



London Borough of Hammersmith & Fulham

Audit, Pensions and Standards Committee Minutes

Thursday 28 June 2012

PRESENT

Committee members: Councillors Michael Adam (Chairman), Robert Iggulden and Lucy Ivimy

Coopted Member: Eugenie White

P-Solve: Nikhil Aggarwal and John Conroy

Majedie: Simon Hazlitt and Rob Hawkins

Deloitte and Touche Tax Advisory: Tim Waterhouse and Ian Stone

Officers: Jane West, Executive Director for Finance and Corporate Governance; Mel Barrett, Executive Director for Housing and Regeneration; Hitesh Jolapara, Bi-Borough Director for Finance; Debbie Morris, Bi-Borough Director for HR; Stephen KIRRAGE, Director for Property and Regeneration; Mike England, Director of Housing Options; Jonathan Hunt, Tri-Borough Director of Treasury and Pensions; George Lepine, Head of HR, HRD; Geoff Drake, Chief Internal Auditor; Michael Sloniowski, Principal Consultant, Risk Management; Piero Ionta, Principal Litigation Lawyer; and Owen Rees, Assistant Committee Coordinator.

1. MINUTES OF THE PREVIOUS MEETING

Councillor Iggulden raised the issue of employer contributions, and asked whether the agreement between the Local Government Association and trade unions would result in a reduction. Jonathan Hunt, Tri-Borough Director of Treasury and Pensions, said that the proposals as they stood would result in a small reduction, estimated at 2%, and included provision for cap and collar/cap and share for employer contributions. However, he said that the primary driver for pension fund deficits was low interest rates, and the consequent high prices of gilts, and that employer contributions would likely remain high until interest rates rose.

The Chairman asked officers to contact Goldman Sachs to ask how the mandate had performed in the light of the poor investment conditions of the current period, and their positive position as stated in their presentation to the previous meeting.

Nikhil Agarwal, P-Solve, gave the Committee figures for the fees due following the introduction of the revised Legal and General mandate; he said that these were appropriate to the work entailed in the new mandate. Councillor Ivimy asked to see details of the fees due to each fund manager: officers agreed to present this to the next meeting of the Committee.

RESOLVED THAT

- (i) The minutes of the meeting of the Audit and Pensions Committee held on 15 March 2012 be agreed as a true and correct record, and;
- (ii) That officers be requested to write to Goldman Sachs regarding their performance in quarter 2, and;
- (iii) That a full summary of fees be reported the next meeting of the Committee.

2. APOLOGIES FOR ABSENCE

Apologies were received from Councillors Cartwright, Ginn, and Murphy, and from the trade unions representative, Sheela Selvajothy.

3. DECLARATIONS OF INTEREST

There were none.

4. MEMBERSHIP AND TERMS OF REFERENCE

RESOLVED THAT

- (i) The terms of reference be noted, and that;
- (ii) The appointment of a Vice-Chairman be deferred until the next meeting.

5. APPOINTMENT OF CO-OPTED MEMBER

RESOLVED THAT

Eugenie White be reappointed as a non-voting, independent cooptee.

6. MAJEDIE MANDATE

Simon Hazlitt, relationship manager, and Rob Harris, fund manager, attended the Committee to explain Majedie's request to vary the terms of the Council's mandate to allow it to invest 20% of funds in overseas equities.

Simon Hazlitt set out Majedie's performance from the inception of the mandate, noting that it had closed its funds a year after receiving the H & F contract, giving Majedie greater freedom of manoeuvre and ensuring a closer focus on existing clients. He then explained the recent performance of the funds, and explained the

factors that Majedie believed would influence future equity performance, and would influence their decision making process.

He said that, while Majedie remained positive regarding London-listed equities as a whole, it was felt that certain sectors were underrepresented in it, meaning that stock related risk was higher, with holdings necessarily concentrated in a few stocks. He gave, as examples, the pharmaceutical sector, given the small number of large cap pharmaceutical companies listed in London, and the technology sector, which was poorly represented on the London exchanges.

He concluded by saying that the change was not structural but would enable Majedie to have additional options as it sought to exceed the benchmark.

The Chairman noted that Majedie had not coupled London-listed stocks with the UK economy, or sought to purchase overseas stocks in pursuit of overseas earnings. Mr Hazlitt confirmed that this was Majedie's view, and that London was a thoroughly internationalised market with good exposure to overseas earning. He said that Majedie also believed that London-listed equities were well-priced, and the smaller exchange made investment more practical. However, it was felt necessary to have some flexibility for the reasons described given earlier.

Councillor Ivimy asked what funds the Council had invested with Majedie, and where these were held. Mr Hazlitt said that the Council had £136.8 million invested, £90 million in Majedie's UK Equities fund, £35 million in the UK Focus fund, and £10 million in Tortoise, a long/short absolute return fund, focused on delivering steady returns. In response to a further question from Councillor Ivimy, he set out the fee structure applying to each element of the Council's holdings, and how these were affected by performance. He said that there would be no increase in fees as a result of the change, but there would be an increase in custodial costs, offset by what Majedie believed to be the greater advantages of the new arrangements.

With regards to the Tortoise fund, Mr Hazlitt confirmed that it was able to invest overseas, for up to 45% of its holdings. It was also allowed to undertake short selling, doing this through the purchase of contracts for difference, with gross exposure greater than the value of the investment. However, the fund did not use financial gearing, and was designed to ensure steady returns, with a focus on performing well in adverse market conditions.

Eugenie White said that the Committee had been misadvised with regards to its investment in the Tortoise Fund, which she believed had been to increase exposure to emerging markets, rather than to allow short-selling. Officers agreed to check the background of the decision.

Eugenie White said that the UK/London market was currently unfashionable and potentially undervalued, with companies trading there benefiting from a weak currency. She asked if it was correct to purchase overseas stocks at a time of currency weakness, currency risk being one of the reasons why pension funds were generally invested locally.

Rob Harris said that the correlation between equity market returns and GDP growth were historically weaker than generally supposed, and that Majedie only wished to make investments overseas where it was felt it would genuinely add value. He confirmed that the UK market remained attractive and the fund's main focus.

Councillor Iggulden asked whether Majedie could expect to outperform American fund managers in selecting technology stocks, for example. Mr Hazlitt said that the Tortoise fund had performed very strongly when investing overseas, and that that technological basis of stock selection at Majedie now made it able to invest overseas.

In response to a question from Councillor Iggulden, Mr Hazlitt clarified that the changes would apply to the UK Equities and UK Focus products, but the Council could chose to opt out of the change for its UK Equities holding.

The Chairman thanked Majedie for attending. The Committee agreed that the proposal should be agreed, but wanted to look at its allocations more widely, in advance of the next actuarial valuation in 2013.

RESOLVED THAT

- (i) That the request from Majedie to revise the mandate to allow 20% of funds to be invested in overseas equities be agreed, and;
- (ii) That officers investigate the advice given regarding Tortoise, short-selling and emerging market equities and report back to the Committee, and;
- (iii) That officers bring forth a report to a future meeting on the allocation of the fund's assets.

7. PENSION VALUE AND INVESTMENT PERFORMANCE

ikhil Agarwal, P-Solve, introduced the report, which set out the fund's performance in the quarter to 31st March 2012. He said that it had been a good quarter, with riskier assets performing reasonably well. He said that confidence had declined starkly in the following quarter, with risk assets performing more poorly. The Chairman asked whether, given that the Dynamic Asset Allocation Mandates had failed to capitalise on improved markets, they could expect to outperform a negative market as previously. Mr Agarwal said that the equities mandates were performing in line with the market, but the Dynamic Asset Allocation mandates were designed to perform in such circumstances.

Eugenie White requested that the report show LIBOR, Councillor Ivimy requested that report show whether returns were net of fees, Councillor Iggulden noted that the period to judge Goldman Sachs' performance should be shorter than their suggested 5 years, and the Chairman requested that officers invite the private equity fund managers to attend a future meeting of the Committee.

RESOLVED THAT

- (i) The report be noted, and;
- (ii) That future performance reports include the LIBOR rate and state the position of the figures in relation to fees, and
- (iii) That the private equity fund managers be invited to a future meeting of the Committee.

8. STATEMENT OF INVESTMENT PRINCIPLES

Jonathan Hunt, Tri-Borough Director of Treasury and Pensions, introduced the report, which set out the updated Statement of Investment Principles.

RESOLVED THAT

The Statement of Investment Principles be agreed, subject to references to the Audit and Pensions Committee being amended to read Audit, Standards and Pensions Committee.

9. ANNUAL REVIEW OF RETIREMENTS AND REDUNDANCIES 2011-12

Debbie Morris, Bi-Borough Director for HR, introduced the report, which set out the retirements and redundancies affecting the fund in 2011-12. She said that while these did not give rise to an increase in employer contributions for the local authority, they would require an interested contribution from three admitted bodies.

RESOLVED THAT

The report be noted

10. EXTERNAL AUDIT PROGRESS REPORT

Jon Hayes, District Auditor, introduced the report, which set out the external auditor's current work and general issues. He said that work had begun on the Pension Fund and Wormwood Scrubs Charitable Trust, and that the General Fund accounts were due shortly.

In response to a question regarding Housing Benefit, Mr Hayes clarified that the issue related to the time taken to process changes in claims. He said that the additional days required made claim files more complex, increasing the difficulty of the audit and increasing the risk of a claim being mishandled.

RESOLVED THAT

The report be noted.

11. HEAD OF INTERNAL AUDIT ANNUAL REPORT

Geoff Drake, Chief Internal Auditor, introduced the report, which set out his annual report to the Committee. He said that significant control weaknesses were identified in 2.2, and that these would be fed into the Annual Governance Statement. With regards to the item relating to reconciliation, Hitesh Jolapara, Bi-

Borough Director for Finance, said that this would not be in the AGS Action Plan, as it had been agreed as unnecessary following discussions between Internal Audit and himself.

With regards to the issue regarding home repairs and adaptations, Mr Drake said that the issue related to the calculation and apportionment of charges. With regards to the programme of tests mentioned at 1.7.5, Mr Hayes clarified that these were carried out by the Internal Audit service to check whether external audit testing was necessary.

RESOLVED THAT

The report be noted.

12. COMBINED RISK MANAGEMENT HIGHLIGHT REPORT

Michael Sloniowski, Principal Consultant- Risk Management, introduced the report, which set out risk management activity undertaken in the previous period. He described ongoing work with the Housing and Regeneration department, and the increased focus on Tri and Bi-Borough integration. He also described work undertaken with Business Continuity and Emergency Planning in the light of discussions at the previous meeting of the Committee.

Councillor Ivimy asked whether the legal and contractual risks that the Council faced, such as judicial reviews, were included in the risk register.

RESOLVED THAT

The report be noted.

13. CORPORATE ANTI-FRAUD SERVICE ANNUAL REPORT

Geoff Drake, Chief Internal Auditor, introduced the report, which was the annual report of CAFS for the 2011-12 financial year. He said that the service had seen a reduction in staff numbers at the start of the year. The service had made 24 prosecutions, with 209 successful outcomes overall, with £8.5 million in fraud detected. He said that £700,000 had been recovered in the year, of which £280,000 had been recovered by CAFS. He said that work was underway to establish a single Tri-Borough fraud investigation service.

The Chairman asked whether CAFS was able to monitor what percentage of funds recoverable were subsequently recovered. Mr Drake said that the system used by debtors did not automatically tie the funds recoverable to the CAFS investigation, and would require some interrogation. Jane West, Executive Director for Finance and Corporate Governance, said that officers would look at what information could be made available.

Eugenie White noted that the performance of the service had been good, but asked whether a reduction in capacity meant that cases worthy of investigation were not proceeded with, with a possible reduction in the deterrent effect. Mr Drake said that CAFS investigated those cases in which the evidence was

strongest and the possible offence committed most serious, and that the service manager was given a target based on the quality of outcomes. He said that there would always be cases that were not investigated.

RESOLVED THAT

The report be noted.

14. INTERNAL AUDIT QUARTERLY REPORT

Geoff Drake, Chief Internal Auditor, introduced the report, which set out internal audit activity in the period to 31 March 2012. He said that there had been 19 reports and 3 management letters issued from which 3 limited assurance reports had been issued in the period, which had been distributed to members with the agenda, all recommendations for these reports past their due date for implementation had been implemented. He was also able to report that there no outstanding reports or recommendations to report to Committee. It was reported that the updated Internal Audit plans for the 2012/13 year were provided at Appendix B following agreement of the tri- and bi- borough elements of the plan with K&C and Westminster. A tri-borough project has now commenced to establish single tri-borough services for internal audit, risk management, and fraud. Progress on these will be reported to future Committee meetings

RESOLVED THAT

The report be noted.

15. EXCLUSION OF THE PUBLIC AND PRESS

RESOLVED THAT

Under Section 100A (4) of the Local Government Act 1972, the public and press be excluded from the meeting during the consideration of the following items of business, on the grounds that they contain the likely disclosure of exempt information, as defined in paragraphs 1,2,3 and 7 of Schedule 12A of the said Act, and that the public interest in maintaining the exemption currently outweighs the public interest in disclosing the information.

16. UPDATE ON TAX ISSUES - VERBAL UPDATE FROM DELOITTE TAX ADVISORY

RESOLVED THAT

The update be noted.

17. GAS SAFETY CERTIFICATION

RESOLVED THAT

The report be noted.

18. ANNUAL REVIEW OF RETIREMENTS 2011/2012- EXEMPT ASPECTS

RESOLVED THAT

The report be noted.

Meeting started: 7.00 pm
Meeting ended: 10.13 pm

Chairman

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