can help to improve investment returns
- Markets can be inefficient, and mispriced for long periods of time; therefore there is a place for active and passive investment management
- Diversification across investments with low correlation improves the risk/return profile
- Secure and growing income streams underpin the ability to meet future liabilities
- Responsible investment can enhance long term investment performance
- Investment management costs should be minimized where possible but net investment returns after costs are the most important factor

Strategic Asset Allocation Benchmark

The Committee aims to balance risk and reward by apportioning the Fund's assets over a range of asset classes to achieve the Fund's goals, to manage risk and to match the investment horizons. The objective is to generate a return that is at least equal to the

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investment return assumed by the actuary in the actuarial valuation. The assumed investment return is used by the actuary to 'discount' the Fund's liabilities to a present day value. The actuarial valuation at 31 March 2019 was prepared on the basis of an investment return of **3.6%** over the next 20 years.

For the longer term, the assumed investment return beyond 20 years is expressed as a margin above long term 'risk free' interest rates. The margin represents the excess return that should be available to the Fund from investing in riskier assets (e.g. equities) and is known as the asset outperformance assumption (AOA).

At the 31 March 2019 valuation, the AOA was 1.8% over a long term UK bond yield of 1.5% giving a longer term investment assumption of **3.3%.** The 31 March 2016 valuation was prepared on the basis of a single discount rate of 4% (1.8% AOA & long term UK bond yield of 2.2%). The lower discount rates used for the March 2019 valuation reflects lower expected investment returns going forward.

The Strategic Asset Allocation Benchmark (the Benchmark) for the Fund has been formulated in consultation with Anthony Fletcher, following the completion of the 2019 triannual valuation conducted by Hymans Robertson, the Fund's actuary. The Benchmark takes into account the required level of return and an appropriate balance between generating long term investment returns and exposure to investment risk. The Benchmark includes a wide variety of asset classes, in order to diversify sources of risk and return, and equity allocations spread by geographic regions. It takes into account the future expected returns from the different asset classes, the historic levels of volatility of each asset class and the level of correlation between the asset classes.

The Fund's asset classes are allocated into three categories:

- Growth Assets: largely equities, plus other volatile higher return assets such as private equity
- Income Assets: assets which are designed to deliver an excess return, but with more stable return patterns than Growth Assets because income represents a large proportion of the total return of these assets
- Protection Assets: lower risk government or investment grade bonds, together with cash

The asset allocation of the Fund is reviewed on a quarterly basis, and tactical positions around the Benchmark are agreed by the Committee following advice from the Fund's in-house investment managers and the Fund's Independent Adviser.

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Derbyshire Pension Fund

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The Fund’s Final Benchmark, together with an Intermediate Benchmark designed to allow the Fund to manage the transition risk towards the Final Benchmark, is set out in the following table:

Asset Category	Intermediate Asset Allocation	Intermediate Permitted Range	Final Asset Allocation	Final Permitted Range	Performance Benchmark
Growth Assets	**56.0%**	**+/- 8%**	**55.0%**	**+/- 8%**	
Total Quoted Equities	*52.0%*	*+/- 8%*	*51.0%*	*+/- 8%*	
-UK Equities	14.0%	+/- 6%	12.0%	+/- 4%	FTSE All Share
-North America	6.0%	+/- 6%	-	-	FTSE World N America
-Europe	4.0%	+/- 4%	-	-	FTSE AW Developed Europe Ex-UK Net
-Japan	5.0%	+/- 2%	5.0%	+/- 2%	FTSE World Japan
-Pacific ex-Japan	2.0%	+/- 2%	-	-	FTSE All World Asia-Pacific ex Japan
-Emerging Markets	5.0%	+/- 2%	5.0%	+/- 2%	FTSE Emerging Markets
-Global Sustainable	16.0%	+/- 16%	29.0%	+/- 8%	FTSE All World
Private Equity	4.0%	+/- 2%	4.0%	+/- 2%	FTSE All Share + 1%
Income Assets	**24.0%**	**+/- 6%**	**25.0%**	**+/- 6%**	
Property	9.0%	+/- 3%	9.0%	+/- 3%	IPD UK Quarterly Property Index
Infrastructure	9.0%	+/- 3%	10.0%	+/- 3%	LIBOR 3m + 2%
Multi-Asset Credit	6.0%	+/- 2%	6.0%	+/- 2%	40% Libor 3m + 3% / 30% ICE BofA Global High Yield Index, GBP / 30% S&P & LSTA Leveraged Loan Index, GBP
Protection Assets	**20.0%**	**+/- 5%**	**20.0%**	**+/- 5%**	
Fixed Income	6.0%	+/- 2%	6.0%	+/- 2%	FTSE UK Gov Fixed All Stocks
Index Linked Bonds	6.0%	+/- 2%	6.0%	+/- 2%	FTSE UK I-L All Stocks
Global Non-Government Bonds	6.0%	+/- 2%	6.0%	+/- 2%	50% ICE GBP Non-Gilt Index (ex EM) / 50% ICE Global Corporate Index (ex GBP and EM), hedged to GBP Base
Cash	2.0%	0 - 8%	2.0%	0 - 8%	Sterling 7 Day LIBID
Total	**100.0%**		**100.0%**		

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The Intermediate Benchmark is expected to come into effect on 1 January 2021, with the Final Benchmark expected to come into effect on 1 January 2022 at the latest.

Asset Classes

All financial instruments are open to consideration by the Committee. The Fund currently invests in quoted and unquoted securities of UK and overseas markets, including equities, government and non-government bonds, multi-asset credit, property, infrastructure and cash, either directly or via pooled vehicles. Derivatives are used to hedge the currency exposure of the overseas government bond holdings. The use of derivatives may be extended further in the future for the purpose of efficient portfolio management or to hedge other specific risks. The introduction of any new financial instrument/asset class or any extended use of derivatives will only be considered by the Committee following the receipt of appropriate training and advice from suitably qualified persons.

Growth Assets

Equities

Equities are classed as growth assets with the potential to provide returns in excess of inflation from growth in both capital values and income. Reinvested income accounts for a large proportion of long term equity returns. As equity returns are linked to company revenues and profits, investing in equities increases exposure to volatility. Investors expect to be compensated for that volatility by higher returns.

Over the last 50 years, in the UK, equities have provided a real return (after inflation) of 5.3% pa, compared with a real return of 3.4% pa from long dated government bonds and 1.0% pa from cash. Over the last 20 years, the respective real returns were 1.8% pa, 3.1% pa and -0.3% pa. In the US, the real returns over the last 50 years were 6.1% pa from equities, 4.1% pa from 20 year government bonds and 0.7% pa from cash. US respective real returns over 20 years were 3.8% pa, 4.8% pa and -0.5% pa.[1] Despite the increasing correlation between the majority of developed equity markets, investing in selected different geographic regions still provides portfolio diversification and investing in emerging markets generally provides access to higher economic growth rates and exposure to different economic drivers of return.

[1] *Source: Barclays Equity Gilt Study 2020*

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Private Equity

Private equity investment refers to investment in unquoted, privately owned companies. Investors expect to receive an illiquidity premium for investing in this asset class and target returns above those expected from publicly quoted equities. Returns from private equity primarily come from capital growth, rather than income when investments are exited (realised) following a period of business growth/transformation. Private equity offers access to a broader universe of companies than the publicly quoted space.

Income Assets

Property

Property investments have traditionally been split between three different sectors: office; retail and industrial. Increasingly within the asset management industry, exposure to niche sectors such as student accommodation and exposure to debt secured against property assets is also included within the property asset class. Returns from this asset class come from rental income and the change in market values. Rental income has accounted for a large proportion of total returns over the long term. Given the relative stability of rental income, which gives property bond like characteristics, the returns from property are generally expected to fall between the returns from equities and those from bonds.

Property investment can be carried out directly via the purchase of physical properties or indirectly via the purchase of pooled vehicles or property company shares. The majority of the Fund's property exposure is gained via direct investment; pooled vehicles are used to gain exposure to niche sectors and overseas assets. The Fund's exposure to property debt is currently contained within the allocation to corporate bonds.

Infrastructure

Infrastructure offers access to long term predictable cash flows, which are often linked to inflation. A low correlation to the business cycle and the other major asset classes provides diversification benefits and long investment horizons. The majority of the Fund's infrastructure investments are in developed European core assets (long term assets with regulated returns) and social PFI concessions (typically schools, hospitals and military accommodation).

Multi-Asset Credit

Multi-asset credit typically relates to sub-investment grade corporate bonds and includes private debt, high yield debt and asset-backed securities. Multi-Asset Credit offers a predictable income stream and a yield pick-up relative to sovereign bonds and investment grade corporate bonds reflecting the increased risk of default.

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Protection Assets

Sovereign & Corporate Bonds

Bonds offer predictable streams of income and predictable returns if held to maturity. They are held as stabilising assets to reduce volatility and to provide diversification. As pension funds mature they can be used to provide liquidity and to match liabilities as they fall due.

The Fund holds conventional fixed income, index-linked and investment grade corporate bonds. Index linked bonds are regarded as a particularly good match for pension fund liabilities. The majority of the Fund's government bond holdings are issued by the government of the United Kingdom; the currency exposure of any overseas sovereign bonds holdings is hedged to sterling.

Cash

Cash management for the Fund comprises cash held in the Fund's cash accounts (i.e. bank and money market funds) and cash held in the custodian's bank account in respect of segregated mandates.

The Fund holds cash to fulfil its daily liquidity requirements, and depending on market conditions, also as a protection asset. The Fund's cash balances are managed by Derbyshire County Council's Treasury Management Team in line with the Fund's annual Treasury Management Strategy.

Each of the Fund's segregated mandates has a cash account with the Fund's custodian. Cash in these accounts is held primarily for the investment managers' day to day liquidity requirements and fluctuates depending on trading activity and dividend income. Each segregated mandate includes a maximum cash limit.

Risk

The overall risk for the Fund is that its assets will be insufficient to meet its liabilities. The Funding Strategy Statement, which is drawn up following the triennial actuarial valuation of the Fund, sets out how any deficit in assets compared with liabilities is to be addressed.

Underlying the overall risk, the Fund is exposed to demographic risks, regulatory risks, governance risks and financial risks (including investment risk). The measures taken by the Fund to control these risks are included in the Funding Strategy Statement and are reviewed periodically by the Committee via the Fund's risk register. The primary investment risk is that the Fund fails to deliver the returns anticipated in the actuarial valuation over the long term. The Committee anticipates expected market returns on a prudent basis to reduce the risk of underperforming expectations.

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It is important to note that the Fund is exposed to external, market driven, fluctuations in asset prices which affect the liabilities (liabilities are partially estimated with reference to government bond yields) as well as the valuation of the Fund's assets. Holding a proportion of the assets in government bonds helps to mitigate the effect of falling bond yields on the liabilities to a certain extent. Further measures taken to control/mitigate investment risks are set out in more detail below:

Concentration

The Committee manages the risk of exposure to a single asset class by holding different categories of investments (e.g. equities, bonds, property, alternatives and cash) and by holding a diversified equity portfolio, spread by both geography and market sectors. Each asset class is managed within an agreed permitted range to ensure that the Fund does not deviate too far away from the Benchmark, which has been designed to meet the required level of return with an appropriate level of exposure to risk, taking into consideration the level of correlation between the asset classes.

Volatility

The Benchmark contains a high proportion of equities with a commensurate high degree of volatility. The strong covenant of the major employing bodies enables the Committee to take a long term perspective and to access the forecast inflation plus returns from equities.

Performance

Investment managers are expected to outperform the individual asset class benchmarks detailed in the overall Strategic Asset Allocation Benchmark. The Fund's performance is measured by an independent provider and reported to the Committee on a quarterly basis. The Committee takes a long term approach to the evaluation of investment performance, but will take steps to address persistent underperformance.

Liquidity

Close attention is paid to the Fund's projected cash flows; the Fund is currently cash flow positive, in that annually there is an excess of cash paid into the Fund from contributions and investment income after pension benefits are paid out. The Fund expects to be cash flow positive for the short to medium term. Despite the growing proportion of illiquid investments in the Fund, a large proportion of the assets are held in liquid assets and can be realised quickly, in normal circumstances, in order for the Fund to pay its immediate liabilities.

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Currency

The Fund's liabilities are denominated in sterling which means that investing in overseas assets exposes the Fund to a degree of currency risk. The Committee regards the currency exposure associated with investing in overseas equities as part of the return on the overseas equities; the currency exposure in repect of the Fund's Income Assets and Protection Assets is hedged back to sterling.

Stock Lending

The Fund does not currently participate in any standalone stock-lending arrangements. As part of the LGPS Central pool, the funds managed by LGPS Central Limited do participate in stock-lending arrangements, and LGPS Central Limited has put controls are in place to protect the security of the Fund's assets.

Custody

The risk of losing economic rights to the Fund's assets is managed by the use of a global custodian for custody of the assets, regular scrutiny of the Fund's providers, and the maintenance of independent investment accounting records.

LGPS Central Pool

Derbyshire Pension Fund is part of the LGPS Central Pool (the Pool) with the LGPS funds of Cheshire, Leicestershire, Nottinghamshire, Shropshire, Staffordshire, West Midlands and Worcestershire. The Pool has been established in accordance with Government requirements for the pooling of LGPS investment assets. Collective investment management offers the potential for substantial savings in investment management fees, increased opportunities for investor engagement and access to a shared pool of knowledge and expertise.

The eight administering authorities of the pension funds within the LGPS Central Pool are equal shareholders in LGPS Central Limited. LGPS Central Limited (the Company) has been established to manage investments on behalf of the Pool, and received authorization from the Financial Conduct Authority in January 2018. The Company launched its first sub-funds within an Authorised Contractual Scheme collective investment vehicle in April 2018, and has launched several additional sub-funds since that date.

The transition of the Fund's assets into products offered by the Company is likely to take several years. In February 2019, the Fund transitioned its Non-Government Bond portfolio into the LGPS Central Global Active Investment Grade Corporate Bond Multi Manager Fund. LGPS Central Limited also provides the Fund with general advisory services in respect of the Fund's Japanese and Asia-Pacific Ex-Japan Equity portfolios. Responsibility

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for determining the Strategic Asset Allocation Benchmark and the tactical quarterly asset allocation positions remains with the Fund.

Robust governance arrangements have been established both within the Company and within the wider Pool to ensure that the Company operates effectively and meets the objectives of the pension funds within the LGPS Central Pool.

A Joint Committee, set up in accordance with provisions of the Local Government Act 1972, provides oversight of the delivery of the objectives of the Pool, the delivery of client service, the delivery against the LGPS Central Pool business case and deals with common investor issues.

A Shareholders' Forum, comprising one shareholder representative from each of the participating administering authorities, oversees the operation and performance of LGPS Central Limited and represents the ownership rights and interests of the shareholding councils within the LGPS Central Pool.

To support the Joint Committee and the Shareholders' Forum, a Practitioners' Advisory Forum has been created, consisting of Officers from each of the shareholding councils within the Pool. This forum provides day-to-day oversight of the Operator, scrutinizing the delivery of products, investment performance and investment costs, monitoring customer service and the delivery of wider investor services, such as voting and responsible investment.

Responsible Investment

The Fund's approach to responsible investment, together with the management of climate-related risks and oppourtunities, are set out in the Fund's Responsible Investment Framework and Climate Strategy. Copies of the Fund's Responsible Investment Framework and Climate Strategy can be found on the Fund's website at [link]

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MJ HUDSON
Allenbridge

Review of the Investment Strategy Statement

PREPARED FOR:

Derbyshire Pension Fund: Pensions and Investments Committee

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Review of the Investment Strategy Statement for Derbyshire Pension Fund

This report has been prepared by Anthony Fletcher, the "External Investment Adviser" of the Derbyshire Pension Fund (the Fund). The review was undertaken at the request of Derbyshire County Council as the Administering Authority for the Derbyshire Pension Fund.

The Fund is required by regulation to have an Investment Strategy Statement (ISS) in place, and to review it following any material change in the factors which are judged to have a bearing on the stated investment policy and at least every three years as required by the Regulations.

The Fund's ISS has been drawn up to be in compliance with Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 ("the Regulations"), as updated by the Department for Communities and Local Government most recently in July 2017. It has been prepared subject to consultation with such persons as Derbyshire County Council considers appropriate.

Anthony Fletcher's role is to provide an independent review of the ISS and to make suggestions for changes that may be considered in light of the regulations and the investment objectives of the Fund.

Meeting date 9th September 2020
Date of paper 31st August 2020

At the request of Derbyshire County Council as the Administering Authority for the Derbyshire Pension Fund, I have carried out a review of the Investment Strategy Statement, the Responsible Investment Framework and the Climate Strategy and to the best of my knowledge, I have found them to be consistent with the objectives of the Derbyshire Pension Fund and compliant with the regulations as set out in Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2017.

Statutory background

Regulation 7(1) requires an administering authority to formulate an investment strategy which must be in accordance with guidance issued by the Secretary of State.

The Investment Strategy Statement required by Regulation 7 must include: -

a) A requirement to invest money in a wide variety of investments;

b) The authority's assessment of the suitability of particular investments and types of investments;

c) The authority's approach to risk, including the ways in which risks are to be measured and managed;

d) The authority's approach to pooling investments, including the use of collective investment vehicles and shared services;

e) The authority's policy on how social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and

f) The authority's policy on the exercise of rights (including voting rights) attaching to investments.

The Investment Strategy Statement must also set out the maximum percentage of the total value of all investments of fund money that it will invest in particular investments or classes of investment. This, in effect, replaces Schedule 1 to the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 ("the 2009 Regulations").

Under Regulation 7(6) and (7), the statements must be published by 1st April 2017 and then kept under review and revised from time to time and at least every three years.

Further to my statement above, I note that the Fund's Investment Strategy Statement and Responsible Investment Framework addresses all the requirements set out in the regulations.

Background

As part of the ongoing need to ensure the Derbyshire Pension Fund's Investment Strategy Statement (ISS) remains inline with the long term objectives of the Fund, the inhouse investment team and I have reviewed the ISS and the Strategic Asset Allocation Benchmark which were last updated in the fourth quarter of 2018.

The new ISS takes into consideration the output of the Triennial Valuation report produced by Hymans Robertson, based on the Fund's position at 31st March 2019 and developments in the medium and long term trends seen in the investment and securities markets.

As part of its fiduciary responsibility, the Fund has always taken into consideration all the factors which may influence the risk and reward opportunity and the probability of delivering sustainable and stable long term returns through a diversified portfolio of investments.

In conducting this review, the inhouse team have in the interests of improved communication and transparency created 2 new documents outside of the ISS, namely; the Responsible Investment Framework (RIF) and the Climate Strategy (CS). The RIF focuses on the Fund's policy on Environment, Social and Governance and how these factors can influence risk and reward, the CS specifically focuses on the risks arising from climate change and how the Fund will seek to measure and mitigate these risks. The new RIF and CS work in tandem with the ISS and the Funding Strategy Statement (FSS), thereby aligning the Fund's investment beliefs, processes and long term objectives with its fiduciary duty.

The Fund's new RIF is an extension and update of the previous framework that was in the past included as a section within the ISS. The new RIF is, like the ISS, consistent with the requirements of the relevant regulations and statutory guidance. While it is a requirement that the Fund has its own policies on responsible investment, it is important to collaborate with its pooling partners and LGPS Central Ltd to have a consistent approach to certain agreed themes to achieve effective engagement and stewardship. These themes are noted in section 8 of the document. Like the RIF itself, these themes are subject to ongoing monitoring and will be reviewed as required or at least every 3 years.

In recognition of the importance of climate change and the impact this could have on investments, the inhouse team have also created a new policy document that formally sets out the Fund's approach to incorporating the implications of climate change into the Fund's investment processes. Again, a consideration of climate change is not new, the inhouse team and its asset managers as long term investors have always taken into consideration any factor that may have an influence on the long term sustainability of an investment.

The new CS document clearly sets out the objectives of the Fund and the actions it will take to achieve those objectives, while recognising that the variation, relevance and quality of, the data on climate impact currently available can be of poor quality and in some cases inconsistent. Despite the issues around data, the Fund has pledged, based on the current metrics available, to seek to reduce the carbon impact of its investments over a reasonable period of time. As the quality of data and the standardisation of reporting improves it should become easier to fulfil the climate strategy objectives.

As well as incorporating the updated policies on responsible investment and climate change, the review has taken into consideration the Triennial Valuation and the future expected returns and volatility of different asset classes.

The Triennial Valuation contained some good news, as a result of the strong investment returns achieved since the last valuation in 2016, the funding level has improved from 87% to 97%. This means the shortfall in the value of assets needed to meet the pensions of scheme members has fallen significantly. This improvement means that the Fund could consider taking a lower level of investment risk in future and still be expected to meet its obligations. This is consistent with the approach of the actuary who has reduced the future expected investment return from 4% pa (in 2016) to 3.6% pa over the next 20 years and only 3.3% pa thereafter.

Changes to the Strategic Asset Allocation Benchmark

The improvement in the funding level means that the Fund can continue on the path of reducing exposure to higher volatility Growth Assets from 57% to 55% and increase its exposure to Income Assets from 23% to 25%. The change will be used to increase the allocation to Infrastructure, where returns are often inflation linked and contractual in nature which should improve the overall probability of achieving the total return target. No change to the exposure to Protection Assets is being suggested at this time.

Growth Assets 55%: The overall allocation is only being reduced slightly from 57% to 55% and there is no change in the 4% allocation to Private Equity, however within the allocation to publicly listed equity there are some significant changes that will need to be phased in over time. It is proposed that the allocation to UK equity is reduced from 16% to 12% and the allocations: 8% Europe ex-UK, 12% North America and 4% Pacific ex-Japan are reduced to 0% with the allocation to Global Sustainable Equity increasing from 3% to 29%. The genuine diversifiers of Japan and Emerging Market equity will remain at 5% each. Substituting the regional allocations for an allocation to global equity looks significant but drilling down into the global benchmark index reveals a similar distribution of regions and allows Derbyshire's fund managers more scope to be dynamic in terms of their regional allocations.

Income Assets 25%: This category consists of Property, MAC and Infrastructure. The 2% reduction in Growth Assets noted above has been deployed to Infrastructure increasing the allocation from 8% to 10%. It is also proposed that the overall allocation to Property remains unchanged but indirect investments are reduced by 1% and direct investments increased by 1%. Like the changes to the mix of equity above, these changes will be phased in over time to give the managers time to get invested. It is also proposed that non sterling denominated income assets should be currency hedged just as they are for protection assets.

Protection Assets 20%: The weight and mix of protection assets remains unchanged. I believe it is prudent to have some allocation to both Gilts and Index Linked Gilts because of their proven diversification characteristics, despite their extremely low expected returns and my belief that at the current level of yield they will not provide as much protection as they have in the past.

Strategic Asset Allocation, Permitted Ranges and Performance Benchmarks

The revised Strategic Asset Allocation is set out on table 1 below, it is proposed that because of the magnitude of the changes to equity allocation and the time needed for the infrastructure and property managers to get invested that the new Strategic Asset Allocation Benchmark is phased in over time. With an intermediate stage from January 2021 and the final new benchmark in place by January 2022.

Table 2 shows the final revised Strategic Asset Allocation, performance benchmarks and permitted ranges for tactical asset allocation expected to be in place from January 2022.

The Fund's liabilities are exclusively denominated in UK pounds. It is therefore prudent to have some exposure to investment assets that are denominated in UK pounds and benchmarked in the UK and to increase the proportion of overseas assets that are currency hedged. However, it is also reasonable for reasons of diversification of risk and return to have exposure to assets which are denominated in other currencies, located in other geographic regions and in sectors that may not be available in the UK. The decision to increase the exposure to global sustainable equity should increase the Fund's level of diversification and dynamic asset allocation between regions and is consistent with the revised Responsible Investment Framework and the Climate Strategy. I therefore support the Fund's change in Strategic Asset Allocation from regional to predominantly global equity as it should widen the range of asset classes, geographies and sectors available for investment.

Over the last 10 years, all equity markets have produced strong relative returns, but it is expected that over the next 10 to 15 years, the returns from developed equity markets, in particular, may be lower and, as recently demonstrated, the volatility of those returns could be higher. Reducing risk by having a lower total weight, together with further diversification within equity, as well as a higher allocation to Income Assets rather than Growth Assets, is a reasonable approach.

Over the last 30 years, bonds have produced high levels of total return as interest rates and inflation have fallen. As a result, nominal and real government bond yields have fallen to very low levels and are probably at their lower boundary. While bonds provide excellent diversification characteristics and predictable cash flows, from a strategic point of view, I believe it is appropriate maintain the current low weight to government bonds.

The decision to increase the exposure to Income Assets and to Infrastructure in particular is a good idea for several reasons. This is an asset class which also derives more of its total return from income rather than growth. Infrastructure investment can provide diversification benefits to traditional asset classes, the cash flows generated by infrastructure are contractual, long term and often inflation linked making them consistent with the long term objectives of a pension fund.

MJ HUDSON
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Table 1. Changes in the Strategic Asset Allocation Benchmark (SAAB) over time.

Asset Class	Current SAAB 1st January 2019	Proposed Intermediate SAAB January 2021	Proposed Final SAAB expected January 2022	Final Change
UK Equities	16.0%	14.0%	12.0%	(4.0%)
North American Equities	12.0%	6.0%	-	(12.0%)
European Equities	8.0%	4.0%	-	(8.0%)
Japanese Equities	5.0%	5.0%	5.0%	-
Asia Pacific Ex-Japan Equities	4.0%	2.0%	-	(4.0%)
Emerging Market Equities	5.0%	5.0%	5.0%	-
Global Sustainable Equities	3.0%	16.0%	29.0%	26.0%
Private Equity	4.0%	4.0%	4.0%	-
Growth Assets	**57.0%**	**56.0%**	**55.0%**	**(2.0%)**
Infrastructure	8.0%	9.0%	10.0%	2.0%
Multi-Asset Credit	6.0%	6.0%	6.0%	-
Direct Property	5.0%	6.0%	6.0%	1.0%
Indirect Property	4.0%	3.0%	3.0%	(1.0%)
Income Assets	**23.0%**	**24.0%**	**25.0%**	**2.0%**
Conventional Bonds	6.0%	6.0%	6.0%	-
Index-Linked Bonds	6.0%	6.0%	6.0%	-
Corporate Bonds	6.0%	6.0%	6.0%	-
Cash	2.0%	2.0%	2.0%	-
Protection Assets	**20.0%**	**20.0%**	**20.0%**	**-**
Total	**100.0%**	**100.0%**	**100.0%**	**-**

Table 2. Final Strategic Asset Allocation, Permitted Ranges and Performance Benchmarks. January 2022

% Asset Category	Asset Allocation	Permitted Range	Performance Benchmark
Growth Assets	**55.0**	**+/- 8**	
Total Equities	51.0	+/- 8	
UK Equities	12.0	+/- 4	FTSE All Share
Japan	5.0	+/- 2	FTSE World Japan
Emerging Markets	5.0	+/- 2	FTSE Emerging Markets
Global Sustainable	29.0	+/- 8	FTSE All World
Private Equity	4.0	+/- 2	FTSE All Share + 1%
Income Assets	**25.0**	**+/- 6**	
Property	9.0	+/- 3	IPD UK Quarterly Property Index
Infrastructure	10.0	+/- 3	LIBOR 3m + 2%
Multi-Asset Credit	6.0	+/- 2	40% Libor 3m + 3% / 30% ICE BofA Global High Yield Index, GBP / 30% S&P & LSTA Leveraged Loan Index, GBP
Protection Assets	**20.0**	**+/- 5**	
Government Bonds	6.0	+/- 2	FTSE UK Government Fixed All Stocks
Inflation Linked Bonds	6.0	+/- 2	FTSE UK Index-Linked All Stocks
Non-Government Bonds	6.0	+/- 2	50% ICE GBP Non-Gilt Index (ex EM) / 50% ICE Global Corporate Index (ex GBP and EM), hedged to GBP Base
Cash	2.0	0 - 8	Sterling 7 Day LIBID
Total	**100.0%**		

I have reviewed the asset categories, % allocation, permitted ranges and performance benchmarks in the table above and find them both prudent and reasonable from the point of view of the Fund's objectives and my understanding of the regulations.

Anthony Fletcher

External Investment Adviser

31st August 2020

Appendix

References

Source material was provided by, including but not limited to, the following suppliers: -

Derbyshire Pension Fund.

Ministry for Housing, Communities and Local Government: -

Local Government Pension Scheme

Guidance on Preparing and Maintaining an Investment Strategy Statement

July 2017.

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Agenda Item No. 4 (e)

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

9 September 2020

Report of the Director of Finance and ICT

DERBYSHIRE PENSION FUND EXIT CREDITS POLICY

1 Purpose of the Report

To advise the Pensions and Investments Committee (Committee) of the outcome of Derbyshire Pension Fund's consultation exercise in respect of the proposed Exit Credits Policy (the Policy) and to seek approval for the updated Policy attached as Appendix 1.

2 Background

Exit Credits

The Local Government Pension Scheme Regulations 2013 were amended in 2018 to allow exit credits to be paid for the first time. The changes came into effect on 14 May 2018 but were backdated to 1 April 2014.

Where an employer ceased to be a participating employer in the Local Government Pension Scheme (LGPS), an exit credit became due if their pension liabilities had been overfunded at their date of exit. (An employer typically ceases to be a participating employer when their last active member of the LGPS leaves or when an admission body's admission agreement comes to an end e.g. on expiry on a contract.)

Following an MHCLG consultation exercise in May 2019, updated regulations with respect to exit credits came into force on 20 March 2020, but had effect from 14 May 2018. The new regulations required administering authorities of LGPS pension funds to determine, at their discretion, the amount of any exit credit payment due, having regard to any relevant considerations.

The new responsibility placed on the administering authority for determining the level of any exit credit, and the discretion available, makes it essential that the Fund adopts a fair and reasonable exit credits policy which:

- ensures that a consistent approach is taken between employers and over time
- aims to protect the interests of the members and employers as a whole
- ensures that representations from all interested parties are taken into account
- is consistent with the approach set out in the Fund's Funding Strategy Statement and Admission, Cessation & Bulk Transfer Policy
- takes into account relevant actuarial and legal advice

Consultation

Given the potential impact on participating employers of the Fund's exercise of its discretion in relation to exit credits, the Fund consulted with scheme employers, the local pension board and other stakeholders on the proposed policy.

An email was sent to the Fund's current scheme employers, to the recently ceased employers and to members of Derbyshire Pension Board to highlight the consultation. The consultation was also featured on the news page of the Fund's website. Two responses to the consultation were received, both from scheme employers.

The first response questioned whether the Fund would ever use its discretion to determine an exit credit in favour of an exiting contractor. The second response expressed concern about possible assumptions that may be made by the Fund regarding the negotiation of contracts that supported admissions to the Fund between 14 May 2018 and 20 March 2020.

The Policy is clear that the Fund will review each case on its own merits and that representations from exiting employers, and, where applicable, from any body that has acted as a guarantor for the employer's pension liabilities (in many cases this will be the letting authority) will form part of the exit credit determination.

The Director of Finance and ICT, in conjunction with the Chair of Committee, determined that no changes were necessary to the Policy that was approved on 21 July 2020 as a result of feedback to the consultation.

The Policy has, however, been revised to clarify that any costs associated with the determination of an exit credit may be deducted from any exit credit payment at the Fund's discretion. This point was raised by a member of Committee when the proposed Policy was considered at the last meeting. The proposed revision to the Policy is highlighted in blue.

4 Other Considerations

In preparing this report the relevance of the following further factors has been considered: financial, legal, human rights, human resources, equality and diversity, health, environmental, transport, property, social value and prevention of crime and disorder.

5 Background Papers

All background papers are held by the Head of Pension Fund.

6 Officer's Recommendation

That the Committee approves the proposed Exit Credits Policy attached as Appendix 1.

Peter Handford

Director of Finance and ICT

Appendix 1

Derbyshire Pension Fund Exit Credits Policy

Introduction

The Local Government Pension Scheme Regulations 2013 (the 2013 Regulations) were amended in 2018 to allow exit credits to be paid for the first time. The amendment came into effect on 14 May 2018 but had retrospective effect back to 1 April 2014. Further amendment regulations came into force on 20 March 2020 which were also deemed to have effect from 14 May 2018.

If an employer becomes an exiting employer under Regulation 64 of the 2013 Regulations, it may be entitled to receive an exit credit if its pension liabilities have been overfunded at its date of exit.

Exit Valuation

When an employer becomes an exiting employer, Derbyshire Pension Fund (the Fund) must obtain from the Fund actuary:

1. an actuarial valuation as at the exit date of the liabilities of the Fund in respect of benefits in respect of the exiting employer's current and former employees

2. a revised rates and adjustments certificate showing the exit payment due from the exiting employer; or the excess of assets in the Fund relating to that employer over its liabilities as calculated by the valuation

When commissioning the valuation from the actuary, the Fund will also request the actuary to confirm the proportion of any excess of assets which has arisen because of the value of the employer's contributions. This a factor the Fund must have regard to when making its determination as to the amount of the exit credit.

Notification

The Fund will notify its intention to make a determination on whether to pay an exit credit to:

- the exiting employer
- where the exiting employer is a ‘transferee’ admission body, the scheme employer in connection with that body (i.e. the letting authority)
- where the exiting employer is an admission body of any type, any other body that has given a guarantee in respect of the admission body

Determination
In accordance with Regulation 64 (2ZAB) of the 2013 Regulations (as amended), Derbyshire Pension Fund (the Fund) will determine the amount of any exit credit (which may be zero) taking into account the following factors:

- the extent to which the exiting employer's assets in the Fund are in excess of its liabilities (in relation to benefits in respect of the exiting employer's current and former employees)
- the proportion of this excess of assets which has arisen because of the value of the exiting employer's contributions
- any representations made by the exiting employer and, where the employer participates in the scheme by virtue of an admission agreement, any body that has acted as a guarantor for the employer's pension liabilities (in many cases this will be the letting authority)
- any other relevant factors

In determining whether an exit credit may be payable, Derbyshire Pension Fund, will review each case on its own merits and will apply the following guidelines:

1. For pre -14 May 2018 admissions, the Fund will take into account the fact that original commercial contracts between admission bodies and letting authorities/guarantors could not have been drafted with regard to the May 2018 regulation changes that implemented exit credits retrospectively. Subject to any representations to the contrary, it will be assumed that the employer priced the contract accordingly and that no subsequent agreements covering the ownership of exit credits have been negotiated.

2. The basis for calculating an employer's pension liabilities to determine the level of any exit credit, will generally be as set out in the Fund's Funding Strategy Statement.

3. No exit credit will be payable to an admission body which participates in the Fund via an agreed fixed contribution rate throughout its participation in the Fund as in this case the pensions risk 'passes through' to the letting authority.

4. The Fund may undertake an exit credit calculation which reflects any contractual pension risk sharing provisions between the exiting employer, the letting authority/guarantor and/or any other relevant body with respect to pension risk sharing. This information, including confirmation of which party is responsible for which funding risk should be provided to the administering authority within one month of the exiting employer ceasing participation in the Fund.

5. Where a guarantor or similar arrangement is in place, but no formal risk sharing arrangement exists, the Fund will take into consideration how the approach to setting contribution rates payable by the employer during its participation in the Fund reflects which party is responsible for funding risks. This may inform the determination of the value of any exit credit.

6. If an employer leaves on the ‘gilts exit basis’ as set out in the Funding Strategy Statement, any exit credit will normally be paid in full to the employer, subject to consideration of the individual circumstances.

7. If an admission agreement ends early, the Fund will consider the reason for the early termination, and whether that should have any relevance on the Fund’s determination of the value of any exit credit payment.

8. If a scheduled body or resolution body becomes an exiting employer due to a reorganisation, merger or take-over, no exit credit will generally be paid.

9. If there is any doubt about the applicable LGPS benefit structure at the date of exit (e.g. McCloud remedy), the Fund’s actuary may include an estimate of the possible impact of any resulting benefit changes when calculating an employer’s pension liabilities to determine the level of any exit credit.

10. The Fund will take into account whether any outstanding contributions or other payments are due to the Fund at the cessation date. Any outstanding payments will be notified to the exiting employer and will be deducted from any exit credit payment.

11. Costs associated with the determination of an exit credit may be deducted from any exit credit payment at the Fund’s discretion.

12. The Fund will consider any representations made by the letting authority and/or any other relevant scheme employer regarding monies owed to them by the exiting employer in respect of the contract that is ceasing. Representations regarding any such outstanding payments should be made to the Fund within one month of the exiting employer ceasing participation in the Fund.

13. The Fund’s final decision will be made by the Director of Finance & ICT with advice from the Head of Pension Fund, and where necessary with advice from the Fund’s actuary, and/or legal advisors, in consideration of the guidelines set out in this policy.

14. There may be some situations which are bespoke in nature. In these situations, the Fund will take into account the factors it considers to be

relevant in determining whether an exit credit is payable, including representations from relevant parties. The Fund's decision on how to make an exit credit determination in these instances will be final.

15. The Fund will inform the exiting employer of any exit credit amount due to be paid and seek to make payment within six months of the exit date. In order to meet the six month timeframe, the Fund will require prompt notification of an employer's exit and all data and relevant information as requested. The Fund will be unable to make an exit credit payment until all the requested data and information has been received. Agreement to an extension of the timeframe will be deemed where data and information have not been provided on time.

Appeals

If a party involved in the exit credit process set out in this Policy wishes to dispute the Fund's determination, this must be routed through the Fund's internal dispute resolution procedure (application for adjudication of disagreements procedure - AADP). A copy of the AADP is available here: AADP

If the relevant party is still unhappy with the exit credit determination, having gone through all the stages of the AADP, they may be able to take a complaint to the Pensions Ombudsman.

Review

This Exit Credits Policy will be reviewed at least every three years as part of the triennial valuation process or following any relevant changes in the LGPS Regulations.

Agenda Item No. 4 (f)

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

9 September 2020

Report of the Director of Finance and ICT

MHCLG AMENDMENTS TO THE STATUTORY UNDERPIN CONSULTATION

1 Purpose of the Report

To advise the Pensions and Investments Committee (Committee) of the publication of the Ministry of Housing, Communities and Local Government's (MHCLG) consultation on draft regulations introducing proposed changes to the LGPS statutory underpin protection. The changes are intended to remove unlawful discrimination found by the Courts in relation to public service pension scheme transitional protection arrangements. The judgement of unlawful discrimination is commonly referred to as the McCloud Judgement.

To seek approval for the Director of Finance & ICT, in consultation with the Chair of the Committee, to consider the Fund's response to the consultation and to authorise its submission to MHCLG.

2 Information and Analysis

McCloud Judgement
The McCloud case relates to transitional protections given to scheme members in the judges' and firefighters' schemes which were found to be unlawful by the Court of Appeal on the grounds of age discrimination. Following the judgement, the Government announced that remedies relating to the judgement would be made in relation to all the public service pension schemes. Risks related to the McCloud judgement have been included on Derbyshire Pension Fund's (the Fund) Risk Register since May 2019.

When the LGPS benefit structure was reformed in 2014, transitional protections were applied to certain older members close to normal retirement age. The benefits accrued from 1 April 2014 by these members are subject to an 'underpin' which means that they cannot be

lower than what they would have received under the previous benefit structure.

Proposed Remedy
The draft regulations set out in the MHCLG consultation propose to:

- remove the condition that requires a member to have been within ten years of their 2008 Scheme normal pension age on 1 April 2012 to be eligible for underpin protection. Members who were active in the 2008 Scheme on 31 March 2012 and who have accrued benefits under the 2014 Scheme without a disqualifying break in service would have underpin protection, subject to aggregation requirements (members will be required to aggregate benefits to qualify for the underpin – aggregation relates to the joining together of separate LGPS employment accounts)

- extend the underpin protection to apply where a member leaves with either a deferred or an immediate entitlement to a pension (previously the underpin did not apply to leavers with a deferred benefit entitlement)

The underpin is essentially an administrative test undertaken at the earlier of the date a qualifying member leaves active service and the date they reach their 2008 Scheme normal pension age. The underpin gives the member the better of the 2014 Scheme CARE (career average revalued earnings) or 2008 Scheme final salary benefits for the eligible period of service.

The final salary for comparison purposes applies at the point that the member leaves active service or reaches age 65.

The underpin period applies between 1 April 2014 and 31 March 2022 but ceases when a member leaves active service or reaches age 65. From 1 April 2022 all service in the LGPS will be on a career average basis, with no underpin.

The changes will be retrospective which means that benefits for all qualifying leavers since 1 April 2014 will need to be reviewed to determine whether the extended underpin will produce a higher benefit. Qualifying leavers include: retirements; deferred leavers; deaths; transfers out; and trivial commutations (commutation relates to converting a ‘small’ pension entitlement into a one-off lump sump payment to be made by the Fund, effectively discharging any further liability).

Impact on Members
The MHCLG consultation sets out the likely impact of the proposed changes on the membership of the LGPS as assessed by the Government Actuary’s Department (GAD):

- older active members on 31 March 2019 are more likely to qualify for the revised underpin than younger active members
- active members between the ages of 41 and 55 as at 31 March 2019 are more likely to benefit from the revised underpin than their younger or older colleagues
- men are marginally more likely to qualify for the revised underpin and benefit to a greater extent from underpin protection than women, in line with the membership profile of the LGPS

Analysis by Hymans Robertson (Hymans), the Fund's actuary, suggests that around **1.2m** members of the LGPS, roughly equivalent to a quarter of all members, may be affected by the revised underpin. The MHCLG consultation notes that for many members the underpin protection will not result in an increase in their pension entitlement. Where an increase is applied, it is likely to be small as most members will build up a higher pension in the career average pension scheme than they would have under the final salary scheme.

Impact on Employers

Any increase in benefits for members will need to be funded by scheme employers. At a whole scheme level, Hymans estimate that total liabilities might increase by around **0.2%**, equivalent to around **£0.5bn** across the whole of the English and Welsh LGPS.

This estimate is significantly less than the **£2.5bn** quoted in the MHCLG consultation. The difference is largely due to the materially higher pay growth assumption used by GAD.

Hymans forecast that the impact of the remedy might be to increase average primary contributions by around **0.2%** of pay, with an increase in secondary contributions of around **0.1%** of pay. The actuary made an allowance for McCloud in the assessment of employer contribution rates at the 2019 actuarial valuation by increasing the required likelihood of reaching the funding target.

Whilst the impact at the whole scheme level is expected to be small, it may be material at an individual employer level.

Impact on Fund Administration

The implementation of the proposed remedy will have a significant affect on the administration of the scheme. Initial analysis had indicated that around 26,000 members of the Fund are likely to fall into the scope of the proposed changes to the underpin. The implementation of the remedy will involve:

- a review of all pension processes and communications to see which are affected by the new regulations
- engagement with the supplier of the Fund's pension administration system to discuss and influence development plans for bulk uploading and calculations related to the implementation of the McCloud remedy
- user acceptance testing on any pension administration system developments
- a comprehensive staff training exercise
- the collection of any additional data from employers needed to perform underpin calculations
- a large number of underpin calculations on an ongoing basis and as a retrospective exercise for leavers
- the payment of backdated benefit adjustments
- effective communication with scheme members and employers

Project Board
A McCloud Project Board has been established to govern the implementation of the remedy and a Project Manager has been assigned to lead the programme. The initial workstreams are:

- governance
- case identification
- staffing/resources
- communications

Further workstreams will be added as the programme progresses.

3 Consultation

The MHCLG consultation will close on 8th October 2020. The Local Government Association (LGA) and the Fund's actuary will be submitting responses to the consultation which will be shared in advance of the closing date.

The Project Board is currently working through the MHCLG consultation document and will formulate a response to the consultation in due course, taking into consideration the responses from Hymans and the LGA.

Approval is sought for the Director of Finance & ICT, in consultation with the Chair of the Committee, to consider the Fund's response to the consultation and to authorise its submission to MHCLG.

4 Other Considerations

In preparing this report the relevance of the following further factors has been considered: financial, legal, human rights, human resources, equality and diversity, health, environmental, transport, property, social value and prevention of crime and disorder.

5 Background Papers

All background papers are held by the Head of Pension Fund.

6 Officer's Recommendation

That the Committee:

I. Notes the publication of MHCLG's consultation on draft regulations introducing proposed changes to the LGPS statutory underpin protection.

II. Delegates the consideration of the Fund's response to the consultation, and the approval of its submission to MHCLG, to the Director of Finance & ICT in conjunction with the Chair of the Committee.

Peter Handford

Director of Finance and ICT

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Ministry of Housing,
Communities &
Local Government

Local Government Pension Scheme (England and Wales)

Amendments to the statutory underpin

July 2020
Ministry of Housing, Communities and Local Government

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If you have any enquiries regarding this document/publication, complete the form at http://forms.communities.gov.uk/ or write to us at:

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July 2020

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Scope of the consultation

Topic of this consultation:	This consultation seeks views on changes to the Local Government Pension Scheme in England and Wales (LGPS). It outlines proposed changes to the LGPS statutory underpin protection to remove unlawful discrimination found by the Courts in relation to public service pension scheme 'transitional protection' arrangements. Specifically, we propose to remove the condition that required a member to have been within ten years of their normal pension age on 1st April 2012 to be eligible for underpin protection. In removing the discrimination, we are proposing a number of supplementary changes to ensure the revised underpin works effectively and consistently for all members.
Scope of this consultation:	MHCLG is consulting on changes to the regulations governing the Local Government Pension Scheme (LGPS).
Geographical scope:	These proposals relate to the LGPS in England and Wales only. Separate consultation exercises will be undertaken by the relevant devolved authorities relating to the issues addressed in this consultation as they affect the local government pension schemes in Scotland and in Northern Ireland.
Impact Assessment:	Public Sector Equality Duty The Ministry of Housing, Communities and Local Government has analysed the proposals set out in this consultation document (MHCLG) to fulfil the requirements of the Public Sector Equality Duty (PSED) as set out in section 149 of the Equality Act 2010. This requires the Department to pay due regard to the need to: 1) eliminate unlawful discrimination, harassment and victimisation and other conduct prohibited by the Act 2) advance equality of opportunity between people who share a protected characteristic and those who do not 3) foster good relations between people who share a protected characteristic and those who do not. The proposals outlined here are intended to remove age discrimination, which had been found to be unlawful in the

	firefighters' and judicial pension schemes, from the LGPS rules governing the underpin. We consider that the changes proposed will significantly reduce differential impacts in how the underpin applies based on a member's age, by removing the age-related qualifying criteria found to be unlawful by the Courts in the context of the firefighters' and judicial pension schemes. Based on analysis undertaken by GAD on active membership data for the LGPS as at 31st March 2019, we anticipate that some differences in how the underpin would apply to members of different age groups would remain. These are set out separately below, along with our assessment of these differences. 1) **Qualification for the underpin -** GAD's analysis shows that older active members on 31st March 2019 would be more likely to qualify for the revised underpin than younger active members. This is principally because of our proposal that the 31st March 2012 qualifying date for underpin protection is retained. The proportion of members active in the scheme as at 31st March 2019 who had been members of the scheme on 31st March 2012 is lower for younger members, where experience shows they have a higher withdrawal rate from scheme membership. We consider that members joining the LGPS after 31st March 2012 do not need to be provided with underpin protection. Members who joined after this date will have joined the LGPS when either it had already transitioned to the career average structure (for post-1st April 2014 joiners), or when it was well publicised that the LGPS benefits were reforming. 2) **Members who benefit from the underpin** - GAD's analysis also shows that active members between the ages of 41 and 55 as at 31st March 2019 would be more likely to benefit from the revised underpin (i.e. where the calculated final salary benefit is higher than the calculated career average benefit) than their younger and older colleagues. This reflects previous experience and future expectation that: • this group are more likely than their older colleagues to experience the pay progression that would make the final salary benefit higher over the underpin period and • this group are more likely than their younger colleagues to remain in active membership until such time as they would receive the pay progression necessary for the underpin to result in an addition to their pension (e.g. through promotions and other pay increases). These differential impacts reflect the workings of a final salary scheme, and demonstrate some of the effects that can arise under that design. The Government proposes to move all local

	government pensions accrual to a career average basis, without underpin protection, from April 2022 to apply a fairer system to all future service. In relation to sex, we anticipate that, broadly, the proportion of men and women who would qualify for the revised underpin and benefit from that protection matches the profile of the scheme. This assessment is also based on analysis undertaken by GAD on active membership data for the LGPS as at 31st March 2019. Proportionally, GAD's assessment is that men would be marginally more likely to qualify for the revised underpin and to benefit to a greater extent from underpin protection than women. This reflects the fact that, in line with previous scheme experience, the average male LGPS member would be expected to have higher salary progression than the average woman and that women are generally expected to have higher voluntary withdrawal rates than men. Members with longer scheme membership and with higher salary progression would be more likely to receive an addition to their pension through the underpin (i.e. where the final salary benefit is higher). These small differential impacts also demonstrate some of the effects that can arise under a final salary design. The Government proposes to move all local government pensions accrual to a career average basis, without underpin protection, from April 2022 to apply a fairer system to all future service. Limited data specific to the LGPS in England and Wales is available in relation to other protected characteristics. However, we have considered wider data from the Labour Force Survey (Q1 2020) and the Annual Population Survey (2019) in considering these characteristics. We do not consider that the changes to underpin protection proposed in the consultation will result in any differential impact to individuals with the following protected characteristics: disability, ethnicity, religion or belief, gender reassignment, pregnancy and maternity, sexual orientation and marriage/civil partnership. Further information regarding the equalities impacts of our proposals is contained in paragraphs 111 to 127. In this consultation, we are seeking views from stakeholders on the equalities impacts of the changes proposed. These views will be considered in determining how to proceed following the consultation exercise. The potential equalities impacts of our proposals will be kept under review. A further equalities impact assessment will be

	undertaken following the consultation at the appropriate juncture. <u>Other impacts</u> The proposals in this paper are estimated to cost LGPS employers £2.5bn in the coming decades, as protected members retire and begin to receive their benefits. This estimate is based on a number of assumptions regarding the demographics of the LGPS in the years to come. Predicting whether the underpin becomes valuable in the future depends heavily on assumptions on long-term future pay growth trends. The £2.5bn estimate is based on an annual future long-term pay growth assumption of CPI+2.2%, which is the assumption used by GAD for the 2016 valuations of public service pension schemes. If annual future pay growth is less than this, the ultimate costs will be lower (and vice versa). As the LGPS is a funded scheme, employer contribution rates are set through local fund valuations and take into account a number of factors. As a result of this, it is not possible to say precisely how the proposals may impact on any individual employer's contribution rate. None of the changes contained in this consultation require a Regulatory Impact Assessment under the Small Business, Enterprise and Employment Act 2015.

Basic Information

To:	This consultation outlines details of proposed changes to the benefits of the LGPS and is particularly aimed at LGPS administering authorities, scheme members, scheme employers and their representatives. Any change to the LGPS is likely to be of interest to other stakeholders as well, such as professional advisers and local taxpayers. We welcome views on the proposals from all interested parties.
Body/bodies responsible for the consultation:	Local Government Finance Stewardship, Ministry of Housing, Communities and Local Government
Duration:	This consultation will last for 12 weeks from 16/07/2020 to 08/10/2020
Enquiries:	For any enquiries about the consultation please contact: LGPensions@communities.gov.uk
How to respond:	Please respond by email to: LGPensions@communities.gov.uk

	Alternatively, please send postal responses to: Local Government Finance Stewardship Ministry of Housing, Communities and Local Government 2nd floor, Fry Building 2 Marsham Street London SW1P 4DF When you are responding, please make it clear which questions you are responding to. Additionally, it would be very useful if you could confirm whether you are replying as an individual or submitting an official response on behalf of an organisation and include: - your name, - your position (if applicable), - the name of your organisation (if applicable), - an address (including post-code), - an email address, and - a contact telephone number.

Introduction

1. This consultation contains proposals to amend the rules governing 'transitional protection' in the LGPS, following a successful legal challenge to transitional protection arrangements in the firefighters' and judicial pension schemes.

2. In April 2014, a series of changes were made to the Local Government Pension Scheme in England & Wales (LGPS) to reform the scheme's benefits structure. These changes were implemented as part of a wider project across Government to reform public service pensions and put them on a more sustainable, affordable and fairer footing for the longer term. In the LGPS, these changes included:

- moving benefit accrual from a final salary to a career average basis, and
- linking members' normal pension age with their State Pension age (but at a minimum of 65).

3. Following negotiations with trade unions, transitional protection for members nearing retirement was implemented by the Government as part of the overall reform package and was designed to ensure that older workers had certainty and would not be any worse off as a result of the reforms made to the scheme. Transitional protection arrangements applied across public service pension schemes and in the LGPS were implemented through a statutory 'underpin'.

4. Whilst all LGPS members joined the career average scheme in April 2014, members who met certain qualifying criteria (including that they had been within ten years of their final salary scheme normal pension age on 1st April 2012) gained statutory underpin protection. Underpin protection means additional checks are undertaken for protected members with the intent of ensuring that the career average pension payable under the reformed LGPS is at least at high as the member would have been due under the final salary scheme. Where it is not as high, scheme regulations provide that an addition must be applied to the member's career average pension to make up the shortfall.

5. In the 'McCloud' and 'Sargeant' court cases (which related to the judicial and firefighters' pension schemes respectively), the Court of Appeal found that the transitional protection arrangements in those schemes directly discriminated against younger members in those schemes and this could not be objectively justified. In July 2019, the Government confirmed its view that the ruling had implications for all the main public service pension schemes, including the LGPS, and that the discrimination would be addressed in all the relevant schemes, regardless of whether members had lodged a legal claim.

6. This consultation sets out how MHCLG propose to amend the statutory underpin to reflect the Courts' findings in these cases. Primarily, we propose to remove the age requirements from the underpin qualification criteria. However, we are also proposing additional changes to ensure that the underpin works effectively and consistently for all qualifying members following the extension of the underpin to younger members. From April 2022, it is proposed that the period of underpin protection will cease and all active LGPS members will accrue benefits in the career average scheme, without a continuing final salary underpin.

7. Views from respondents are sought on questions 1 to 29 as well as on the draft regulations attached as annex B.

Background

Public service pension reform and transitional protection

8. In April 2014 and April 2015 the Government introduced reformed public service pension schemes. The changes followed a fundamental structural review by the Independent Public Service Pension Commission (IPSPC), chaired by Lord Hutton of Furness.

9. The Government commissioned the review because the cost of providing the schemes had increased significantly over the previous decades, with most of this increase falling to the taxpayer. At the same time, occupational pension provision in the private sector had changed significantly; employers were increasingly moving away from offering defined benefit pension schemes[1].

10. In their final report[2], the IPSPC set out a framework for comprehensive reform of public service pensions that sought to balance concerns about the cost of the schemes to taxpayers and the need to ensure decent levels of retirement income for those who have devoted their working lives in the service of the public.

11. The Government accepted Lord Hutton's recommendations as the basis for consultation with scheme employers, trade unions and other interested parties. During negotiations the Government agreed to protect those public service workers who, as of 1 April 2012, had ten years or less to their normal pension age (NPA)[3], as they had least time to prepare.

12. The reforms were implemented in the LGPS in England and Wales from 1st April 2014, and in the other main public service pension schemes from 1st April 2015. The main features of the reformed schemes include later retirement ages to reflect the fact people have been living longer, higher employee contributions to rebalance the costs of the schemes between the members and taxpayers, and pensions based on average earnings rather than on pay at the point members retire or otherwise leave the schemes.

13. The schemes were designed to ensure that members would have good pensions, which at least met the target levels identified by Lord Turner's Pension Commission on the levels of income needed in retirement. The reformed schemes should provide many low and middle earners working a full career with pension benefits at least as good as, if not better than, the benefits they would have received under the previous arrangements.

14. The reformed schemes remain among the most generous available in the UK, and an important part of the remuneration of public service workers. Public service pension

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[1] Chart Ex. 1, p8 of IPSPC interim report, October 2010, https://www.ucu.org.uk/media/4328/Independent-Public-Service-Pensions-Commission---interim-report-7-Oct-10/pdf/hutton_pensionsinterim_071010.pdf
[2] https://www.gov.uk/government/publications/independent-public-service-pensions-commission-final-report-by-lord-hutton
[3] In the 2008 Scheme, a member's normal pension age was known as their normal retirement age. However, for consistency, in this consultation document we refer to it as their normal pension age or their NPA.

provision compares favourably with pension provision in the private sector. In 2019 34% of all employees with workplace pensions in the public sector received contributions of at least 20% from their employer. This compares with just 3% of all employees with workplace pensions in the private sector who received at least 20% from their employer[4].

Reform in the LGPS

15. In the LGPS, the final salary scheme that existed prior to these reforms was known as **'the 2008 Scheme'**. The reform package implemented from April 2014 (**'the 2014 Scheme'**) through the Local Government Pension Scheme Regulations 2013[5] (**'the 2013 Regulations'**) consisted of the following main elements:

- fundamentally, and consistent with the approach taken across the public sector, a move to future benefit accrual based on a member's pay over their career (a 'career average' structure), from a structure where member's benefits were based on a member's pay at leaving the scheme (a 'final salary' structure). Importantly, where active members had membership of the LGPS prior to April 2014 and did not have a disqualifying break in service[6], but had aggregated their membership, they retained a 'final salary link' that meant their pay at point of leaving the scheme would still be used in calculating their 2008 Scheme benefits, even where this is after April 2014.

- a move from a NPA of 65 to a NPA linked to a member's State Pension age, subject to a minimum of 65 (currently ranging from 65 to 68), but with members still able to retire as early as 55 or as late as 75, with actuarial reductions or increases applied, respectively.

- a move from a 1/60th accrual rate to a 1/49th accrual rate. A pension scheme's accrual rate is the proportion of a member's pay that they receive for each year of membership. The change in the LGPS accrual rate in the 2014 Scheme was a 22% improvement from that which applied in the 2008 Scheme.

- revisions to employee contribution bandings. From April 2014, employees' contributions to the LGPS were banded from 5.5% of earnings (for members earning less than £13,500 per year) up to 12.5% of earnings (for members earning over £150,000 per year). Contribution rates had also been banded in the 2008 Scheme, but the range had been narrower, from 5.5% to 7.5% of earnings.

- the introduction of a 50/50 section, giving scheme members the flexibility to pay half the contributions for half the pension accrual for a period of time, whilst still retaining full life cover and ill-health cover.

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[4] https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/workplacepensions/bulletins/annualsurveyofhoursandearningspensiontables/2019provisionaland2018finalresults#contributions-to-workplace-pensions

[5] http://www.legislation.gov.uk/uksi/2013/2356/contents, as amended

[6] Where referred to in this document, a 'disqualifying break in service' is a continuous break of more than five years in active membership of a public service pension scheme.

16. As a whole, the package was designed to achieve the Government's aims in making the LGPS more sustainable, affordable and fairer in the longer term. In particular, the combination of the move to a career average basis and the improvement to the LGPS's accrual rate should mean that many low and medium paid members will receive a pension from the 2014 Scheme at least as good as the pension they would have received from the 2008 Scheme. In addition, whilst LGPS employer contributions vary, members will benefit from significantly higher employer contributions than the average applicable in the private sector.

The statutory underpin

17. The LGPS provided transitional protection to its older workers via a statutory underpin (hereafter referred to as 'the underpin'). All members moved into the 2014 Scheme on the reform date of 1st April 2014, but 'protected members' (being the older group of members who met certain qualifying criteria and originally had underpin protection) were given an underpin that provides their retirement pension cannot be less than it would have been in the 2008 Scheme. In some public service pension schemes, tapered protections were provided to members who were between 10 and 14 years from their NPA on 1st April 2012, and so were not eligible for full protection (which was reserved for those within ten years of their NPA on 1st April 2012) However, in the LGPS, there were no tapered protections.

18. Underpin protection differs from the approach used in other main public service pension schemes[7] where older workers who met the criteria for transitional protection stayed in their final salary schemes after separate, new career average schemes were introduced in April 2015. In those schemes, different rules may therefore apply to protected and unprotected members in relation to areas of scheme design including contribution rates, survivor benefits and ill health retirement.

19. By contrast, the existing underpin only has application in relation to the value of a protected member's pension at their 'underpin date' (see paragraph 20 for further details). All members have participated in the reformed career average scheme from April 2014 and the same rules in relation to contributions and benefits apply to all members in the same way.

20. Underpin protection in the LGPS was implemented through regulation 4 of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendments) Regulations 2014[8] (**'the 2014 Regulations'**). At a high level, underpin protection under regulation 4 works in the following way:

- Underpin protection is granted to those who were active members in the LGPS on 31st March 2012 and who on 1st April 2012 were 10 years or less from the NPA

[7] With the exception of the local government pension schemes in Scotland and Northern Ireland who took a similar approach to the LGPS in England and Wales.
[8] http://www.legislation.gov.uk/uksi/2014/525/contents/made, as amended

applicable to the member under the 2008 Scheme (usually 65[9])[10] (regulation 4(1)(a)).

- Those who meet the basic criteria for underpin protection retain this so long as they are:
    - in active membership in the 2014 Scheme the day before their 'underpin date' (see below),
    - do not have a disqualifying break in service after 31st March 2012, and
    - have not drawn benefits from the 2014 Scheme before their underpin date (regulation 4(1)(b) to (d) and (3)).
- The underpin test is carried out on an individual's 'underpin date' which is the earlier of:
    - the date the protected member reaches their NPA under the 2008 Scheme (usually 65), or
    - the date the protected member ceased to be an active member of the scheme with an immediate entitlement to a benefit (regulation 4(2)).
- The underpin test is carried out by comparing the 'assumed benefits' (i.e. the career average benefits the protected member has accrued) against the 'underpin amount' (i.e. the final salary benefits the protected member would have accrued if the scheme had not been reformed) (regulations 4(5) and (6)). These paragraphs contain detailed provisions which enable administrators to take into account a variety of factors in the comparison of benefits. For example, where the protected member is due to receive an enhancement to their 2014 Scheme benefits as a result of retiring on ill-health grounds, the difference between that enhancement and the enhancement they would have received under the 2008 Scheme would be considered.
- If the underpin amount is calculated to be higher than the assumed benefits on the underpin date, the protected member's pension account is to be increased by the difference (regulation 4(4)).

The McCloud and Sargeant cases

21. Soon after the reformed scheme benefit structures were introduced in other public service pension schemes in April 2015, legal challenges were brought against the transitional protection arrangements in the judicial and firefighters' pension schemes ('McCloud' and 'Sargeant', respectively) on various grounds including that the transitional protections offered to older members constituted unjustified direct age discrimination. In those cases, younger firefighters and judges argued that younger members were treated less favourably than older members who were given transitional protection. The Court of

[9] By virtue of regulation 24(4) of the 2014 Regulations, some groups had a protected 2008 Scheme NPA of 60 in relation to their 2008 Scheme benefits.
[10] By virtue of regulation 9(1) of the 2014 Regulations, members who were not active in the LGPS on 31st March 2012, but who were active in another public service pension scheme on that date and who meet certain qualifying criteria may also have underpin protection

Appeal ruled in December 2018[11] that transitional protection in the judicial and firefighters' pension schemes gave rise to unlawful age discrimination.

22. The Government sought permission to appeal to the Supreme Court. This application was refused on 27 June 2019. In a written ministerial statement on 15 July 2019[12], the Government explained that it accepted that the Court of Appeal's judgment had implications for all schemes established under the Public Service Pensions Act 2013, as all schemes had provided transitional protection arrangements for older members. The Government confirmed that it would take steps to address the difference in treatment across all schemes and for all members with relevant service, regardless of whether they had lodged a claim. The matter has been remitted to the Employment Tribunals to determine a remedy for claimants[13]. Since summer 2019, MHCLG have been considering the changes necessary to remove the unlawful discrimination from LGPS regulations, and in February 2020 held technical discussions with the Scheme Advisory Board on these proposals.

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[11] https://www.judiciary.uk/wp-content/uploads/2018/12/lord-chancellor-v-mcloud-and-ors-judgment.pdf
[12] https://www.parliament.uk/business/publications/written-questions-answers-statements/written-statement/Commons/2019-07-15/HCWS1725/
[13] The LGPS in England and Wales does not have any ongoing court cases relating to its underpin protection.

Addressing the discrimination

Our approach

23. In the McCloud and Sargeant cases, the Courts identified unjustified age discrimination in transitional protection arrangements in the Judicial and Firefighters' Pension Schemes. In relation to the LGPS, this difference in treatment exists between two groups of LGPS members:

- those who were in service on 31st March 2012 and were within ten years of NPA on 1st April 2012, therefore benefiting from underpin protection and 'better off' than the second group; and,

- those who were in service on 31st March 2012 and were more than ten years from NPA, were not eligible for underpin protection and therefore 'worse off' than the protected members (as they were not guaranteed a pension of at least the level they would have received in the final salary scheme).

24. At a high-level, our proposal for removing the difference in treatment from the LGPS is to extend underpin protection to the second group of members listed above – i.e. those who were not old enough to receive underpin protection when it was originally introduced. This should ensure that the two groups listed are treated equally for benefits accrued from April 2014 onwards. This proposal is described in more detail in the next section ('Detailed proposals'). The updated underpin is referred to here as 'the revised underpin'. The members who would be in scope of the revised underpin, both the group originally protected and those who would newly gain underpin protection under our proposals, are collectively referred to as 'qualifying members' in this document.

25. Consultees may be aware that Government has separately recently launched a consultation[14] seeking views on this matter as it applies to most of the other main public service pension schemes[15]. As noted already, transitional protection arrangements were different in other public service pension schemes and therefore different issues arise in considering an appropriate remedy for the discrimination found in McCloud and Sargeant. That other Government consultation seeks views on two options for removing the discrimination in those schemes, both involving an element of member choice between the reformed career average schemes and the legacy final salary schemes.

26. Member choice is being considered in relation to other public service pension schemes because, in those schemes, the two groups of members have participated in different pension schemes since April 2015 with different benefits between reformed and legacy schemes and, potentially, different employee contribution rates. This is not the case in the LGPS because underpin protection is designed to ensure that a qualifying member is better off without needing to make a choice.

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[14] https://www.gov.uk/government/consultations/public-service-pension-schemes-consultation-changes-to-the-transitional-arrangements-to-the-2015-schemes
[15] The LGPS is out of scope for the other Government consultation.

27. As set out in paragraphs 17 to 20, the underpin is principally an administrative test undertaken at the earlier of the date a qualifying member leaves active service and the date they reach their 2008 Scheme normal pension age. It is designed to guarantee that a qualifying member's pension calculation gives them the better of a) the pension they have built up in the career average 2014 Scheme and b) the pension they would have built up in the final salary 2008 Scheme, over the same time period.

Question 1 – Do you agree with our proposal to remove the discrimination found in the McCloud and Sargeant cases by extending the underpin to younger scheme members?

28. To achieve the full benefits of the career average reforms made in April 2014, it is the Government's view that the underpin period should end for all qualifying members at a specified point in time.

29. Under the rules governing the existing underpin, no further underpin dates will arise beyond 31st March 2022, as this is the last date a protected member can reach their 2008 Scheme NPA. In considering how to equalise treatment between the unprotected and protected groups, we propose that both groups will be given underpin protection from 1st April 2014 to 31st March 2022 (or to the members' underpin date, where this is earlier). We consider that this approach will mean there is a consistent period of protection for all qualifying members – i.e. those who were members of the scheme on 31st March 2012 and who went to on to have 2014 Scheme membership without a disqualifying break in service (and who aggregated their membership), regardless of their age.

30. From 1st April 2022 it is our intention that all service in the LGPS will be on a career average basis, with no underpin. As set out in the Background section, we believe that the move from a final salary to a career average pension scheme design in April 2014 created a fairer structure for LGPS members. Under the 2014 Scheme, those public servants who see considerable increases in earnings over their career – and particularly towards the end of their career – are no longer likely to be relatively favoured compared with their colleagues who did not. Phasing out underpin protection is an important step to achieving the full benefits of a career average scheme design.

Question 2 – Do you agree that the underpin period should end in March 2022?

31. We are keen to ensure that the group of younger members who, under our proposals, would gain underpin protection have an equivalent level of protection to their older colleagues. It is therefore proposed that the underpin comparison would not, for most qualifying members, take place upon the underpin period ending in March 2022. Instead, the comparison of 2008 Scheme and 2014 Scheme benefits would take place at a qualifying member's underpin date (generally, the earlier of the member's date of leaving and age 65), even if this is after March 2022 – i.e. qualifying members will retain an ongoing 'final salary link', consistent with their pre-2014 pension accrual. For those who are currently at an earlier stage of their career, and who may have promotions and other salary increases later in their career, this ensures a fairer comparison of the two schemes' benefits. The final pay calculation would be based on a member's pay over their last 365

days of active membership, and would take into account the existing ‘lookback’ provisions where members have had a reduction in pay[16].

32. As part of this project we have considered how the existing underpin regulations work and the following section contains details of changes we are proposing. Collectively, the changes mean that the revised underpin regulations will differ in a number of respects from the existing underpin provisions contained in regulation 4 of the 2014 Regulations. We consider that these amendments are essential to ensure that the underpin regulations are clear and consistent and provide a framework of protection that works more effectively for all stakeholders and which, at the same time, provides in essence the same level of protection to scheme members.

33. Nonetheless, to avoid creating new differences in treatment in the LGPS, we propose that the amended regulations will apply retrospectively from 1st April 2014, ensuring that all qualifying members are subject to the same detailed provisions. We believe this is the best approach and one which will allow us to be confident we are addressing the findings of the Courts, and removing differences in treatment between older and younger workers. We do not plan that members’ accrued rights would be detrimentally affected as a result of this approach, but we welcome comments from stakeholders if there are specific concerns about potential accrued rights issues.

34. In proposing these changes, we have considered the legal principle of ‘minimum interference’. The courts have found this principle generally applies to pensions changes following an equal pay issue. Whilst it has not been recognised outside the context of equal pay, it could be considered in other contexts too. ‘Minimum interference’ means that the scheme is obliged to make the minimum necessary interference to ensure the scheme operates lawfully. Whilst some of the changes outlined in this consultation paper are not a direct consequence of the Courts’ findings in the McCloud and Sargeant cases, we believe that they are necessary for the effective and consistent application of underpin protection to members of the LGPS.

35. Retrospective application of the proposed regulations means that certain cases will need to be revisited by scheme administrators. Below are examples of such cases:

- Cases where a member had underpin protection originally and the revised underpin may have applied differently to them. In practice, this may be all cases where a member already has underpin protection and has since had their underpin date.
- Cases where a member does not currently have underpin protection, but would have under the revised underpin, and has since retired or left the LGPS with a deferred benefit.
- Cases where a member does not currently have underpin protection, but would have under the revised underpin, and has since transferred out of the LGPS or trivially commuted their benefits.

36. There will also be more difficult cases, for example, where members who may have benefitted from the proposals outlined in this consultation have died. In such cases, it is

[16] Under the 2008 Scheme, members with pay reductions or restrictions in their last ten years of continuous employment may have the option to have their final pay calculated as the average of any 3 consecutive years’ pay in their last 13 years.

our view that administrators should take all steps to ensure that any retrospective increase in a member's pension arising from the underpin is taken into account in respect of relevant survivor benefits that became payable at the time of the member's death.

37. We are aware that retrospective application of the proposed draft regulations will lead to significant administrative complexity. We do not anticipate any recalculations would result in members' benefits being detrimentally affected. Further consideration of the complexities arising from retrospection are considered in the Implementation and Impacts section.

Question 3 – Do you agree that the revised regulations should apply retrospectively to 1st April 2014?

38. This consultation sets out proposals which are principally about removing unlawful discrimination from the LGPS. Achieving this key aim, and minimising the risk of further issues arising, has therefore been our primary concern in coming forward with these proposals. However, in doing so, we have been conscious of the additional administrative burden these changes would create and have sought to minimise the impacts wherever possible. We consider that the proposed approach is the simplest way we can effectively ensure that the revised underpin works effectively and fairly for all. Further consideration of the potential administrative impacts of the proposals is outlined in paragraphs 134 to 136.

Detailed proposals

39. This section contains our detailed proposals on the proposed amendments to the underpin. Draft regulations have been prepared (**annex B**) and we would welcome general comments on those draft regulations, as well as specific comments on the below questions.

Question 4 – Do the draft regulations implement the revised underpin which we describe in this paper?

Question 5 – Do the draft regulations provide for a framework of protection which would work effectively for members, employers and administrators?

Question 6 – Do you have other comments on technical matters related to the draft regulations?

The revised underpin – basic elements

40. The approach we have taken to the revised underpin consists of a number of basic elements, as described here.

Qualification criteria

41. Fundamentally, under the revised underpin, members would no longer need to have been within ten years of their 2008 Scheme NPA to qualify for underpin protection. Members who were active in the 2008 Scheme on 31st March 2012 and who have accrued benefits under the 2014 Scheme without a disqualifying break in service (five or more years) would have underpin protection, subject to aggregation requirements.

42. An aspect of the existing underpin regulations that we are seeking to change is the requirement that a member must leave active service with an immediate entitlement to a pension for underpin protection to apply to them (regulation 4(1)(b) of the 2014 Regulations). We anticipate that when underpin protection is extended to younger workers, it is much more likely that members will leave the scheme before having an immediate entitlement to benefits, meaning they would not, as things stand, benefit from underpin protection. Under the revised underpin, we propose that underpin protection would apply where a member leaves with either a deferred or an immediate entitlement to a pension. This approach is also more likely to ensure that LGPS regulations are compliant with preservation requirements under the Pension Schemes Act 1993, which broadly require[17] that schemes do not contain rules which mean that leavers prior to normal pension age are treated less favourably than leavers at normal pension age. The retrospective application of this change would also aim to ensure that any members protected under the

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[17] Section 72 of the Pension Schemes Act 1993

existing underpin who have suffered detriment due to the current wording would regain their underpin protection[18].

43. As per existing requirements, members who leave the LGPS without an immediate or deferred entitled to a pension[19] would not have underpin protection, as they would only be eligible for a refund of their contributions, aggregation with another LGPS record or a transfer to another scheme

Question 7 – Do you agree that members should not need to have an immediate entitlement to a pension at the date they leave the scheme for underpin protection to apply?

Question 8 – Are there any other comments regarding the proposed underpin qualifiying criteria you would like to make?

Aggregation

44. In reviewing the operation of the existing underpin, it has become clear that the current regulations do not implement our policy intent as clearly as we would like in one important respect, and the existing regulations could cause substantial new issues to arise. Whilst the LGPS is one pension scheme, with rules defined at the national level through scheme regulations, it is a locally administered scheme, with 87 administering authorities throughout England and Wales. It is an important principle for the effective and efficient administration of the scheme that administrators are generally able to calculate pension benefits independently and do not need to obtain data from other LGPS administrators to be able to undertake basic pension calculations. Such an approach also ensures that the scheme is run in accordance with the principle of 'data minimisation', where personal data is not shared between data controllers any more than is necessary for the effective administration of a member's pension.

45. To prevent such complications, the LGPS has aggregation provisions which mean that separate pension records can be joined together[20]. This means that, in most cases, members can choose whether to have LGPS records aggregated (or 'joined up') or kept separate from one another. Since 1st April 2014, aggregation is usually automatic[21] - where a member leaves an employment with a deferred benefit and then rejoins the LGPS

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[18] For example, members who, under regulation 24(1) of the 2014 Regulations, had a protected NPA of 60 in the 2008 Scheme. Some of these protected members would have been younger than 55 in April 2014 and may not have had an immediate entitlement to benefits at their underpin date.
[19] This applies where members do not have a qualifying service for a period of two years (regulation 3(7) of the 2013 Regulations). Special provisions apply where members joined before 1st April 2014.
[20] This does also require data sharing between administering authorities. However, the transfer of a record from one authority to another following a structured aggregation process is likely to be simpler and less prone to error than ad hoc sharing necessary to undertake pension calculations from time-to-time over a member's career.
[21] Where a member only has a deferred refund entitlement (i.e. has left with a refund entitlement which has not yet been paid) from a ceased period of LGPS membership, this must be aggregated with their subsequent LGPS membership and there is no choice (regulation 22(5) and (6) of the 2013 Regulations.

in another employment (potentially in another pension fund), they have 12 months to elect to their administrator for aggregation not to apply[22].

46. Where a member takes a decision which means their LGPS benefits are unaggregated, these are generally administered as separate entitlements. Where a member takes a decision which means their LGPS benefits are aggregated, their combined record is generally administered as one period of membership. For example, where a member with 2008 Scheme membership has not had a disqualifying break in service and aggregates that record with another LGPS membership, they would retain their final salary link on the combined record. By contrast, if the same member decides not to aggregate their membership they would lose their final salary link[23] on the unaggregated record. These rules preserve the approach described above, through which local administrators are generally able to calculate separate benefits independently.

47. However, regulation 4 of the 2014 Regulation does not appear to include an aggregation requirement for underpin protection to apply. A strict interpretation of regulation 4(1)(a) therefore appears to suggest that where, for example, a member was:

a) active in the LGPS on 31st March 2012,

b) subsequently active in the 2014 Scheme in a separate employment without a disqualifying break in service, and

c) the two records were not aggregated,

underpin protection would still apply. In our view, this would be extremely difficult for scheme administrators to effectively administer in the coming decades. It is also inconsistent with the general approach MHCLG has adopted in relation to the administration of the LGPS, as described in paragraph 45, and as has been applied in relation to the final salary link.

48. Where there is no requirement to aggregate benefits, administrative difficulties would not only arise in determining who has underpin protection (as a previous record may be held in another fund), but also in actually undertaking the underpin comparison. One scenario that may be likely to occur more frequently, as a result of the significant expansion of the underpin proposed in this document, would be situations like the following:

- A member has two, unaggregated LGPS records in separate funds:
    - Membership one – active from 2011 to 2016, and
    - Membership two – active from 2017 to 2022.
- As the member was in active service on 31st March 2012 and had 2014 Scheme membership, without a disqualifying break in service, they have underpin protection.
- Upon leaving membership one, the member would have an underpin date (calculated in the normal way).

[22] By virtue of regulation 22(8) of the 2013 Regulations.
[23] By virtue of regulation 3(8) of the 2014 Regulations.

- The member would also have an underpin date upon leaving membership two for their active membership in the scheme over the underpin period (for this member, 2014 to 2016 and 2017 to 2022). This would require the second fund to undertake an underpin comparison for the whole period using data they hold and data they need to obtain from the other fund (in relation to membership one).
- In this situation, it may also need to be considered whether any underpin addition arising should be split between the two funds and the two employers, so as to ensure liabilities are appropriately held.

49. This would clearly be extremely administratively complex and potentially lead to an increased likelihood of errors being made. It is likely that other similar scenarios would also arise, and that the administrative complexities would continue for many years (as some members' underpin date may not take place for 30 or 40 years).

50. In light of this, we are proposing that regulation 4 of the 2014 Regulations is amended to make clear that members must meet the qualifying criteria in a single membership (a 'relevant Scheme membership' as defined in the proposed regulations) for underpin protection to apply. So, where a member has had a break in service, or a period of concurrent employment, their benefits must be aggregated for underpin protection to apply. The introduction of the concept of 'relevant scheme membership' has allowed us to define more clearly in the regulations the benefits administrators should be assessing when undertaking underpin calculations.

51. As our intention is for the revised underpin regulations to apply retrospectively, it is possible these changes will mean that some members of the LGPS who have underpin protection at the moment (across separate LGPS memberships) would lose this. To ensure that no member is worse off as a result of our proposed amendments, we are proposing that active and deferred members are given an additional 12 months to elect to aggregate previous periods of LGPS membership, where such a decision would mean they have 'relevant Scheme membership' and therefore would have underpin protection. It is not proposed that this decision would be required for pensioner members, whose existing pensions would be unaffected by the aggregation changes outlined here. Circumstances where current pensioner members have underpin protection which is based on unaggregated membership and they have received an addition to their pension as a result of their underpin protection are expected to be rare[24].

52. The additional 12 months would apply from the date the regulations come into force. This additional election period would not apply in respect of other periods of membership members may wish to aggregate, only to periods where a failure to aggregate would mean the member would not obtain underpin protection[25]. Good communications with members

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[24] Such situations are expected to be rare due to a combination of factors. Generally, we expect that most protected LGPS members currently retiring are better off under the career average scheme, due in part to its substantially better accrual rate. Moreover, LGPS administrators are unlikely to be aware that a member has underpin protection if a member has not aggregated their previous LGPS membership. We expect that situations where a member has been awarded an underpin on unaggregated membership by their administrator and that subsequent underpin calculation has shown the final salary pension to be better than the member's career average pension would be rare.
[25] However, it should be noted that LGPS employers generally have the ability to allow aggregation beyond the statutory limits set out in scheme regulations.

in this situation will be crucial so that they understand whether this election period applies to them and the implications of the decision they are being asked to consider. As set out in paragraphs 131 and 133, we would plan to work closely with the Scheme Advisory Board on member communications to support the changes proposed in this paper.

53. The Public Service Pensions Act 2013 applies certain requirements where a responsible authority[26] proposes to make scheme regulations containing retrospective provisions which appear to the authority to have 'significant adverse effects in relation to the pension payable to or in respect of members of the scheme' (section 23(1))[27]. Specifically, where this is the case, the following applies:

- The authority must obtain the consent of persons (or representatives of the persons) who appear to the responsible authority to be likely to be affected by the provisions (sections 23(1) and (3)).

- The authority must lay a report before Parliament (section 23(4)).

- The regulations become subject to the affirmative procedure, meaning they have to be approved by a resolution of each House of Parliament (sections 24(1)(b) and 38).

54. We welome stakeholders' views on whether the changes we describe in paragraphs 50 to 52 would have 'significant adverse effects' in relation to the pension payable to or in respect affected members. Whilst the changes would have retrospective application, the additional 12 month election period we are proposing would ensure that members have the opportunity to aggregate their pension records and obtain underpin protection if they wish. Members who wish to keep their records separate (perhaps as they have re-joined the LGPS in a lower paid post and do not want a final salary link) would also be able to retain this position by doing nothing.

Question 9 – Do you agree that members should meet the underpin qualifying criteria in a single scheme membership for underpin protection to apply?

Question 10 – Do you agree with our proposal that certain active and deferred members should have an additional 12 month period to decide to aggregate previous LGPS benefits as a consequence of the proposed changes?

Question 11 – Do you consider that the proposals outlined in paragraphs 50 to 52 would have 'significant adverse effects' in relation to the pension payable to or in respect of affected members, as described in section 23 of the Public Service Pensions Act 2013?

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[26] Under section 2 and schedule 2 of the Public Service Pensions Act 2013, the Secretary of State is the responsible authority for the LGPS in England and Wales.

[27] Certain requirements also apply under section 23(2) of the Public Service Pensions Act 2013 where the responsible authority proposes to make scheme regulations that are retrospective in nature, but which have significant adverse effects in other ways (for example, in relation to injury or compensation benefits). We are content that these provisions would not apply in respect of these proposed changes.

Achieving a fair and consistent underpin

55. Alongside the changes necessary to remedy the discrimination found by the Courts, and the aggregation proposal above, we are also proposing some changes to underpin provisions to ensure that the underpin works effectively and consistently for all members.

56. **Breaks in service of less than five years** – the 2014 Regulations do not currently make clear whether it is permitted for the underpin to be re-calculated if a protected member leaves active service and returns without a disqualifying break in service (i.e. within five years). We propose that where a qualifying member leaves active service, rejoins within five years and aggregates their benefits, a further underpin comparison would be undertaken when they next reach their underpin date (i.e. leave active service or reach their 2008 Scheme NPA), using their final salary at the most recent date of leaving (and the results of the previous comparison disregarded). Taking this approach means that promotional pay increases that may apply where a qualifying member progresses in their career are taken into account in their underpin calculations. It also ensures younger members of the scheme have equivalent protection to their older colleagues (whose final salary benefit is based on their pay at the end of their career, after relevant promotions and pay rises). It may also benefit those qualifying members who are more likely to have a break in employment, such as women[28] or those who have a disability. However, it is proposed that qualifying members who re-join the LGPS after their 2008 Scheme NPA would not have a further underpin date, even if they aggregate their previous pension rights. This is consistent with our general approach that underpin protection only provides protection until a member's 2008 Scheme NPA.

57. **Early/late retirement factors** - When a protected member leaves the scheme, the current underpin calculation does not take into account the impact of early/late retirement factors, which may mean the calculation does not correctly identify the scheme in which the member would receive the higher benefits. This situation arises because of differences in NPAs in the 2008 and 2014 Schemes, which may mean early and late retirement factors apply at different rates. We therefore propose that the revised underpin should include a 'check' to ensure that, at the point a qualifying member takes their benefits from the scheme, they are still due to receive at least the pension they would have received under the 2008 Scheme, after the application of any early/late retirement factors. Further detail on how this will work is outlined in the next section regarding the two-stage process we intend to adopt.

58. **Death in service** – the existing definition of the underpin date set out in regulation 4(2) of the 2014 Regulation do not make clear what should happen where a member who has underpin protection dies in active service. On a strict interpretation, the 2014 Regulations would therefore appear to mean that there is no underpin comparison for such a member (which could reduce any survivor benefit that may be payable). We do not believe that was or should be the policy intent. In relation to the revised underpin, we therefore propose that there would be a clear requirement for an underpin comparison to be undertaken where a qualifying member dies in service.

59. **Survivor benefits** – it is not always clear how the survivor benefits provisions in the 2013 Regulations apply in relation to the underpin, and whether increases in benefits

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[28] http://www.parliament.uk/briefing-papers/sn06838.pdf

arising from the underpin should be included in the calculation of survivor benefits following the death of a protected member (from any status). We intend that the amended regulations will make clearer how the underpin applies in relation to survivor benefits. In general terms, it is our policy that where a qualifying member has an addition to their pension arising from the underpin, this should be taken into account in determining the value of relevant survivor benefits, where such benefits are based on the value of the qualifying member's pension. The next section of this paper outlines our policy on the underpin and survivor benefits in more detail.

60. Together and individually, the changes we describe in paragraphs 56 to 59 are intended to be beneficial for scheme members, and are intended to ensure that the revised underpin works for all members with underpin protection in a consistent and effective way. As outlined in paragraph 34, we have considered the principle of minimum interference but believe that these changes are both appropriate and necessary.

Question 12 – Do you have any comments on the proposed amendments described in paragraphs 56 to 59?

A two-stage process

61. Under current provisions, the underpin calculation takes place at a single point in time – a member's underpin date, being the earlier of the date a member leaves active service with an immediate entitlement to a pension, and the date they reach their 2008 Scheme NPA. This has its advantages, such as in respect of administration. However, in the round, we now consider a two-stage underpin process would provide a more robust form of protection and the draft regulations attached propose such an approach. Under this, all qualifying members would have an 'underpin date' and an 'underpin crystallisation date':

- the purpose of the underpin date would be to provide for a provisional assessment of the underpin, broadly comparing the qualifying member's 2014 Scheme benefits in a relevant scheme membership against the 2008 Scheme benefits they would have accrued over the same period, in respect of the same membership. The underpin date would take place at the earliest of the date the qualifying member:

    - leaves active service in a relevant scheme membership,
    - reaches their 2008 Scheme NPA, or
    - dies.

  Regardless of the outcome of this provisional comparison, there would be no adjustment to a member's pension at their underpin date. The purpose of the comparison at a member's underpin date would primarily be so that the member has early information on how the underpin may apply to them. This recognises that there may be many years between a qualifying member's underpin date and their underpin crystallisation date, when the final comparison is due to take place.

- The purpose of the underpin crystallisation date would be to provide for a final check at the point the qualifying member's benefits from the scheme are 'crystallised' (where the member takes their pension from the scheme). The check would be designed to ensure that qualifying members always receive at least the

higher of the pension they would have been due from the 2014 Scheme and the 2008 Scheme, taking into account the impact of factors like early/ late retirement adjustments.

62. We consider that the use of a two-stage process will achieve the following:

- Fundamentally, it should give qualifying members greater confidence that the underpin process has given them the benefit that is better for their own personal situation, even if they take their benefits many years after they leave the scheme.

- By undertaking an initial comparison at a member's underpin date, it would give qualifying members information about how the underpin may apply to them at the earliest possible date, even if such calculations would only be provisional.

- It is more compatible with the revised underpin where members can re-join, aggregate their membership and have a further underpin date at a subsequent point in time. Until the final underpin check at a member's underpin crystallisation date, there will be no change to a member's active or deferred pension arising from the underpin.

- It reflects the fact that for most members retiring on age grounds, early and/or late retirement factors will apply in calculating their 2008 and/or 2014 Scheme benefits. As these will not apply in the same way to a member's 2008 and 2014 Scheme entitlements (unless their 2008 Scheme NPA is the same as their State Pension age), a final check at the point benefits are paid is necessary to ensure the member is getting the higher benefit.

63. Further detail on the proposed two-stage process is contained in **annex C** and illustrative examples of a variety of scenarios are included in **annex D**.

Question 13 – Do you agree with the two-stage underpin process proposed?

Underpin period and final salary link

64. As discussed earlier in the consultation (paragraphs 28 to 31), we propose that:

- the revised underpin be extended to provide underpin protection to all qualifying members for service from 1st April 2014 up to and including 31st March 2022, except where a member's underpin date is sooner.

- from 1st April 2022, all LGPS membership accrues on a career average basis, with no underpin,

- but to ensure that there is an equivalent level of protection between older and younger members, the comparison of 2008 Scheme and 2014 Scheme benefits would take place at a qualifying member's underpin date, even if the underpin period ends sooner.

The revised underpin – application

65. This section describes how the revised underpin is intended to apply to qualifying members at different stages of their membership of the scheme, and at different life events.

Whilst in active membership

66. Whilst a qualifying member is in active service below their 2008 Scheme NPA, they will remain a member of the 2014 Scheme. For the period up to 31st March 2022, active qualifying members will accrue underpin protection. From 1st April 2022, accrual will be on a career average basis alone, but active qualifying members will retain a final salary link in relation to their underpin protection. Each year, a qualifying member's annual benefit statement will include an estimate of how the underpin would have applied to them if they had left the scheme at the end of the scheme year (i.e. as if their underpin date had been 31st March in that year). In these estimates, no account would be taken of actuarial adjustments relating to a member's age.

67. If a qualifying member remains in active service at their 2008 Scheme NPA (normally 65), their underpin date will be triggered in relation to their relevant scheme membership, meaning a comparison of their 2008 Scheme and 2014 Scheme pension (relating to the period from 1st April 2014 up to 31st March 2022, or their 2008 Scheme NPA if earlier) would be undertaken. This calculation would be based on the member's final pay as at their 2008 Scheme NPA (taking into account appropriate lookback provisions where appropriate). The member would be informed of the results of this comparison, but also informed that a check at their underpin crystallisation date would be undertaken at the point they take their benefits to ensure they are getting the higher benefit. Final salary increases or reductions beyond the member's 2008 Scheme NPA would not impact on the member's underpin protection.

Concurrent employments

68. Underpin protection may apply to qualifying members who hold two or more active memberships of the scheme at the same time ('concurrent employments'). Under our proposals, underpin protection would be linked to specific scheme memberships, with members who have 'relevant scheme membership' having underpin protection on that membership. Relevant scheme membership applies where:

- a member was an active member on 31st March 2012,
- a member has been an active member of the 2014 Scheme, and
- they did not have a disqualifying break in service.

69. Relevant scheme membership would apply in the normal way where a qualifying member has concurrent employments – for example, if a member has two posts and meets the criteria in one but not the other, they would have underpin protection in the former post, but not the latter. Where a qualifying member leaves a concurrent post in which they had relevant scheme membership before reaching their 2008 Scheme NPA their underpin date would apply in relation to that employment. If they were to then aggregate that membership with their ongoing post, the member would have a further

underpin date at the earlier of the date they leave that post or the date they reach their 2008 Scheme NPA.[29]

At date of leaving (without taking scheme benefits)

70. Where an active qualifting member leaves the LGPS before their 2008 Scheme NPA with a deferred entitlement to benefits, their underpin date would apply at their date of leaving. A provisional underpin comparison would be undertaken for the period up to 31st March 2022, or to the member's date of leaving if earlier. The member would be informed of the results of this comparison, but also informed that a check at their underpin crystallisation date would be undertaken at the point they take their benefits to ensure they are getting the higher benefit.

Whilst a deferred member

71. For qualifying members who have had an underpin date after leaving active membership of the scheme with a deferred benefit, annual benefit statements sent to the member would include details of the provisional calculations undertaken at their underpin date. The results of these calculations would be adjusted to reflect cost of living changes between the member's underpin date and the date of their annual benefit statement.

Re-joiners

72. Where a qualifying member who has had an underpin date in respect of a relevant scheme membership re-joins the scheme without a disqualifying break in service and aggregates their previous scheme membership with their active pension account[30], they will retain continuing underpin protection for any service up to 31st March 2022. For service from April 2022 onwards, the member will retain a continuing final salary link in relation to their underpin protection (as well as in respect of their pre-2014 final salary membership). A further underpin date will occur at the date the member leaves active service or the date they reach their 2008 Scheme NPA.

Age retirement

73. When a qualifying member takes voluntary payment[31] of their benefits in a relevant scheme membership at any age between 55 and 75, their underpin crystallisation date will apply. This means that the final comparison of their benefits will be undertaken to determine whether the 2014 Scheme or 2008 Scheme benefits would be better. For qualifying members who retire from active status and do so before their 2008 Scheme NPA, the member's underpin date will take place as at their date of leaving[32]. The underpin crystallisation date will take place upon their pension coming into payment.

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[29] Under regulations 22(6) or (7) of the 2013 Regulations

[30] Under regulation 22 of the 2013 Regulations, all scheme members must have a pension account. Unless aggregated, members have multiple pension accounts for multiple periods of scheme membership.

[31] Non-voluntary payment of benefits following redundancy and business efficiency are covered in paragraph 100.

[32] As described in paragraph 67, where a qualifying member is in active service at their 2008 Scheme NPA, this would be their underpin date.

74. In the underpin crystallisation date calculation, the scheme administrator will take the provisional calculations from a qualifying member's underpin date and update these to take into account the effects of cost of living changes since the member's underpin date, as well as the impact of early/ late retirement factors. Where the final values show that the member would have been better off under the 2008 Scheme, an addition will be made to the member's 2014 pension account. The member's total pension in that relevant scheme membership for the period from 1st April 2014 to 31st March 2022 would also be payable without any further actuarial adjustment relating to the member's age.

Ill-health retirement

75. For most qualifying members retiring on ill-health grounds, their date of leaving will be their underpin date[33]. As applies under the existing underpin provisions, the underpin calculation at a qualifying member's underpin date will take into account any enhancements that they may be due where they are receiving 'tier 1'[34] or 'tier 2'[35] benefits under regulation 39 of the 2013 Regulations, and compare these against the relevant enhancements that would have applied under the 2008 Scheme. This comparison of enhancements would apply up to the earlier of a qualifying member's 2008 Scheme NPA and 31st March 2022.

76. A qualifying member's ill-health retirement date will be their underpin crystallisation date, in all cases. This calculation will take into account cost of living adjustments between the member's underpin date and their underpin crystallisation date for members retiring from deferred or deferred pensioner status. No account will be taken of actuarial reductions relating to their age as these do not apply in relation to ill-health retirements, but where the qualifying member is over their 2008 Scheme or 2014 Scheme NPA, the impact of actuarial increases will be considered.

77. Whilst in most cases a member can only have one underpin crystallisation date, an exception applies in relation to members who have retired with 'tier 3'[36] benefits. As tier 3 pensions are temporary, a qualifying member would typically have an underpin crystallisation date at the point they begin receipt of their temporary pension and a subsequent one at the point they receive payment of their suspended pension from the scheme or the underpin otherwise crystallises (from deferred pensioner status). Whilst the

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[33] With the exception of deferred or deferred pensioner members taking ill-health retirement under regulation 38 of the 2013 Regulations, and members who have previously reached their 2008 Scheme normal retirement age. Deferred pensioner members are members who were previously in receipt of a temporary tier 3 ill-health pension which has since ceased, and the member has not yet taken their main scheme benefits.

[34] Subject to other criteria that apply, tier 1 benefits apply to members retiring on ill-health grounds who are unlikely to be able to undertake gainful employment before their NPA (regulation 35(5)). Members receiving tier 1 benefits receive an adjustment to their pension equalling the full benefits they would have accrued between date of leaving and their 2014 Scheme NPA.

[35] Subject to other criteria that apply, tier 2 benefits apply to members retiring on ill-health grounds who are unlikely to be able to undertake gainful employment within three years of leaving the employment, but who are likely to be able to undertake gainful employment before reaching their NPA (regulation 35(6)). Members receiving tier 2 benefits receive an adjustment to their pension equalling 25% of the benefits they would have accrued between date of leaving and their 2014 Scheme NPA.

[36] Subject to other criteria that apply, tier 3 benefits apply to members who are likely to be capable of undertaking gainful employment within three years of their date of leaving (regulation 35(7)). Members receiving tier 3 benefits receive an unadjusted pension for a maximum of three years.

former calculation would not take into account actuarial reductions that may apply, the latter calculation would.

Death benefits

78. As noted earlier, under existing scheme regulations, it is sometimes unclear how scheme death benefits interact with the underpin. Our policy intent is set out in this section, and we have aimed to make these points clearer in the draft regulations. These clarifications are essential to ensuring that the underpin works effectively and consistently.

79. **Deaths in service** - For a qualifying member in active service, their date of death will be both their underpin date and their underpin crystallisation date. It is proposed that the underpin comparison would take into account the enhancements that apply under the 2008 and 2014 Scheme regulations in relation to deaths in service. This comparison of enhancements would apply up to the earlier of the qualifying member's 2008 Scheme NPA and 31st March 2022. This would be a new addition to the underpin regulations, and would be consistent with the approach taken in relation to ill-health retirements (outlined above in paragraph 75).

80. No adjustment relating to the underpin would apply to a qualifying member's death grant, as death grants for active members are based on a member's pay, not their pension.

81. Where survivor benefits are payable following a death in service of a qualifying member, the underpin comparison would be based on the provisional calculations and would not take into account the impact of early or late retirement factors which do not apply in relation to survivor benefits. Where there is an addition (i.e. the 2008 Scheme benefit is higher based on the unadjusted values), this addition would apply in the calculation of the survivor's benefit, at the appropriate accrual rate for each type of survivor.

82. **Deaths from deferred status** - Where a qualifying member dies from deferred status, their underpin date will have already taken place (on the date the member left active service, or on their 2008 Scheme NPA, if earlier). The day of the member's death would be their underpin crystallisation date.

83. Where survivor benefits are payable following a death from deferred status, the underpin comparison would be based on the provisional calculations and would not take into account the impact of early or late retirement factors which do not apply in relation to survivor benefits. Where there is an addition (i.e. the 2008 Scheme benefit is higher based on the unadjusted values), this addition would apply in the calculation of the survivor's benefit, at the appropriate accrual rate for each type of survivor.

84. Any addition arising from the provisional calculations undertaken at a member's underpin date will also apply in the calculation of the death grant. For deferred members, a death grant applies at 5 times the annual rate of pension, without actuarial adjustment relating to the age of the member.

85. **Deaths from pensioner status** – Where a qualifying member dies from pensioner status, the underpin date and the underpin crystallisation date will already have taken place.

86. Where survivor benefits are payable following the death of a pensioner, the underpin comparison will be based on the provisional calculations undertaken at a qualifying member's underpin date and will not take into account the impact of early or late retirement factors which do not apply in relation to survivor benefits. Where there is an addition (i.e. the 2008 Scheme benefit is higher based on the unadjusted values), this addition will apply in the calculation of the survivor's benefit, at the appropriate accrual rate for each type of survivor.

87. Any addition arising from the provisional underpin calculation will also apply in the calculation of the death grant, where applicable. For pensioner members, a death grant applies at 10 times the annual rate of pension, reduced by the actual amount of pension the member received prior to their death and by any lump sum commutation.

Public Sector Transfer Club transfers

88. The LGPS is a member of the Public Sector Transfer Club[37]. The Club is an arrangement that facilitates the mobility of employment within the public sector by, for example, enabling employees to avoid the reduction in the value of their accrued pension that could otherwise occur as a result of changing employment. Final salary pension transferees are awarded a service credit that maintains the member's final salary link for the pension accrued in their previous scheme. CARE transferees are awarded a pension credit that continues the rate of in-service revaluation that was provided in the member's previous scheme. The intention of the Club is that a member should not lose out as a result of changing employment within the public sector. Equally, the member should not receive benefits that are higher in value than if they had not changed employment.

89. Separately, the Government is consulting[38] on proposals to remove the unlawful discrimination from the other main public service pension schemes. That consultation includes a section seeking views on how transfers under the Public Sector Transfer Club may work in relation to the remedy proposals outlined in that consultation. It sets out that one option would be for a member to make a choice between career average and final salary benefits at the date of transfer, so that only one set of scheme benefits for the remedy period needs to be considered for the transferred service.

90. The consultation also notes that considerations in the LGPS may be different, given the different nature of transitional protection in the LGPS and that we would consult on more detailed proposals in relation to Club transfers between the LGPS and the other public service pension schemes.

91. One approach, which would be consistent with the option outlined in the wider consultation, would be for the same principle to apply. This would mean the following:

- **For Club transfers of protected service (accrued between April 2015 and March 2022) into the LGPS** - the receiving LGPS fund would give the member the option of deciding whether they wanted to use the transfer to buy final salary

[37] https://www.civilservicepensionscheme.org.uk/members/public-sector-transfer-club/
[38] https://www.gov.uk/government/consultations/public-service-pension-schemes-consultation-changes-to-the-transitional-arrangements-to-the-2015-schemes

membership or career average pension in relation to the transferred service. Quotations would be provided to help members make an informed choice.

- **For Club transfers of protected service (accrued between April 2014 and March 2022) out of the LGPS** – the receiving scheme administrator would give the member the option of deciding whether they wanted to use the transfer to buy final salary membership or career average pension in relation to the transferred service (which in the LGPS would have provided them with underpin protection). Quotations would be provided to help members make an informed choice.

92. It should be noted that, in certain situations, a transferring member might be at an advantage if the transitional protection could continue in their new scheme (for example, if members transferring into the LGPS were to obtain underpin protection for protected service they transfer in, or LGPS members transferring out were to obtain a choice in their new schemes). However, such an approach would likely lead to significant administrative complexity across the public sector.

93. We propose that, consistent with existing LGPS regulations[39] that, where a member with final salary membership in another public service pension scheme transfers that membership into the LGPS, and they would have met the qualifying criteria for underpin protection in the LGPS had they been a member of the scheme, they would be granted underpin protection for their LGPS membership up to 31st March 2022. This would apply even if the initial transfer into the LGPS was not a Club transfer.

94. We welcome views from respondents on the options set out here. The final approach in relation to transfers within the Public Sector Transfer Club will be considered across Government, taking into account the responses to this consultation along with those to the wider consultation.

Non-Club transfers

95. Where a qualifying member transfers relevant scheme membership and the transfer is not a 'Club' transfer[40], a different approach is proposed. The date of transfer would be their underpin crystallisation date. In the draft regulations we propose the detailed requirements in relation to such cases will be contained in actuarial guidance issued by the Secretary of State. We propose that the actuarial guidance we issue will require the following approach:

1) Calculate Cash Equivalent Transfer Values (CETVs) of the following:

   a) the member's accrued rights,

   b) the member's 'provisional assumed benefits' (see **annex C**), and

   c) the member's 'provisional underpin amount' (see **annex C**).

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[39] Regulation 9(1) and (2) of the 2014 Regulations

[40] Either because it is not a transfer to a pension scheme in the Public Sector Transfer Club, or because it does not qualify as a Club transfer.

2) Where c) is greater than b), add the difference between the two amounts to a) and that is the total CETV.

3) Where c) is not greater than b), just pay the CETV based on the member's accrued rights (i.e. the CETV calculated at a)).

96. This approach would be consistent with the general approach taken to calculating pension benefits under the underpin, and should achieve a similar outcome.

97. Where a member with underpin protection has transferred in pension rights from another scheme that is not a public service pension scheme, the value of the transfer would not be taken into account for the purposes of the member's underpin calculations. This is the same as applies in relation to transfers under the existing underpin regulations.

Other ways of taking benefits

98. **Flexible retirement** – Where a qualifying member makes an election to reduce their working hours or grade in an employment, with their employer's consent, that would be their underpin date, even though they remain in active employment after this date. As applies under the existing underpin provisions, no further underpin protection would apply after a qualifying member's date of flexible retirement. The underpin crystallisation date calculation, also undertaken at the point of a member's flexible retirement, would take into account the impacts of early and late retirement factors to determine which scheme benefit is better for the individual.

99. Where a qualifying member takes 'partial' flexible retirement, i.e. they do not take all the benefits they accrued prior to their flexible retirement date straight away, there is a question about the appropriate treatment of the underpin. We propose that, in partial flexible retirement situations, where there is an addition to the member's pension arising from the underpin (i.e. because the 2008 Scheme benefit is higher), the amount of the addition given to the member at that point in time should be proportionate to the amount of the 2014 Scheme pension they are choosing to receive. For example, if a member is only receiving 20% of their 2014 Scheme pension upon flexibly retiring, they would only receive 20% of the underpin addition. The remainder would be payable at the point the member takes the rest of their benefits.

100. **Redundancy**[41] – Redundancy below a qualifying member's 2008 Scheme NPA would trigger their underpin date. For members aged 55 or over, who have an immediate entitlement to their pension at point of redundancy, the date their redundancy pension commences would also be their underpin crystallisation date. As actuarial reductions do not apply in this situation, no account should be taken of these in the final underpin comparison. However, actuarial increases, where the member is made redundant after their 2008 Scheme or 2014 Scheme NPA, should be considered in the usual way.

101. **Trivial commutation**[42] – Under regulation 34 of the 2013 Regulations, members with small total pension rights can extinguish their future right to a pension from the scheme

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[41] This paragraph also covers members leaving active membership of the LGPS on grounds of business efficiency.

[42] This paragraph also covers members taking benefits via any of the other means referred to in regulation 34 of the 2013 Regulations. These payments are made at the discretion of administering authorities.

and receive a lump sum instead ('trivial commutation'). Under our proposals, qualifying members trivially commuting their pension will already have had their underpin date, as at their date of leaving the LGPS or reaching their 2008 Scheme NPA. If a qualifying member has not yet taken their pension, the date they trivially commute their benefits would be their underpin crystallisation date and the draft regulations propose the detailed requirements in relation to such cases will be contained in actuarial guidance issued by the Secretary of State. This is consistent with the general approach set out in the 2013 Regulations[43]. We propose that the actuarial guidance we issue will require the following approach:

1) Calculate the trivial commutation sum due of the following:

a) the member's total accrued rights,

b) the member's 'provisional assumed benefits' (see **annex C**), and

c) the member's 'provisional underpin amount' (see **annex C**).

2) Where c) is greater than b), add the difference between the two amounts to a) and that is the total sum due.

3) Where c) is not greater than b), just pay the trivial commutation sum based on the member's accrued rights (i.e. the sum calculated at a)).

102. This approach would be consistent with the general approach taken to calculating pension benefits under the underpin, and should achieve a similar outcome. Where a qualifying member who trivially commutes their benefits has already taken their pension from the LGPS (and had an underpin crystallisation date in doing so), there would be no further underpin calculations due at the point of the trivial commutation.

Question 14 – Do you have any comments regarding the proposed approaches outlined above?

Question 15 – Do you consider there to be any notable omissions in our proposals on the changes to the underpin?

Supplementary matters

Annual benefit statements

103. Pension schemes are vitally important workplace benefits. For many people contributing to a pension scheme, the annual benefit statement (ABS) is the main way that they receive updates on the value of their pension and when they will be able to receive it. Whilst it is true that information presented on an ABS about the underpin cannot provide certainty to a qualifying member on their underpin protection (in most cases, there will not be certainty until a member's underpin crystallisation date), we believe it is important that estimates are provided on member ABSs if scheme regulations are amended in the

[43] Regulation 34(2) of the 2013 Regulations requires that payments of the description contained in regulation 34(1) are to be calculated in accordance with actuarial guidance issued by the Secretary of State.

manner outlined in this paper. Appropriate wording would need to be considered so that members have the information needed to understand how the underpin works and that the figures included in their statement are provisional, and may change. We would plan to ask the Scheme Advisory Board to lead on agreeing standardised wording that LGPS funds thoughout England and Wales can include in ABSs regarding underpin protection.

104. Our draft regulations propose the following approach for members who meet the underpin qualifying criteria and have relevant scheme membership:

- That where a member is in active service below their 2008 Scheme NPA, their ABS should estimate the value of the underpin to the individual as if the end of the Scheme year[44] was their underpin date – including the provisional assumed benefits, the provisional underpin amount and any provisional guarantee amount.

- That where a member remains in active service beyond their 2008 Scheme NPA, their ABS should include the provisional estimates from the member's underpin date, as updated to reflect cost of living changes to the end of the Scheme year.

- For deferred and deferred pensioner members[45], their ABS should include the provisional estimates from the member's underpin date, as updated to reflect cost of living changes to the end of the Scheme year.

Question 16 – Do you agree that annual benefit statements should include information about a qualifying member's underpin protection?

Question 17 – Do you have any comments regarding how the underpin should be presented on annual benefit statements?

Annual allowance

105. The annual allowance is the maximum amount of tax-relieved pension savings that can be accrued by an individual in a year. The standard annual allowance is currently £40,000, but for those on the highest incomes, it tapers down to a minimum level of £10,000 (from April 2016 to March 2020) and to £4,000 (from April 2020). For defined benefit pension schemes like the LGPS, liability for tax charges above the annual allowance is calculated using the value of pension accrued in a particular year. Where an individual's pension accrual in a single year exceeds the annual allowance, then a tax charge may be due on the amount accrued above the member's annual allowance[46] to claw back the excess tax relief.

106. Whilst we would not expect a significant number of qualifying members to experience any change to their tax liability as a result of the proposals in this consultation document, it

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[44] Under Schedule 1 of the 2013 Regulations, a period of one year beginning with 1st April and ending with 31st March.
[45] Deferred pensioner members are members who were previously in receipt of a temporary tier 3 ill-health pension which has since ceased, and the member has not yet taken their main scheme benefits.
[46] However, 'carry forward' provisions allow members to carry forward unused annual allowance for the previous three years.

is important that underpin protection is considered for the purposes of determining a qualifying member's annual allowance.

107. LGPS regulations do not contain detailed provisions regarding the application of pensions tax to scheme benefits. Scheme administrators must follow the pensions tax framework as set out in the Finance Act 2004 and secondary legislation, and as explained in HMRC's Pensions Tax Manual[47]. Consistent with our approach generally, we do not plan to include in scheme regulations specific details regarding the tax treatment of the revised underpin.

108. We understand that, in accordance with guidance provided by the Local Government Association (LGA)[48], LGPS administrators have generally been taking the following approach in relation to the current underpin and the annual allowance:

- Whilst a protected member is in active service and their underpin date has not yet occurred, no account has been taken of a member's underpin protection for the purposes of determining a member's pension input amount in a given pension input period. This reflects that, under existing scheme regulations, a member may only receive an addition to their pension at the point of their underpin date.

- In the year of a protected member's underpin date, any addition in the member's pension arising from the comparison undertaken at the member's underpin date would be considered for the purposes of determining a member's pension input amount in that pension input period.

109. Whilst interpretation and application of the requirements of the Finance Act 2004 is a matter for individual administrators to consider, we believe that this approach is correct and would remain so if our proposals were to be implemented in scheme regulations. However, a change will be needed to reflect that, under our proposals, the point where an addition may arise from the underpin would be different. As described in paragraphs 61 and 62, our proposal is that the underpin moves to a 'two stage process'. Under this, a member's underpin protection can only result in a change to their pension entitlement at their 'underpin crystallisation date' and under our proposals it would be in this pension input period that the underpin should first be given consideration for the purposes of the annual allowance. As there would be no change to a member's pension entitlement at the point of a member's underpin date, the underpin should not be given consideration for annual allowance purposes in that pension input period[49].

110. However, we recognise that there may be circumstances where this approach means that a qualifying member has a higher pension input amount in the year of their underpin crystallisation date than an approach where the potential value of the underpin is considered on a year-by-year basis whilst a qualifying member remains in active membership. This may particularly be the case for qualifying members who have a relatively low career average pension for the years from 1st April 2014 to 31st March 2022, but a relatively high final salary pension over the same period. This may occur where a

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[47] https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual
[48] 'The Underpin' technical guide, latest version v1.8 (dated 18/07/2018), http://lgpsregs.org/resources/guidesetc.php
[49] Except where the member's underpin crystallisation date occurs in the same pension input period.

qualifying member is at an early stage of their career now, but goes on to be a high-earner in the future. We would appreciate views from stakeholders on the potential likelihood of this issue arising, the scale of the issue and how any impacts might be mitigated, if appropriate.

Question 18 – Do you have any comments on the potential issue identified in paragraph 110?

Public sector equality duty

111. The Ministry of Housing, Communities and Local Government has analysed the proposals set out in this consultation document (MHCLG) to fulfil the requirements of the Public Sector Equality Duty (PSED) as set out in section 149 of the Equality Act 2010. This requires the department to pay due regard to the need to:

1) eliminate unlawful discrimination, harassment and victimisation and other conduct prohibited by the Act
2) advance equality of opportunity between people who share a protected characteristic and those who do not
3) foster good relations between people who share a protected characteristic and those who do not.

Data

112. In undertaking our assessment of the equalities impacts of our proposals, we have drawn upon analysis provided to us by GAD. The analysis particularly looks at the protected characteristics of age and sex and is based on membership data supplied to GAD by LGPS administrators as at 31st March 2019. The following points should be borne in mind when considering the analysis:

- GAD's analysis has principally considered those who would benefit from the proposals outlined in this consultation. Members who already have underpin protection under existing provisions (being those aged 62 and older on 31st March 2019, who were aged at least 55 on 1st April 2012) have not been considered directly.

- GAD's analysis is based on active membership records totalling 1.68mn. The analysis has been conducted on a per-member basis, meaning additional records where members have more than one active employment have been removed.

- The proportion of the qualifying membership which is eventually likely to be better off as a result of underpin protection is heavily influenced by the rate of future pay growth in the LGPS. Consistent with the assumption used for the 2016 valuations of public service pension schemes, the long-term annual future pay growth assumption used is CPI + 2.2%.

- The analysis is based on the LGPS's active membership as at 31st March 2019. Under our proposals, the proposed changes to the underpin would be backdated to 1st April 2014. We would therefore expect that a number of additional members not

included in the analysis would benefit from our proposals. However, we do not anticipate this limitation would significantly change the results of the analysis.

- The analysis is based on an "average" member at each particular age. Allowing for variations in individual members' future service or salary progression could produce different figures.

113. Limited data specific to the LGPS in England and Wales is available in relation to other protected characteristics. However, we have considered wider data from the Labour Force Survey (LFS) (Q1 2020)[50] and the Annual Population Survey (APS) (2019)[51] in looking at the potential impacts of the following characteristics.

Age

114. The proposals outlined here are intended to remove age discrimination, which had been found to be unlawful in the firefighters' and judicial pension schemes, from the LGPS rules governing the underpin. We consider that the changes proposed will significantly reduce differential impacts in how the underpin applies based on a member's age, by removing the age-related qualifying criteria found to be unlawful by the Courts.

115. Based on analysis undertaken by GAD on active membership data for the LGPS as at 31st March 2019, we anticipate that some differences in how the revised underpin would apply to members of different age groups would remain. These are described below, along with our assessment of these differences.

116. **Qualification for the underpin –** GAD's analysis shows that older active members on 31st March 2019 would be more likely to qualify for the revised underpin than younger active members. This is principally because of our proposal that the 31st March 2012 qualifying date for underpin protection is retained. The proportion of members active in the scheme as at 31st March 2019 who had been members of the scheme on 31st March 2012 is lower for younger members, as experience shows they have a higher withdrawal rate from active scheme membership. We consider that members joining the LGPS after 31st March 2012 do not need to be provided with underpin protection. Members joining the LGPS after 31st March 2012 fall into two groups:

a) members who joined after 1st April 2014 when the LGPS had already reformed to a career average structure, and

b) members who joined between 1st April 2012 and 31st March 2014, who joined the LGPS when it was still a final salary scheme, but when a well-publicised reform process was already underway.

117. In relation to both groups, it is the Government's view that providing them underpin protection would not be appropriate. Transitional protection, as applied across public

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50 https://www.ons.gov.uk/surveys/informationforhouseholdsandindividuals/householdandindividualsurveys/labourforcesurvey

51 https://www.nomisweb.co.uk/articles/1167.aspx#:~:text=The%20Annual%20Population%20Survey%20(APS,regional%20(local%20authority)%20areas.

service pension schemes, was always designed to help members with the transition from the old scheme designs to the new (in the LGPS, mainly in relation to the move from a final salary to a career average structure). Members who joined after 31st March 2012 will have joined the LGPS when either it had already transitioned to the career average structure, or when it was well publicised that the LGPS benefits were reforming.

118. **Members who benefit from the underpin** – GAD's analysis shows that active members between the ages of 41 and 55 would be more likely to benefit from the revised underpin (i.e. where the calculated final salary benefit is higher than the calculated career average benefit) than both their younger and older colleagues. This reflects previous experience and future expectation that:

- this group are more likely than older colleagues to experience the pay progression that would make the final salary benefit higher over the underpin period (bearing in mind that the career average accrual rate (1/49ths) is better than the final salary accrual rate (1/60ths) so above inflation pay increases are needed for the underpin to lead to an increase in pension), and

- this group are more likely than younger colleagues to remain in active membership until they receive the pay progression necessary for the underpin to result in an addition to their pension. Younger members are estimated to have a higher voluntary withdrawal rate than older members, and so would be less likely to remain in the LGPS until such time as they have the pay increases for the final salary benefit to be higher.

119. These differential impacts reflect the fact that final salary schemes typically benefit members with particular career paths (for example, they usually favour high-earners with long service). The Government proposes to move all local government pensions accrual to a career average basis, without underpin protection, from April 2022 to apply a fairer system to all future service.

Sex

120. In relation to sex, GAD's analysis shows that broadly the proportion of men and women who would qualify for the revised underpin protection and benefit from that protection matches the profile of the scheme. As at 31st March 2019:

- 74% of scheme members were female, and 26% male

- 73% of the scheme members who were estimated to qualify for the revised underpin protection were female, and 27% male

- 73% of the scheme members who were estimated to benefit from the revised underpin were female, and 27% male

121. Proportionally, GAD's assessment is that men would be marginally more likely to qualify for the revised underpin and to benefit to a greater extent from underpin protection than women. This reflects the fact that, in line with previous scheme experience, the average male LGPS member would be expected to have higher salary progression than the average woman and that women are generally expected to have higher voluntary withdrawal rates than men. Members with longer scheme membership and with higher

salary progression would be more likely to receive an addition to their pension through the underpin (i.e. where the final salary benefit is higher).

122. These small differential impacts also demonstrate some of the effects that can arise under a final salary design. The Government proposes to move all local government pensions accrual to a career average basis, without underpin protection, from April 2022 to apply a fairer system to all future service.

Other protected characteristics

123. As noted in paragraph 113, limited data specific to the LGPS in England and Wales is available in relation to other protected characteristics. However, we have considered wider data from the LFS (Q1 2020) and the APS (2019) in looking at these characteristics. The LFS breaks down results to public sector level, which we have used as a proxy for LGPS membership for ethnicity, disability and marital status. For religion, the APS has been used as a proxy for the public service pension schemes as it also incudes a public sector breakdown.

124. Whilst these data sets show some differences in the demographic make-up of the UK population generally and the public sector workforfce, we do not consider that the changes to underpin protection proposed in the consultation will result in any differential impact to LGPS members with the following protected characteristics: disability, ethnicity, religion or belief, pregnancy and maternity, sexual orientation and marriage/civil partnership.

125. Data on sexual orientation, gender reassignment, pregnancy and maternity is not available. However, we expect there to be no differential impacts in relation to these groups as they won't be explicitly affected by any changes to transitional arrangements.

Next steps

126. Whilst we have detailed data on the protected characteristics of age and sex in relation to the LGPS membership, we are aware that our analysis of the impacts on other protected characteristics may be limited as it has not been based on local government specific data. We welcome suggestions from stakeholders of other data sets that may be available that may help us better understand the impacts on the LGPS membership more specifically.

127. We welcome views from stakeholders on our analysis, which is set out in more detail in the equalities impact assessment published alongside this consultation. These views will be considered in determining how to proceed following the consultation exercise. The potential equalities impacts of our proposals will be kept under review. A further equalities impact assessment will be undertaken following the consultation at the appropriate juncture.

Question 19 – Do the proposals contained in this consultation adequately address the discrimination found in the 'McCloud' and 'Sargeant' cases?

Question 20 – Do you agree with our equalities impact assessment?

Question 21 - Are you aware of additional data sets that would help assess the potential impacts of the proposed changes on the LGPS membership, in particular for the protected characteristics not covered by the GAD analysis (age and sex)?

Question 22 – Are there other comments or observations on equalities impacts you would wish to make?

Implementation and impacts

128. Following the closure of the consultation, we will consider the consultation responses received in detail to determine the best approach for removing the unlawful age discrimination from LGPS regulations.

129. The draft regulations at **annex B** have been prepared based on existing powers under the Public Service Pensions Act 2013. However, as noted in the wider Government consultation[52] on removing the unlawful age discrimination from public service pension schemes, the Government intends to bring forward new primary legislation regarding public service pensions. When proposals for removing the unlawful discrimination are finalised, further consideration will be given to the appropriate powers for the changes, based on the legislation in force at the time.

130. We recognise that in the period between now and scheme regulations being amended, some members of the scheme who would be due to benefit from the changes outlined in this paper will crystallise scheme benefits. This will include voluntary age retirements, as well as ill-health retirements, redundancies and transfers. There will also be dependants of those qualifying members who sadly die before changes are implemented. In respect of all such cases, we would expect the retrospective application of our proposed amending regulations to ensure that, overall, members and their dependents would get the full benefit of the revised underpin.

Communications

131. As noted in paragraphs 103 and 104, member communications in relation to the proposals outlined here will be vitally important to ensure members understand what underpin protection is and how it may or may not apply to them. This is particularly important due to the complexities of the underpin. The two-stage process we describe in paragraphs 61 and 62 is designed to protect members and to provide clarity, but it is important its purpose is well explained, so that qualifying members understand that they may have an addition to their pension arising from the underpin, even if there was not an addition at their underpin date. Equally, qualifying members should be aware that the benefits payable from the 2014 Scheme are very good, and, for many, underpin protection will not result in an increase to their pension entitlement.

132. Communications aimed at scheme employers will also be important so that they understand the proposed changes, particularly bearing in mind the number and variety of LGPS employers (just over 18,000 in 2018/19). The changes outlined in this paper would lead to an upward pressure on scheme liabilities and, potentially, to future increases in employer contributions. It is vital that employers understand the potential changes and

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[52] https://www.gov.uk/government/consultations/public-service-pension-schemes-consultation-changes-to-the-transitional-arrangements-to-the-2015-schemes

how they may impact their funding position. More generally, employers would have a practical role in providing the data necessary for scheme administrators to deliver the changes outlined in this document, and should understand how these changes may impact upon them.

133. Achieving good communications, and deciding on the appropriate medium for those communications, will require input from stakeholders across the LGPS, including administering authorities, employers and trade unions. We are aware that the Scheme Advisory Board has already commenced discussions with the sector on communications and we are strongly supportive of this continuing. We will continue working with the Scheme Advisory Board on this in the coming months.

Question 23 – What principles should be adopted to help members and employers understand the implications of the proposals outlined in this paper?

Administration impacts

134. We are conscious that the proposals outlined in this consultation paper would require significant changes to administration practices and systems. Amongst other matters, local administrators would need to consider the appropriate prioritisation of cases after amendments to regulations are made. Recognising that the LGPS is a single scheme, albeit locally administered, we are supportive of there being consistency across the scheme in respect of prioritisation and hope to work with the sector and the Scheme Advisory Board to agree a standard approach.

135. Priorisation decisions will be influenced by the fact that the revised underpin would have retrospective effect to April 2014, meaning that some members would already be in receipt of pensions that would need to be re-calculated, and retrospectively applied, in line with the new regulations.

136. A major challenge of implementing the changes proposed would apply in respect of obtaining additional data from employers for members who are newly benefitting from underpin protection – estimated to be around 1.2 million individuals. Under the 2014 Scheme, certain member data which was required for administering the 2008 Scheme (such as details of members' working hours and breaks in service) are not required for calculating member benefits. To administer the revised underpin, administrators would need to obtain this data for qualifying members for the period back to April 2014. This would be a highly significant exercise for the scheme's 87 administering authorities and its 18,000 employers. Particular challenges are likely to arise where employers have changed their payroll provider, and the data isn't stored in current systems.

Question 24 – Do you have any comments to make on the administrative impacts of the proposals outlined in this paper?

Question 25 – What principles should be adopted in determining how to prioritise cases?

Question 26 – Are there material ways in which the proposals could be simplified to ease the impacts on employers, software systems and scheme administrators?

137. We are grateful to the Scheme Advisory Board for their work on this project so far, in particular for their input on the remedy proposals outlined in this paper and for their establishment of working groups to consider some of the complex issues associated with this project.

138. We will continue working closely with the Scheme Advisory Board after the closure of the consultation as the sector prepares for the potential changes to scheme regulations. In particular, we intend to ask that the Scheme Advisory Board consider what guidance may be necessary to help administrators implement the proposed changes, and we are grateful for respondents' views on this.

139. Guidance would help support a consistent approach across the LGPS which would be desirable, in particular on matters like prioritisation. It would also potentially help on the complex issues connected with the fact that scheme employers would need to provide administrators with membership data going back to April 2014.

Question 27 – What issues should be covered in administrative guidance issued by the Scheme Advisory Board, in particular regarding the potential additional data requirements that would apply to employers?

Question 28 – On what matters should there be a consistent approach to implementation of the changes proposed?

Costs

140. The LGPS is a locally administered, funded scheme with three-yearly funding valuations to determine employer contribution rates. The next funding valuation is due on 31st March 2022[53]. Employer contribution rates are, in most cases, determined on an individual employer basis, and take into account a number of factors, some related to the individual employer (such as membership demographics) and some related to the fund more broadly (such as the peformance of fund investments since the previous valuation).

141. As a result of this backdrop, it is not possible to say how these changes would impact employer contribution rates at future valuations. However, the proposals in this paper can only lead to improvements in scheme benefits for qualifying members and, by necessity, there will be an upward pressureon liabilities. Because a variety of factors influence LGPS employer contribution rates, this upward pressure does not necessarily mean any particular employer's contributions will go up as a result of these changes, and administering authorities are required to smooth employer contributions as far as possible over the long term. Where any fund or employer would like to understand how these proposals may affect their own position, they should speak to their fund actuary. As scheme liabilities predominantly sit with local authorities and other public bodies, which are

[53] Under regulation 64 of the 2013 Regulations. In 2019, we consulted on potential changes to the funding valuation cycle - https://www.gov.uk/government/consultations/local-government-pension-scheme-changes-to-the-local-valuation-cycle-and-management-of-employer-risk. The Government has not yet responded to the proposal on the LGPS valuation cycle.

largely taxpayer funded, any employer contribution increases that do arise would need to be met, for the most part, by the taxpayer.

142. At a scheme level, costing estimates have been provided by the scheme actuary[54], the Government Actuary's Department, based on data provided by LGPS funds for the 2016 valuation. Assuming future member experience replicates the 2016 scheme valuation assumptions[55] the future cost to LGPS employers could be around £2.5bn in the coming decades. This is between 4% and 5% of the expected cost of benefits earned over the proposed underpin period, April 2014 to March 2022. However, if, for example, long-term real earnings growth were around a third lower than assumed for the 2016 valuation, we estimate the cost would roughly halve.

143. The costs are sensitive to both individual member experience and future pay. Predicting whether the underpin becomes valuable in the future depends heavily on assumptions on long-term future pay growth trends. In this estimate, we have used the 2016 valuation assumption that annual long-term pay growth is CPI + 2.2%. However, if long-term pay growth in the LGPS is lower than this, the costs may be lower (and vice versa).

144. The Government cost control mechanism was paused in February 2019 given the uncertainty arising from the McCloud judgment. The Government has made a separate announcement on the cost control mechanism[56]. In addition to the main Government cost control mechanism for the LGPS, the LGPS has a separate cost control process run by the Scheme Advisory Board[57] which was also paused as a result of the uncertainty arising. We expect the Scheme Advisory Board will also take the decision to unpause their process following the Government's announcement.

Question 29 – Do you have any comments regarding the potential costs of McCloud remedy, and steps that should be taken to prevent increased costs being passed to local taxpayers?

[54] As appointed under regulation 114 of the 2013 Regulations
[55] Based on directions issued by HM Treasury and LGPS experience
[56] https://www.gov.uk/government/consultations/public-service-pension-schemes-consultation-changes-to-the-transitional-arrangements-to-the-2015-schemes
[57] Regulation 116 of the 2013 Regulations

About this consultation

This consultation document and consultation process have been planned to adhere to the Consultation Principles issued by the Cabinet Office.

Representative groups are asked to give a summary of the people and organisations they represent, and where relevant who else they have consulted in reaching their conclusions when they respond.

Information provided in response to this consultation, including personal data, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 2018 (DPA), the General Data Protection Regulation, and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, as a public authority, the Department is bound by the Freedom of Information Act and may therefore be obliged to disclose all or some of the information you provide. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

The Ministry of Housing, Communities and Local Government will process your personal data in accordance with the law and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties. A full privacy notice is included at annex A.

Individual responses will not be acknowledged unless specifically requested.

Your opinions are valuable to us. Thank you for taking the time to read this document and respond.

Are you satisfied that this consultation has followed the Consultation Principles? If not or you have any other observations about how we can improve the process please contact us via the complaints procedure.

Annex A

Personal data

The following is to explain your rights and give you the information you are be entitled to under the Data Protection Act 2018.

Note that this section only refers to your personal data (your name address and anything that could be used to identify you personally) not the content of your response to the consultation.

1. **The identity of the data controller and contact details of our Data Protection Officer**
The Ministry of Housing, Communities and Local Government (MHCLG) is the data controller. The Data Protection Officer can be contacted at dataprotection@communities.gov.uk

2. Why we are collecting your personal data
Your personal data is being collected as an essential part of the consultation process, so that we can contact you regarding your response and for statistical purposes. We may also use it to contact you about related matters.

3. Our legal basis for processing your personal data
Section 21(1) of the Public Service Pension Act 2013 states:

'Before making scheme regulations the responsible authority must consult such persons (or representatives of such persons) as appear to the authority likely to be affected by them'.

MHCLG will process personal data only as necessary for the effective performance of this duty. In this case, the Secretary of State is the responsible authority for the LGPS in England and Wales.

The Data Protection Act 2018 states that, as a government department, MHCLG may process personal data as necessary for the effective performance of a task carried out in the public interest. i.e. a consultation.

3. With whom we will be sharing your personal data
We do not anticipate sharing personal data with any third party.

4. For how long we will keep your personal data, or criteria used to determine the retention period.
Your personal data will be held for two years from the closure of the consultation.

5. Your rights, e.g. access, rectification, erasure
The data we are collecting is your personal data, and you have considerable say over what happens to it. You have the right:

a. to see what data we have about you

b. to ask us to stop using your data, but keep it on record
c. to ask to have all or some of your data deleted or corrected
d. to lodge a complaint with the independent Information Commissioner (ICO) if you think we are not handling your data fairly or in accordance with the law. You can contact the ICO at https://ico.org.uk/, or telephone 0303 123 1113.

6. Your personal data will not be sent overseas

7. Your personal data will not be used for any automated decision making.

8. Your personal data will be stored in a secure government IT system.

Annex B – Draft regulations

S T A T U T O R Y   I N S T R U M E N T S

2020 No.

PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

The Local Government Pension Scheme (Amendment) Regulations 2020

Made - - - -	***
Laid before Parliament	***
Coming into force - -	***

The Secretary of State makes the following Regulations:

Citation, commencement and extent

1.—(1) These Regulations may be cited as the Local Government Pension Scheme (Amendment) Regulations 2020.

(2) These Regulations come into force on [XXXXXX] but regulations 2, 4, 5 and 6 have effect from 1st April 2014.

(3) These Regulations extend to England and Wales.

Amendment of the Local Government Pension Scheme Regulations 2013

2. The Local Government Pension Scheme Regulations 2013([58]) are amended in accordance with regulations 3 and 4.

3. In regulation 89 (annual benefit statement) after paragraph (4) insert—

"(5) Where regulation 4 of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 applies the statement in respect of a relevant scheme membership must include the following additional information for active members who had not reached their 2008 Scheme normal retirement age at the end of the scheme year to which it relates—

(a) the provisional guarantee amount;

(b) the provisional assumed benefits; and

(c) the provisional underpin amount

which would apply if the member's underpin date was the closing date of the Scheme year to which the statement relates.

([58]) S.I. 2013/2356; those Regulations have been amended by S.I. 2014/44, S.I. 2014/525, S.I. 2014/1146, S.I. 2015/57, S.I. 2015/755, S.I. 2018/493,S.I.2019/1449.

(6) Where regulation 4 of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 applies the statement in respect of a relevant scheme membership must include the following additional information for deferred and deferred pensioner members—

(a) the provisional guarantee amount;

(b) the provisional assumed benefits; and

(c) the provisional underpin amount

calculated as at their underpin date and adjusted by the appropriate index rate adjustment to the end of the Scheme year to which the statement relates.

(7) Where regulation 4 of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 applies the statement in respect of a relevant scheme membership must include the following additional information for active members who had reached their 2008 Scheme normal retirement age at the end of the relevant Scheme year—

(a) the provisional guarantee amount;

(b) the provisional assumed benefits; and

(c) the provisional underpin amount

calculated as at their underpin date revalued to the end of the Scheme year to which the statement relates.

(8) The provisional guarantee amount is calculated in accordance with regulation 4(4) of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014.

(9) The provisional assumed benefits are calculated in accordance with regulation 4(5) of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014.

(10) The provisional underpin amount is calculated in accordance with regulation 4(6) of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014.

4.—(1) In Schedule 1 (interpretation) after the definition of "registered pension scheme" insert—

"relevant scheme membership" has the meaning given by regulation 4(1A) of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014;"

Amendment of the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014

5. The Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014([59]) are amended in accordance with regulation 6.

6. In regulation 4 (statutory underpin)—

(a) in paragraph (1)(a) omit the words from "and who on 1st April 2012" to the end;

(b) for paragraph (1)(b) substitute—

"(b) is or has been an active member of the 2014 Scheme; and"

(c) in paragraph (1)(c) substitute "; and" with ".";

(d) omit paragraph (1)(d);

(e) at the end insert—

"(1A) For the purpose of this regulation a member's relevant scheme membership is a single Scheme membership which meets the requirements of paragraph (1)(a), (1)(b) and (1)(c).

(1B) Where a member has had periods of concurrent employment, or a break in service that is not a disqualifying break in service, a member only has a relevant scheme membership if the member's scheme membership including the period referred to in paragraph (1)(a) has been aggregated with their 2014 Scheme pension account, following a decision taken under—

([59]) S.I. 2014/525.

(a) regulations 16 or 17 of the Administration Regulations, where the member has subsequently joined the 2014 Scheme by virtue of regulation 5(1),

(b) regulations 10(5) or (6) of these Regulations, or

(c) regulations 22(5), 22(6), 22(7) or (8) of the 2013 Regulations.

(1C) Paragraph (1D) applies where;

(a) an active or deferred member would otherwise have relevant Scheme membership;

(b) but prior to [XXXXXXXX] previous Scheme membership including the period referred to in paragraph (1)(a) had not been aggregated with the member's 2014 Scheme pension account under paragraphs (1B)(a), (1B)(b) or (1B)(c).

(1D) Where this paragraph applies, an active or deferred member has a twelve month period commencing from [XXXXXXXXX] to elect to aggregate the previous Scheme membership that would give the member relevant Scheme membership.

(f) in paragraph (2) for "The underpin date" substitute "Subject to paragraphs (2A) and (2B) a member's underpin date in a relevant Scheme membership";

(g) for paragraph (2)(b) substitute—

"(b) the date the member ceased to be an active member of the 2014 Scheme in an employment with a deferred or immediate entitlement to a pension; or";

(h) after paragraph 2(b) insert—

"(c) the date a member elects with their Scheme employer's consent to receive immediate payment under regulation 30(6) of the 2013 Regulations."

(i) after paragraph 2 insert—

"(2A) A member's date of death shall be their underpin date in a relevant Scheme membership where that date is earlier than the date provided for by paragraphs (2)(a) or (2)(b).

(2B) A member to whom paragraph (2)(b) has applied may have further underpin dates under paragraphs (2) or (2A) where they have either—

(a) become an active member of the 2014 Scheme again before reaching their 2008 Scheme normal retirement age without a disqualifying break in service and aggregated their previous relevant scheme membership with their active member's pension account under regulation 22(8) of the 2013 Regulations, or

(b) continued in active membership of the 2014 Scheme in an employment which had been concurrent with the employment through which they had an underpin date under paragraph (2)(b) and aggregated their previous relevant scheme membership with their active member's pension account under regulation 22(7) of the 2013 Regulations."

(j) for paragraph (3) substitute—

"(3) For the purpose of this regulation a disqualifying break in service is a continuous break after 31st March 2012 of more than 5 years in active membership of a public service pension scheme."

(k) for paragraph (4) substitute—

"(4) A member's provisional guarantee amount in a relevant scheme membership is the amount by which a member's provisional underpin amount exceeds the provisional assumed benefits on their underpin date."

(l) after paragraph (4) insert—

"(4A) Where paragraph (2B) applies, the value of the member's provisional assumed benefits, provisional underpin amount and provisional guarantee amount as calculated at their latest underpin date must be used for the purpose of this regulation."

(m) for paragraph (5) substitute—

"(5) The provisional assumed benefits are calculated by assessing the benefits the member would have been entitled to under the 2014 Scheme in a relevant Scheme membership if—";

(n) in paragraph (5)(a) substitute "the underpin date" with "31st March 2022 or the member's underpin date, whichever date is the earlier";

(o) in paragraph (5)(b) substitute "the underpin date" with "31st March 2022 or the member's underpin date, whichever date is the earlier";

(p) after paragraph (5) insert—

"(5A) Where the member's pension has come into payment under regulation 35 of the 2013 Regulations, the provisional assumed benefits calculated in accordance with paragraph (5) must include any adjustment under regulation 39 of the 2013 Regulations for the period up to the earlier of the member's 2008 Scheme normal retirement age and 31st March 2022.

(5B) Where a member's underpin date has arisen under paragraph (2A), the provisional assumed benefits calculated in accordance with paragraph (5) must include the amount calculated under regulation 41(4)(b) of the 2013 Regulations for the period up to the earlier of the member's 2008 Scheme normal retirement age and 31st March 2022."

(q) for paragraph (6) substitute—

"(6) The provisional underpin amount is calculated by assessing the benefits the member would have had an immediate entitlement to payment of under the 2008 Scheme in a relevant Scheme membership if–"

(r) in paragraph (6)(a) substitute "the underpin date" with "31st March 2022 or the member's underpin date, whichever date is the earlier";

(s) in paragraph (6)(b)(iii)—

(i) substitute "the member's assumed benefits" with "the member's provisional assumed benefits";

(ii) at the end add "but limited to the earlier of the member's 2008 Scheme normal retirement age and 31st March 2022"

(t) after paragraph (6) insert—

"(6A) Where a member's underpin date has arisen under paragraph (2A), the provisional underpin amount calculated in accordance with paragraph (6) must include an amount equivalent to the enhancement that would apply under regulation 24(2) of the Benefits Regulations, for the period up to the earlier of the member's 2008 Scheme normal retirement age and 31st March 2022."

"(7) Subject to paragraph (8) a member's underpin crystallisation date in a relevant Scheme membership is the earliest of the following dates—

(a) the date from which the member elects to receive payment of a retirement pension under regulations 30(1), 30(5) or 30(6) of the 2013 Regulations;

(b) the date from which the member becomes entitled to receive payment of a retirement pension under regulation 30(7) of the 2013 Regulations;

(c) the date from which the member becomes entitled to an ill-health retirement pension under regulation 35(1) or regulation 38(1) of the 2013 Regulations;

(d) the date the member receives payment under regulation 34 of the 2013 Regulations;

(e) the date the member transfers their benefits out of the 2013 Regulations following;

(i) an application made under regulation 96 of the 2013 Regulations; or

(ii) by virtue of regulation 98 of the 2013 Regulations.

(f) the date a member dies.

(8) A deferred pensioner member who has had an underpin crystallisation date in a relevant Scheme membership pursuant to paragraph (7) following receipt of Tier 3 benefits has an additional underpin crystallisation date which is the earliest of the subsequent events referred to in paragraphs (7)(a) to (f).

(9) Where paragraphs 7(a), (b) or (c) apply to a member, the member's pension account must be increased by the final guarantee amount at the underpin crystallisation date.

(10) The final guarantee amount is the amount by which the final underpin amount exceeds the final assumed benefits on the underpin crystallisation date.

(11) Where a member who elects to receive payment of a retirement pension under regulation 30(6) of the 2013 Regulations has a final guarantee amount at their underpin crystallisation date, a proportion of that final guarantee amount equal to the proportion of the member's 2014 Scheme benefits that the member has elected to take under regulation 30(6) must be transferred to the member's flexible retirement pension account.

(12) A final guarantee amount payable to a member pursuant to paragraph (7)(a) and the remainder of the member's final underpin amount are payable to the member without further actuarial adjustment relating to the age at which the benefits are taken.

(13) When paragraph (7)(a) applies to a member the final assumed benefits for the member are the value of provisional assumed benefits calculated in accordance with paragraph (5) with the following adjustment—

(a) any revaluation adjustment or index rate adjustment that would have applied to the member's pension under the 2013 Regulations between the member's underpin date and their underpin crystallisation date; and

(b) any actuarial adjustment which would have applied under the 2013 Regulations, relating to the age at which the pension was taken.

(14) When paragraph (7)(a) applies to a member the final underpin amount is the value of the provisional underpin amount calculated in accordance with paragraph (6) but—

(a) updated to the underpin crystallisation date to include increases which would have applied under the Benefits Regulations by virtue of the Pension (Increase) Act 1971([60]) between a member's underpin date and their underpin crystallisation date; and

(b) including any actuarial adjustment which would have applied under the Benefits Regulations relating to the age at which the pension was taken.

(15) When paragraph (7)(b) or (c) applies to a member the final assumed benefits for the member are the value of provisional assumed benefits calculated in accordance with paragraph (5) with the following adjustment—

(a) any revaluation adjustment or index rate adjustment that would have applied to the member's pension under the 2013 Regulations between the member's underpin date and their underpin crystallisation date; and

(b) any actuarial increase which would have applied under the 2013 Regulations, relating to the age at which the pension was taken.

(16) When paragraph (7)(b) or (c) applies to a member the final underpin amount is the value of the provisional underpin amount calculated in accordance with paragraph (6) but—

(a) updated to the underpin crystallisation date to include increases which would have applied under the Benefits Regulations by virtue of the Pension (Increase) Act 1971 between a member's underpin date and their underpin crystallisation date; or

(b) including any actuarial increase which would have applied under the Benefits Regulations relating to the age at which the pension was taken.

(17) When paragraphs (7) (d), (e) (i) or (e)(ii) apply to a member the value of the payment due at a member's underpin crystallisation date must be calculated in accordance with actuarial guidance issued by the Secretary of State.

([60]) 1971 c. 56.

(18) A request for a cash equivalent value of a member's pension rights under Regulation 4 of the Pension Sharing (Valuation) Regulation 2000([61]) is not to be treated as a member's underpin date or underpin crystallisation date.

(19) A request made pursuant to paragraph (18) is to be calculated in accordance with actuarial guidance issued by the Secretary of State.

(20) Following the death of a person to whom this regulation applies, any provisional guarantee amount applicable at the member's underpin date must be updated to include any revaluation adjustment or index rate adjustment that would have applied to the member's pension under the 2013 Regulations between the member's underpin date and their date of death, and shall be known as the member's adjusted provisional guarantee amount.

(21) Where, pursuant to paragraph (20), a provisional guarantee amount applied at a deceased member's underpin date, the rate listed in column two of the below table must be applied to the adjusted provisional guarantee amount, to determine the addition to the relevant survivor benefit.

2013 Regulation	*Rate*
41(4)	49/160
42(4)	49/320
42(5)	49/160
42(9)	49/240
42(10)	49/120
44(4)	49/160
45(4)	49/320
45(5)	49/160
45(9)	49/240
45(10)	49/120
47(4)	49/160
48(4)	49/320
48(5)	49/160
48(9)	49/240
48(10)	49/120

(22) Where, pursuant to paragraph (20), a provisional guarantee amount applied at a deceased member's underpin date, the adjusted provisional guarantee amount must be used in determining the annual amount of pension the member would have been entitled to under regulations 43(3) and 46(3) of the 2013 Regulations.

We consent to the making of these Regulations

Names
Two of the Lords Commissioners of Her Majesty's Treasury

Signed by authority of the Secretary of State for Housing, Communities and Local Government

Name
Parliamentary Under Secretary of State
Ministry of Housing, Communities and Local Government

Date

([61]) S.I. 2000/1052.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Local Government Pension Scheme Regulations 2013 and the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 ("the Transitional Regulations"). Both sets of regulations came substantively into effect on 1st April 2014 and certain provisions listed in regulation 1 take effect from that date.

Regulations 2 to 4 amend the Local Government Pension Scheme Regulations 2013.

Regulations 5 and 6 amend the Transitional Regulations in regards to the operation of the underpin.

An impact assessment has not been produced for this instrument as no impact is anticipated on the private or voluntary sectors.

Annex C – The two-stage process

As outlined in paragraphs 61 and 62, we are proposing the introduction of a two-stage process for calculating a qualifying member's entitlement from the underpin. Under this, calculations would take place at a qualifying member's underpin date and their underpin crystallisation date. This annex contains further details on the proposals we set out in our draft regulations.

The underpin date – proposed approach

- A qualifying member's underpin date would be the earlier of:
  - the date they leave active service with an immediate or deferred entitlement to a pension,
  - the date they reach their 2008 Scheme NPA, or
  - the date they die.
- The underpin date would relate to a specific 'relevant scheme membership' – i.e. a single, aggregated (where appropriate), scheme membership in which the member:
  - was active in the LGPS on 31st March 2012,
  - had membership of the 2014 Scheme, and
  - did not have a disqualifying break in service.
- It is possible a qualifying member may have two (or more) relevant scheme memberships. Where this applies, they may have different underpin dates in respect of each one.
- At a qualifying member's underpin date, an initial comparison of the member's 2014 Scheme and 2008 Scheme benefits would be undertaken based on:
  - the member's 'provisional assumed benefits' in a relevant scheme membership – broadly[62], the career average benefits they have accrued in the 2014 Scheme over the underpin period[63], and
  - the member's 'provisional underpin amount' in a relevant scheme membership – broadly, the final salary benefits the member would have built up in the 2008 Scheme over the same period[64].

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[62] For members who have had a period in the 50/50 section of the 2014 Scheme, the underpin calculation assumes the member remained in the full section of the 2014 Scheme.
[63] The underpin period runs from 1st April 2014 to 31st March 2022, or to the member's underpin date where that is earlier than 31st March 2022.
[64] If the underpin date is after 31st March 2022, the member's final salary for the year up to their underpin date would be used for the purposes of calculating their provisional underpin amount.

- If the provisional underpin amount is higher than the provisional assumed benefits at a qualifying member's underpin date, the member would be awarded a 'provisional guarantee amount' in respect of that relevant scheme membership.

- A provisional guarantee amount is a provisional assessment that the 2008 Scheme benefits would have been better for the member. At a qualifying member's underpin date, there would be no change to their pension entitlement arising from the provisional guarantee amount[65]. However, annual benefit statements sent to the member after their underpin date would confirm if a provisional guarantee amount has applied.

- Qualifying members may have multiple underpin dates in respect of a relevant scheme membership. This may occur where:

    - The member has concurrent employments and ceases to be an active member in one before their 2008 Scheme NPA (in which they have relevant scheme membership). An underpin date would apply at the point the member leaves the LGPS in that post. If the member then aggregates their relevant scheme membership with their ongoing post, a further underpin date would apply at the earlier of the following:

        - the date they leave active service,

        - the date they reach their 2008 Scheme NPA, or

        - the date they die.

    - The member leaves an employment in which they have relevant scheme membership with an immediate or deferred entitlement to a pension. An underpin date would apply at their date of leaving. If the member then re-joins the LGPS and aggregates their membership (without a disqualifying break in service), a further underpin date would apply at the earlier of the following:

        - the date they leave active service,

        - the date they reach their 2008 Scheme NPA, or

        - the date they die.

- Where a qualifying member has multiple underpin dates, it would be their provisional amounts from their latest underpin date that would be used for the purposes of the calculations at their underpin crystallisation date.

[65] Unless their underpin crystallisation date immediately follows their underpin date – for example, if a member takes immediate payment of their benefits upon leaving the scheme.

The underpin crystallisation date – proposed approach

- As the period between a qualifying member's underpin date and the date they take their benefits from the LGPS could be as much as 30 or 40 years, we propose that all qualifying members have an underpin crystallisation date in respect of a relevant scheme membership. This would ensure the comparison can be made when there is certainty on the final actuarial adjustments that might be applied, and in respect of the member's State Pension age.

- A variety of circumstances would give rise to a qualifying member's underpin crystallisation date and, in general[66], a qualifying member can only have one underpin crystallisation date in respect of a relevant scheme membership. A qualifying member's underpin crystallisation date would be the earliest of the following in respect of a relevant scheme membership:

    - the date a member takes voluntary payment of their pension, at any age between 55 and 75,

    - the date a member takes flexible retirement,

    - the date a member aged 55 or over leaves active membership as a result of redundancy, or due to business efficiency,

    - the date a member retires on ill-health grounds,

    - the date a member transfers out or trivially commutes their benefits, or

    - the date a member dies.

- What happens at a qualifying member's underpin crystallisation date would vary, and is described in more detail for each circumstance in 'the revised underpin – application' section in the body of this document. In most cases, however, it would involve a member's provisional underpin amount and their provisional assumed benefits being updated to give a member's 'final underpin amount' and their 'final assumed benefits'. How the provisional figures are updated to become final figures would vary depending on the circumstance. The below table summarises what is proposed to apply under the draft regulations.

Circumstance giving rise to a member's underpin crystallisation date	**How provisional underpin amount and provisional assumed benefits calculated at a qualifying member's underpin date are updated at a member's underpin crystallisation date**

[66] An exception applies in relation to members who receive a temporary (tier 3) ill-health pension. For such members, they will have an underpin crystallisation date upon receiving their temporary ill-health pension and then a subsequent one when their underpin crystallises from 'deferred pensioner' status.

Voluntary age retirement or flexible retirement	• To include any cost of living increases that would have applied to the member's pension under the 2008 or 2014 Schemes between the member's underpin date and their underpin crystallisation date, and • To include any actuarial adjustments relating to the member's age, that would have applied under the 2008 or the 2014 Schemes.
Redundancy[67] and ill-health pension being paid (from active or deferred status)	• To include any cost of living increases that would have applied to the member's pension under the 2008 or 2014 Schemes between the member's underpin date and their underpin crystallisation date, and • To include any actuarial increases relating to the member's age, that would have applied under the 2008 Scheme and 2014 Scheme.

- Where a qualifying member's final underpin amount is higher than their final assumed benefits at their underpin crystallisation date, the member would be awarded a 'final guarantee amount' in respect of that relevant scheme membership. An addition would be made to their pension account in respect of that final guarantee amount.

- For certain types of underpin crystallisation, the draft regulations do not prescribe that members' provisional underpin amount and provisional assumed benefits are updated to give 'final' amounts. This applies in the following cases:

    - Transfers out – instead, administrators would need to comply with actuarial guidance issued by the Secretary of State, and the Public Sector Transfer Club memorandum, where appropriate
    - Trivial commutations – instead, administrators would need to comply with actuarial guidance issued by the Secretary of State
    - Deaths – instead, the regulations prescribe what should apply in relation to any survivor benefits that may be payable.

[67] Including termination on grounds of business efficiency

Annex D – Illustrative examples

This annex provides examples to illustrate how the proposed underpin would operate in different situations. These examples illustrate some (but not all) of the factors which may impact whether or not an underpin addition may apply in different situations.

The examples shown are:

1. Retirement from active service at age 65
2. Retirement from active service at State Pension age (‘SPa’)
3. Early retirement from active service at age 60
4. Deferred retirement with no underpin at underpin date
5. Deferred retirement with an underpin at underpin date

All the examples are based on a member aged 47 in 2012, who did not receive underpin protection originally. This member has a 2014 Scheme normal pension age equivalent to their SPa under the current timetable, 67.

The examples rely on the following assumptions:

- The pension calculated is the pension accrued over the underpin period (1st April 2014 to 31st March 2022), as payable at retirement. In practice, such members will also have pension relating to pre-2014 and post-2022 periods which is not considered here.
- Inflation reflects actual experience up to 2020, with 2% pa assumed thereafter; increases are applied on 1 April.
- Salary increases, promotions and retirements occur on 31st March in the relevant year.
- The current State Pension age timetable is followed.
- The pension amounts are in nominal terms at retirement.
- The amounts are shown rounded to the nearest £10.

Please note that these examples are for illustrative purposes only. Generally, they only consider one of the key variables which may impact how the proposed underpin would apply to a member, in practice other variables may also be significant. The comparisons are based on the pension payable at retirement.

Example 1 (retirement at age 65)

In **2012 the member was aged 47**, and so **did not receive underpin protection originally**. However, under our proposals, an underpin check would be undertaken to ensure that their benefits in the eight year underpin period are the greater of either:

2014 Scheme	2008 Scheme
1/49h of revalued salary each year Payable unreduced from State Pension age	1/60th of final salary each year Payable unreduced from age 65

In this example the member's underpin date will be the same as the underpin crystallisation date and, practically, only one check will be required.

As the member is taking their benefits immediately upon leaving, we can adjust the 2014 Scheme pension to allow for this being paid two years earlier than their 2014 Scheme normal pension age (age 67). No adjustment would be required in this example for the calculation of the 2008 Scheme benefit (as this would be paid without adjustment from age 65).

If the member had a **salary of £30,000 in 2014**, experiences future annual **salary increases of 1% above inflation** and **retires at age 65**, their pensions over the underpin period would be as follows:

2014 Scheme (age 65): £6,100 pa	2008 Scheme (age 65): £6,060 pa

In this example the member's 2014 Scheme benefits are higher and there would be **no underpin addition required.**

Alternatively

If the member was promoted twice, receiving **an additional 5% salary increase** at the end of the underpin period **and an additional 5% salary increase** five years later, the underpin is now more than the age-adjusted 2014 Scheme pension at age 65:

2014 Scheme (age 65): £6,100 pa	2008 Scheme (age 65): £6,670 pa

The **final guarantee amount** is the difference between these two amounts which equals £570. Following high salary increases the 2008 Scheme benefit structure becomes relatively more valuable and hence an **underpin addition** would be required**.** The 2014 Scheme benefit would be increased by the underpin addition of £570 per year.

Example 2 (retirement at SPa)

In **2012 the member was aged 47**, and so **did not receive underpin protection originally.** However, under our proposals, an underpin check would be undertaken to ensure that their benefits in the eight year underpin period are the greater of either:

2014 Scheme	2008 Scheme
1/49th of revalued salary each year Payable unreduced from State Pension age	1/60th of final salary each year Payable unreduced from age 65

In this example the member's underpin date will be when the member reaches age 65. At the underpin date the 2014 Scheme and 2008 Scheme benefits will be compared (with no allowance for actuarial adjustment).

If the member has the same **salary of £30,000 in 2014**, experiences future annual **salary increases of 1% above inflation** and **retires at Spa** (67, in this case), the comparison at the underpin date is as follows:

2014 Scheme (age 65): £6,770 pa	2008 Scheme (age 65): £6,060 pa

The check at the underpin date shows the 2014 Scheme benefits are greater than the 2008 Scheme benefits and therefore **no 'provisional guarantee amount'** is required.

A subsequent test will be carried out at the member's underpin crystallisation date, their retirement age, SPa (age 67), when the revalued pension amounts and correct actuarial adjustment factors are known. In both cases the provisional assumed benefits and provisional underpin amount will be revalued in line with cost of living between age 65 and retirement. No actuarial adjustment will be required for the 2014 Scheme benefit, however the 2008 Scheme benefit is increased by two years late retirement factors:

2014 Scheme (SPa): £7,040 pa	2008 Scheme (SPa): £6,770 pa

For this member **no underpin addition** would be required**.**

Alternatively

However, if the member was promoted twice, receiving **an additional 5% salary increase** at the end of the underpin period **and an additional 5% salary increase** five years later, the comparison at the underpin date (age 65) is now:

2014 Scheme (age 65): £6,770 pa	2008 Scheme (age 65): £6,670 pa

The check at the underpin date shows **no 'provisional guarantee amount'** is required.

A further check would be untaken when the member takes their pension at their underpin crystalisation date, SPa (age 67). This check shows that once revaluation and different actuarial adjustments are allowed for the 2008 Scheme benefits are higher and the difference or **final guarantee amount** would be £400. The member's 2014 Scheme benefit would be increased by an **underpin addition** of £400 per year.

2014 Scheme (SPa): £7,040 pa	2008 Scheme (SPa): £7,440 pa

Example 3 (early retirement)

In **2012 the member was aged 47**, and so **did not receive underpin protection originally**. However, under our proposals, an underpin check would be undertaken to ensure that their benefits in the eight year underpin period are the greater of either:

2014 Scheme	2008 Scheme
1/49h of revalued salary each year Payable unreduced from State Pension age	1/60th of final salary each year Payable unreduced from age 65

In this example the member's underpin date will be the same as the underpin crystallisation date and, practically, only one check will be required.

As the member is taking their benefits immediately upon leaving, we can adjust the 2014 Scheme pension to allow for this being paid seven years earlier than the 2014 Scheme normal pension age (SPa, age 67); and the 2008 Scheme benefits are also reduced to reflect that this is being paid five years earlier.

If the member had a **salary of £30,000 in 2014**, experiences future annual **salary increases of 1% above inflation** and **retires at age 60**, their pensions over the underpin period would be as follows:

2014 Scheme (age 60): £4,350 pa	2008 Scheme (age 60): £4,070 pa

In this example the member's 2014 Scheme benefits are higher and there would be **no underpin addition** required**.**

Alternatively

If the member was promoted twice, receiving **an additional 10% salary increase** at the end of the underpin period **and an additional 5% salary increase** five years later, the 2008 Scheme benefit is now more than the 2014 Scheme pension at age 60:

2014 Scheme (age 60): £4,350 pa	2008 Scheme (age 60): £4,460 pa

Following high salary increases the 2008 Scheme benefit structure becomes relatively higher and hence an **underpin addition** would now be required**.** The 2014 Scheme benefit would be increased by £110 pa.

Example 4 (retirement from deferment #1)

In **2012 the member was aged 47**, and so **did not receive underpin protection originally**. However, under our proposals, an underpin check would be undertaken to ensure that their benefits in the eight year underpin period are the greater of either:

2014 Scheme	2008 Scheme
1/49th of revalued salary each year Payable unreduced from State Pension age	1/60th of final salary each year Payable unreduced from age 65

The example shows how the underpin check would work where the member leaves service at age 58 (with a deferred pension) which they subsequently draw at age 67. Under our proposals, an initial underpin check would be undertaken at the date of leaving active service (their underpin date) which would compare the 2014 Scheme benefits with the 2008 Scheme benefits over the underpin period. This comparison would not consider the effect of actuarial adjustments for age, as these would not be known at the member's underpin date.

If they had a **salary of £30,000 in 2014**, experience future annual **salary increases of 1% above inflation** until **leaving the scheme at age 58,** the pensions over the underpin period would be as follows:

2014 Scheme: £5,890 pa	2008 Scheme: £4,930 pa

The check at the underpin date shows the 2014 Scheme benefits are greater than the 2008 Scheme benefits and **no 'provisional guarantee amount'** is required.

A subsequent underpin crystallisation test will be carried out when the member takes their pension at SPa (age 67), when the final revalued amounts and correct actuarial adjustment factors are known. In both cases the pension amounts will be revalued in line with cost of living between age 58 and retirement. No further actuarial adjustment will be required for the 2014 Scheme benefit, however the 2008 Scheme benefit is increased by two years' late retirement factors:

2014 Scheme (SPa): £7,040 pa	2008 Scheme (SPa): £6,320 pa

In this example the member's 2014 Scheme benefits are higher and there would be **no underpin addition** required**.**

Alternatively

If the member was promoted twice, receiving **an additional 5% salary increase** halfway through the underpin period and **an additional 10% salary increase** at the end of the underpin period, the calculations at the underpin date would show the 2014 Scheme benefits are higher:

2014 Scheme:
£6,040 pa

2008 Scheme:
£5,670 pa

A further test would be undertaken at the underpin crystallisation date; when the member retires (SPa, age 67). This check shows that once revaluation and different actuarial adjustments are allowed for the 2008 Scheme benefits are higher and the difference or **'final guarantee amount'** would be £50.

2014 Scheme (SPa):
£7,220 pa

2008 Scheme (SPa):
£7,270 pa

Following high salary increases the 2008 Scheme benefit structure becomes relatively more valuable and hence an underpin addition would now be required. The 2014 Scheme benefit would be increased by £50 pa.

Example 5 (retirement from deferment #2)

In **2012 the member was aged 47**, and so **did not receive underpin protection originally**. However, under our proposals, an underpin check would be undertaken to ensure that their benefits in the eight year underpin period are the greater of either:

2014 Scheme	2008 Scheme
1/49h of revalued salary each year Payable unreduced from State Pension age	1/60th of final salary each year Payable unreduced from age 65

This example shows how the underpin check would work where the member leaves service at age 63 (with a deferred pension) which they subsequently draw at age 67. Under our proposals, an initial underpin check would be undertaken at the date of leaving active service (their underpin date) which would compare the 2014 Scheme benefits with the 2008 Scheme benefits over the underpin period. This comparison would not consider the effect of actuarial adjustments for age, as these would not be known at the member's underpin date.

If the member has a **salary of £30,000 in 2014**, experiences future annual **salary increases of 1% above inflation**, **an additional 10% salary increase** halfway through the underpin period and **an additional 10% salary increase** at the end of the underpin period until **leaving the scheme at age 63,** the relative pensions over the underpin period would be as follows:

2014 Scheme:	2008 Scheme:
£6,830 pa	£6,870 pa

In this example there is a **'provisional guarantee amount'** of £40 pa**.**

A subsequent test will be carried out at the member's underpin crystallisation date, their retirement age, SPa (age 67), when the final revalued amounts and correct actuarial adjustment factors are known. In both cases the pension amounts will be revalued in line with cost of living between age 63 and retirement. No further actuarial adjustment will be required for the 2014 Scheme benefit, however the 2008 Scheme benefit is increased by two years' late retirement factors:

2014 Scheme (SPa):	2008 Scheme (SPa):
£7,390 pa	£7,980 pa

This check shows that once revaluation and different actuarial adjustments are allowed for, the 2008 Scheme benefits are higher and the difference or **final guarantee amount**

would be £490. The member’s 2014 Scheme benefit would be increased by an **underpin addition** of £490pa.

This again illustrates that following high salary increases the 2008 Scheme benefit structure can become relatively more valuable than the 2014 Scheme benefit, and also how the required underpin addition can change between a member’s underpin date and their underpin crystallisation date.

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