Appendix 1

AVON PENSION FUND COMMITTEE
ANNUAL REPORT TO COUNCIL
(April 2020 - March 2021)

1 INTRODUCTION

This is the annual report to Council detailing the work carried out by the Avon Pension Fund Committee for the period from 1 April 2020 to 31 March 2021.

The Council has delegated responsibility for the Fund to the Avon Pension Fund Committee (the "Committee") which is the formal decision-making body for the Fund. The Committee's role is strategic in nature, setting policy framework and monitoring implementation and compliance within that framework.

Due to the wide scope of the Committee's remit it is supported by the Investment Panel (the "Panel") which considers the investment strategy and investment performance in greater depth. The Committee has delegated authority to the Panel for specific investment decisions.

The Pensions Committee and administering authority are scrutinised by the Local Pension Board ensuring that the governance surrounding the scheme remains robust and fit for purpose.

The scheme is regulated and overseen by the Pensions Regulator. Other bodies and agencies undertake key roles, particularly the LGPS Scheme Advisory Board, the Department for Levelling Up, Housing and Communities, and CIPFA, which sets the accounting standards.

Brunel Pension Partnership Ltd (Brunel), the company established by the Brunel pool to implement the Fund's investment strategy is regulated by the Financial Conduct Authority.

The Avon Pension Fund is a statutory scheme regulated by the Local Government Pension Scheme Regulations 2013 (as amended) and the Local Government Pension Scheme Regulations (Management and Investment of Funds) Regulations 2016 (as amended).

Bath & North East Somerset Council ("the Council") administers the Fund on behalf of approximately:

- 464 employing bodies
- 125,000 members

The value of the Fund as at 31 March 2021 was £5.3 billion.

In 2020/21 the Fund:

- received £211m in pension contributions
- paid out £183m in pension payments and benefits

Full details can be found in the Fund's annual report (https://www.avonpensionfund.org.uk/finance-and-investments)

2 COMMITTEE MEMBERSHIP

The Committee structure is as follows:

Voting members (14)	5 elected members from B&NES (subject to the rules of political proportionality of the Council) 3 independent members 1 elected member nominated from each of the other 3 West of England unitary councils 1 nominated from the Higher and Further Education bodies 1 nominated from Academy bodies 1 nominated by the Trade Unions
Non-voting members (3)	1 nominated from the Parish Councils 2 nominated from different Trade Unions

The Committee meets quarterly. Attendance at the meetings was 96% for the voting members and 50% for the non-voting members.

Due to the Covid 19 pandemic all meetings over the last year, of both the Committee & Panel, took place remotely. This was in accordance with regulations made under section 78 of the Coronavirus Act 2020 allowing local authorities in England to have express powers to hold public meetings virtually by using video or telephone conferencing technology.

Investment Panel

The Panel consists of up to six voting members from the Committee and meets at least quarterly ahead of Committee meetings.

The Panel met formally four times during the year, with attendance of 100%.

3 TRAINING

The Fund provides training to committee members to ensure they possess an appropriate level of knowledge, skill and understanding to discharge their fiduciary duties.

The Fund has in place a training framework which is based on CIPFA's (Chartered Institute of Public Finance and Accounting) Knowledge and Skills Framework for LGPS funds. All Committee members are also encouraged to undertake the Pension Regulator's online learning toolkit.

Committee training is delivered in a variety of formats such as detailed Committee and Panel reports and workshops where the topic is explored in greater detail.

Along with the Local Pension Board the Committee took part in the LGPS National Knowledge Assessment carried out by Hymans Robertson in May 2020.

A number of workshops have been planned over the next year based on the recommendations of the assessment.

Over the last year all training has been held remotely, with members attending several seminars and conferences such as LGE's Trustee Fundamentals and Governance & Investment Update plus Brunel Investor Days. These events help to broaden their understanding of investments and topics of relevance to the LGPS.

4 COMMITTEE ACTIVITIES & REVIEW OF THE YEAR

2020/21 was dominated by the impact of the pandemic on the pension fund's operations, service delivery and investment portfolio. During the year the Committee's focus was on how the service was being delivered remotely, whether service standards could be maintained given the circumstances and how resources were prioritised.

Remote working arrangements were successfully implemented, and all staff were still working remotely at the end of the year. Although the operations and administration are highly digitalised, remote working has been challenging and workloads unrelenting. This meant that specific aspects of the process have been prioritised to ensure member service has not been compromised.

To ensure member benefits could be processed whilst working remotely, new processes were implemented, such as a secure member portal for the transfer of documents and electronic verification of member details. These were implemented very quickly, early in the year, to reduce the need for paper documentation.

Our scheme employers have been working under similar conditions and our partnership approach has helped maintain a high level of service to employers.

a) Investment Strategy Review

Following the Investment Strategy review in 2019/20, the increase in the allocations to Private Debt, Renewable Infrastructure and Secured Income were implemented, as was the allocation to sustainable global equities. We now have £1.2 billion (or 23%) of our assets invested in Sustainable and Low Carbon Equities which will help mitigate the financial impact of climate change on the asset portfolio. In addition, £148 million of capital has been invested in renewable energy and infrastructure assets. Lastly, but very importantly, a significant year-on-year improvement in the Weighted Average Carbon Intensity (WACI) of our listed equity portfolio saw us achieve one of our interim climate change objectives two years ahead of target. Our equity portfolio is now 30% less carbon intensive than the wider market.

b) Investment performance

During the year the value of the Fund's assets increased by £834 million to £5,301 million at 31 March 2021. Following a negative return in the previous year and a volatile start to 2020/21, it was positive to achieve 17.3% return in this year. As a result, the return over the last three years has been 4.9% per annum which is in line with the funding plan.

The year started with highly volatile markets but they recovered from the 1Q20 lows as governments unveiled unprecedented support packages to offset the economic contraction. However, the longer-term impact is still uncertain. The unprecedented stimulus and economic rebound have increased inflationary pressures and the risk of higher interest rates is now affecting markets, with bond yields rising from the yields at the beginning of the year. Whether the pandemic results in other structural changes such as less offshore supply chains, the durability of greater online shopping trends or less demand for office space is not yet clear. Such changes in consumer and industry behaviour following the pandemic will determine how attractive different assets will be in the long-term. Some such as property could face unique challenges if working patterns significantly change as a result of the crisis.

The Fund weathered the crisis well due to the diverse range of assets within the portfolio. As markets fell the equity protection strategy protected the value of the equity portfolio, but the protection was eroded as markets rose through the year. Allocations to diversifying assets such as Diversified Growth Funds and Hedge Funds also provided some downside protection as equity markets fell. Bond markets having initially rallied as riskier assets fell, gave up gains as fears of inflationary pressure increased. Credit markets which were badly affected as investors feared a rise in defaults at the height of the volatile markets, recovered to produce strong returns.

Sterling strengthened against all major currencies over the year in a reversal of currency weakness in previous years, buoyed by a post Brexit rally after the final transition out of the EU and the successful roll out of the vaccine.

Committee and Panel monitored the asset performance and funding implications throughout the volatile market conditions.

c) Pooling of Assets

The transition of assets to Brunel continued during the year despite a short delay due to the high level of volatility in the markets in the second quarter of 2020. We completed two transitions to the Diversified Returns Fund and Global Sustainable Equities portfolios. The final transition will complete in 2021, which means all the transitions have completed in line with the transition plan. In addition, all allocations to Secured Income, Private Debt and Infrastructure assets are being invested via Brunel’s portfolios. As a result Brunel now manage over 70% (or £3.8 billion) of the Fund’s assets. The residual legacy assets will be wound down over time and the proceeds invested in Brunel portfolios where they meet our investment objectives

The Committee receive an update report on Brunel at each committee meeting. Governance arrangements are in place for monitoring service delivery, investment performance and the ongoing costs & savings. The Committee is represented by its Chairperson on the Brunel Oversight Board; the Board is supported by officers from each of the funds.

Eight committee members attended the remote Stakeholder Engagement days arranged for Brunel to update members on the progress made in developing and delivering the investment services Brunel provided to its ten LGPS clients.

d) Climate Emergency

In March 2019 Bath & North East Somerset Council declared a climate emergency and awareness of climate change has continued to be high profile. For pension funds the focus is to manage the financial risk to asset values as the world transitions to a low carbon economy. Significant work is now in progress across the investment industry to develop investment products/solutions that are aligned to the transition and the Paris Agreement. One example is the global project led by the Institutional Investors Group on Climate Change (IIGCC) to develop an investment framework aligned to the Paris Agreement which both Brunel and Avon participated in.

During the year the committee received statements from members and campaigners requesting that the Fund divests from fossil fuel companies. The Committee welcomed the informed questions it received on its climate strategy and responded in kind; providing details of the Fund's carbon exposure, how it monitors engagement activity and how it is adapting its portfolio to ensure it is aligned with the goals of the Paris agreement. As a result, the West of England Unison branches commended the Fund and Brunel on their level of ambition and the actions taken so far to tackle climate change within the pensions & finance sector.

The Fund has set clear climate change investment objectives, targets and milestones that are monitored and kept under review. They have led to the Committee increasing the allocation to sustainable and low carbon equities and to renewable infrastructure assets.

In addition, Brunel's Climate Change Policy published in 2020 is aligned with the Fund's own objectives and will be crucial in enabling the Fund to achieve those objectives over then coming years.

To promote better climate disclosure, the Committee supported the Fund's intention of be an early adopter of the Taskforce for Climate-related Financial Disclosures (TCFD) recommendations for reporting. This is a critical framework to help the Fund deliver its own climate change objectives but is also a way of signalling to investee companies, service providers and partners how important climate risk transparency is to the Avon Pension Fund if it is to achieve reductions in emissions in the real world. The first report covering the 12 months to 31 March 2021 will be presented to Committee later in 2021.

e) Responsible Investing Policy (RI)

Although there is much focus on climate risk, the other aspects of RI, namely Social and Governance risk, are equally important in terms of financial risk to the Fund and the some of the Fund's activity in managing such risks during the year are as follows:

- Prior to the introduction of the FRC UK Stewardship Code 2020 (the "Code"), the Fund was a tier 1 signatory to the UK Stewardship Code 2012, which meant it provided a good quality and transparent description of its approach to stewardship.

The Fund will submit its first Stewardship Report in line with the new Code by the October 2021 deadline for the 12 months to 31 March 2021. This report will focus on activities and outcomes to evidence how the Fund has applied the Code and will be available on the Fund's website www.avonpensionfund.org.uk (search FRC Stewardship Code) following FRC assessment.

- The assets managed by Brunel are governed by its Stewardship and Voting policies, which, with input from the Fund, underwent a comprehensive review during the year to improve transparency and factor in the enhanced requirements of the new Code.
- The Fund continues to participate in industry leading initiatives to promote responsible investment such as the Local Authority Pension Fund Forum (LAPFF), Climate Action 100+ and the IIGCC. In particular, LAPFF seeks to maximise the influence the LGPS funds have as shareholders through co-ordinating shareholder activism amongst the pension funds. This year they were instrumental in lobbying the mining sector for improved disclosures around tailings dams. Officers and Committee members attended four LAPFF business meetings during the year. Alongside 26 international investors, Avon joined a collaborative engagement supported by the Marine Conservation Society to engage with the largest manufacturers of washing machines to promote technological solutions to tackle micro plastic leakage.
- The Fund's ability to engage with, and drive change, at the underlying investment manager level is amplified through Brunel. Over the year, each quarter the Fund engaged with around 300 companies held in its equity portfolios, across a broad range of ESG issues. Environmental topics, on average, featured in 24% of engagements, 78% of which related directly to climate change. Social topics featured in 20% of engagements, where diversity and human rights featured prominently. Of the 37% of Governance related engagements the majority revolved around executive remuneration. Strategy, risk and communications topics such as audit and accounting and cyber security featured in the remaining 19% of engagements over the year.

f) Risk Management Strategy

The Fund uses a number of risk management strategies specifically to provide as stable as possible contribution plans for employers and to protect the Fund from significant falls in asset values.

The two main strategies are (i) the Liability Driven Investment (LDI) framework which seeks to increase the Fund's exposure to inflation-linked assets in order to offset the impact of rising inflation on the Fund's liabilities and (ii) the equity protection strategy which protects against significant market falls.

The Committee has strategic oversight of these strategies whereas the Panel monitors the performance and financial impact more closely and considers issues that could affect them. During the year the Panel considered the impact of rising inflation expectations which led to the decision to increase the inflation hedge to the maximum permitted under the strategy. In addition, the Panel worked closely with advisors to implement a more dynamic structure for the equity protection strategy that would more efficiently provide protection and simplify the governance burden.

g) Funding Strategy

The last actuarial valuation was in 2019 which projected a deficit of £284m and a funding level of 96%. In 31 March 2020 the funding position deteriorated to 84% due to the fall in asset prices at the end of the year. However, due to the recovery in asset prices, by 31 March 2021 the funding level had improved to 97%.

Ahead of the next valuation in 2022, an interim valuation exercise will be undertaken in 2021/22 to identify pressures on the funding position. Given the impact of the pandemic on the scheme employers, affordability of pension costs will be a key consideration in managing financial risk for both employers and the Fund. A workshop is planned for the Winter to go through the results with the Committee.

During the year the Committee agreed new policies in line with regulatory changes to permit more flexibility when agreeing funding plans for employers that exit the scheme or for those that are approaching exit. The Funding strategy Statement was updated to reflect these new policies.

h) Pensions Administration

(i) Chartered Institute of Public Finance & Accountancy (CIPFA) Benchmarking (Benefits Administration)

The fund is committed to achieving and enhancing value for money and to make the administration of the scheme as efficient and cost effective as possible.

LGPS Costs

Costs per staff FTE	**2019/20**
Net admin cost per staff FTE £'000	55.7
National Average £'000	69.4
Members per FTE	2,306
National Average	2,781

Costs per member	**2019/20**
Investment Management Expenses	
Total Cost £'000	26,943
Cost per member	221.66
National Average £	232.11
Administration Costs	
Total Cost £'000	2,408
Cost per member	19.81
National Average £	20.16
Oversight & governance costs	
Total cost £'000	1,752
Cost per member	14.41
National Average £	15.55
Total Costs £'000	**31,103**
Total cost per member £	**255.88**
Total National Average £	**267.82**

The CIPFA benchmarking data from 2019/20 (table above, the latest available) highlights the Fund’s comparative performance in key cost areas, as shown below. They demonstrate the Fund’s positive cost performance when compared with national averages.

(iii) Pensions Administration Strategy

The Administration Strategy sets out how the administering authority and scheme employers will work together to provide an improving quality level of service to Fund members.

The strategy ensures the Fund can continue to deliver a high quality service at a time when the operating environment is becoming more complex. The employer base has fragmented, especially with the creation of academies and the increase in the number of third party HR and payroll providers.

The strategy was last updated and approved by Committee in March 2019. The main objectives are:

- Full electronic receipt of data from all employers
- Digital delivery of all communications to members
- Introduction of chargeable services for employers

The strategy to deliver digital communications to members together with the electronic receipt of data across the employer portfolio aligns with Council strategy to reduce carbon emissions.

Over the course of the next year the administration strategy will be reviewed again with the focus on the digital transformation project. Whilst the need to adapt to a more flexible and remote working environment is paramount, recruitment, staff training and wellbeing is also a top priority. The Committee expect to see more detail about the new strategy by the end of the year.

(iv) The Pension Regulator

Since the introduction of the Pension Regulator’s (TPR) Code of Practice 2014 and Record Keeping Regulations, the Fund has a data improvement plan in place to improve both the quality of the Fund’s data as a whole and, also working with individual employers to improve their data. A data score of 95% for Common Data & 85% for Scheme Specific Data was reported in the TPR Scheme Return as at September 2020.

(v) Risk Register

The Fund’s Risk Register identifies the governance, operational, funding and investment risks that the Fund is exposed to and, having evaluated the financial and operational impact of the risk on the Fund’s objectives, states the actions taken to mitigate and effectively manage the risk.

The register is reviewed regularly by the management team and is reported quarterly to the Committee.

i) Approval of the 3 year Service Plan & Budget

Each year the Committee approves the Service Plan which sets out the Pension Fund's objectives for the next three years together with a three year budget to deliver the plan including work relating to the investment strategy, risk management, compliance and improvements in the administration of the Fund.

The budget approved for Administration in 2020/21 was £2,935m. The budget for 2021/22 has been increased to £3,170m. The increase includes additional resource to strengthen the management team and to also implement and manage the transformation program. It also includes continued additional temporary resources to meet expected increased workload resulting from the McCloud remedy.

Budget Outturn (2020/21)

During the year administration costs (excluding advisory and investment management costs) were £2.4 million, 17% below the budget of £2.9 million. The main savings were on salaries as recruitment was delayed due to the pandemic and remote working. There were also other pandemic related savings such as reduced travel, training and conference attendance.

Annual investment management fees paid in the year were below budget at £18 million.

The budget for governance costs was £1.7 million with actual costs just over budget at £1.8 million. More advice than anticipated was required to address pandemic related issues for both investment and actuarial strategies.

j) Treasury Management Policy and Cash Management Policy

The Committee approves the Fund's Treasury Management Policy annually. The policy sets out how the Fund's cash is invested to meet its day-to-day requirements. The cash managed under this policy is 0.5-1% of the Fund's value (up to c. £45m).

The management of this cash is delegated to the Council's Treasury Management Team but it is invested separately from the Council's and the Fund has a bespoke Treasury Management Policy.

k) Work plans

Separate workplans are prepared for the Committee and Panel detailing the forthcoming areas of work relating to the investment strategy, funding strategy and the administration of benefits to give the Committee and officers the opportunity to review the workload, plan Committee agendas and workshops and accommodate issues that may arise.

5 FUTURE ACTIVITY

Our forward looking 3 year Service Plan sets out the Pension Fund's objectives and priorities with a budget that supports the objectives and actions arising from the plan. The focus is the digital transformation project, addressing the climate emergency and managing employer risk.

The Committee and Panel's focus over the next twelve months will be:

Funding Strategy:

1. Undertake an interim valuation during 2021 to identify the issues that may materially affect the 2022 valuation (which sets employer contribution rates with effect from April 2023).
2. Ongoing covenant assessment for incorporating into the Funding Strategy and funding plans.
3. Ongoing management of smaller employers to ensure pension costs remain affordable for the employer and financially sustainable for the Fund.

Investment Strategy:

4. Monitor the performance of Brunel and their portfolios, ensuring Brunel are delivering the Fund's strategic objectives.
5. To meet our climate objectives, review the equity portfolio with the objective of having all the equity assets managed in sustainable or Paris aligned (with low carbon transition) investment strategies.
6. In light of the interim valuation and expectations of future returns, consider whether the current investment strategy meets the funding objectives or whether the level of risk embedded in the strategy is too low.
7. Monitor and develop the Risk Management Framework as required as a mechanism for managing liability risk through the investment portfolio and mitigating investment risk.
8. Support initiatives and undertake activity to demonstrate the Fund's commitment to meeting its climate emergency targets such as reporting in line with the TCFD recommendations in 2021, as a signatory to IIGCC initiatives to influence government policy and regulatory change.
9. Increase communications with our broad array of stakeholders about the investment strategy with a focus on how the strategy is mitigating the financial risk of climate change.
10. Realign the investment advice required post transition of assets to Brunel.
11. Maintain the Investment Strategy Statement reflecting strategy developments and changes due to Brunel operations.

Administration Strategy:

12. To continue the move towards digital delivery of Scheme communications to members.
13. To complete the rollout of I-Connect and the receipt of monthly member data returns.

14. To introduce a training & development programme covering operational and digital transformation requirement.
15. To complete the final phase of the GMP data reconciliation exercise as required by HMRC to ensure the fund is not at risk of erroneous pension liability.
16. To complete the member address rectification project to identify missing data and implement actions to resolve outcomes.
17. To monitor outcomes of McCloud judgement and implement actions to manage remedy including actions to support Fire Schemes Immediate Detriment cases.
18. Undertake gap analysis and specification for digital requirements across all stakeholders.
19. Develop revised Admin Strategy proposals to include digital transformation and to take to Pensions Committee.

Governance:

20. Keep governance arrangements under review to ensure effective monitoring of Brunel and the transition of the assets.
21. Implementation of the Good Governance Review (SAB) requirements.
22. To ensure the Committee and the Pensions Board is fully trained and briefed on current strategies and operations and in position to scrutinise and make decisions effectively.
23. Retender advisory contracts to align contracts with Fund objectives.

September 2021