Annual Members Meeting (AMM): Tuesday 12 October 2010

Q1 Following the latest valuation employers are now paying around £240 million per year in contributions with additional lump sum payments due in 2017-2020. If the deficit widens further can they pay more?

A1 The finalisation of the latest actuarial valuation has resulted in agreed recovery plans covering the next 10 years. However the next actuarial valuation will be carried out as at 31 March 2012. This means the position will be looked at again then and a new recovery plan and schedule of contributions can be agreed between the Trustee and employers. This could involve higher contributions, but the negotiations over the recovery plan are intended to address issues such as affordability.

Q2 I understand that pension increases are made based on the September to September Retail Prices Index (RPI). This was announced today as being 4.6%. Is this the increase which will apply?

A2 Yes the 4.6% RPI increase will be used to calculate the TfL Pension Fund pension increases which apply from 1 April 2011.

Q3 The investment update focused on returns across asset classes and managers. What about the risk profile and what level of risk is safe ?

A3 There are overlay risk controls which operate within the Fund's investment portfolios designed to keep the overall risk within certain parameters. For example if we are seeking a 10% return target for a particular asset class, then we set risk control parameters to ensure a level of certainty that actual performance will be within (say) plus or minus 3% of this 10% target. Further risk control is provided by the asset allocation within the Fund, for example by diversifying between equities and bonds. More recently, the introduction of "alternative" investments such as infrastructure and private equity has enabled the Fund to trim the risk further. In addition, some of the investments that the Fund holds ("liability driven investments") result in material risk reductions by explicitly matching the a portion of the assets to move in line with the value of a portion of the liabilities.

Q4 What action are the Trustees taking with respect to its members who lost money through investments with Equitable Life?

A4 Individual members do not have a policy with Equitable Life, the policy is held in the name of the Fund. However the arrangement is between the member and provider in the choice of investment made. The Trustees monitor the performance of the investment funds used for Additional Voluntary Contributions (AVCs) and make changes when appropriate. AVCs are held separately from Fund assets.

The Trustees have made representations to the Treasury and Prime Minister recently on Equitable Life. These were in respect of the compensation scheme which is currently being determined and was seeking to ensure that Government takes account that a “per policy” basis would disadvantage members in a group policy such as ours. The bill to enact compensation has now received its second reading and the Trustees will await the final results and details of the process for claiming compensation expected early next year and will keep members informed.

Q5 Are Trades Unions still represented on the Trustee Board ?

A5 Yes, there are 4 members of the Trustee Board nominated by Trades Unions.

Q6 The presentation mentioned a number of government announcements which will apply to other pension schemes but not TfL Pension Fund. These do raise concerns that they will apply at some point.

A6 We believe it is appropriate to share with you what is happening generally in pensions. It does not signal that there is anything about to change with respect to TfL’s pension arrangements. But there has been a lot of activity in pensions in recent years and some of what we have seen taking place in the private sector is now flowing through to the public sector.

Q7 I have heard rumours that the Spending Review to be announced on 20 October will involve the tax free lump sum being taxed with immediate effect.

A7 We have not heard any such rumours and are not expecting any such change. If it were to be introduced at any point, then it would be more likely to be done gradually. [Note: The subsequent Spending Review announcement did not mention any change being made to the tax free lump sum].

Q8 What are the key criteria for changing investment managers?

A8 A key driver is the asset classes in which the Fund wishes to invest, i.e. we have to look for the right manager for the type of investments we want managed. This will in part be driven by the results of the actuarial valuation, in particular the split between equities and bonds. The next decision is the proportion of these assets to manage passively (less cost but only achieving market or “benchmark” performance) or actively (more expensive but with the prospect of better than benchmark returns). In selecting the particular manager, both quantitative and qualitative analyses are considered, such as reports on the quality of investment process, past performance data and commentary on key people within the manager’s organisation. In terms of the selection process, the Fund’s investment consultants will put forward a short list of candidates for an identified role and the Investment Committee will select the most appropriate structure following detailed due diligence an interviews.

Q9 From the presentation you mentioned that managers had successfully achieved benchmark. Are we are not seeking something better than that ?

A9 Yes, the active managers are set targets when they are appointed to achieve performance above the benchmark and are measured in respect of how well they perform against these targets.

Q10 I note investment management expenses have increased by £1 million. Could you comment ?

A10 The investment management fees are in part determined by the value of holdings under management and as the Fund value has risen compared with last year, so have investment management fees. There has also been some switching during the year from passive to active management which has resulted in higher fees being paid. Overall the increase in fees needs to be considered not in absolute terms, but in relation to performance.

Q11 Could you comment on the legality of the scheme introduced by the last government for helping pension schemes that have fallen by the wayside?

A11 The Pension Protection Fund (PPF) was established by act of parliament to safeguard the pensions of employees whose companies became insolvent. As such we consider that it was a positive step. However we do have reservations regarding how the PPF levy has been applied in the case of TfL Pension Fund and continue to have contact with the PPF on this issue.

Q12 Last year inflation was negative and no pension increase was given, while later in the year it was positive. Why cannot pension increases be determined later in the year?

A12 The Rules provide that the increase in pensions will follow the September to September increase in the Retail Prices Index. This is also the same reference point used for state benefits and by a majority of other pension schemes. If we moved to a different reference point, then it may produce a higher result in one year, but the year by year ups and downs would still persist following that. For example in the preceding September to September period the RPI increase was 5%, but a different 12 month reference point then would have produced a lower pension increase figure as RPI increases were lower in other months.

Q13 Our alternatives portfolio includes investment in private equity. There has sometimes been controversy about how such firms behave.

A13 Our investment is within a “fund of funds” arrangement managed by Partners Group where they pick private equity managers who in turn select the companies and new ventures that represent the ultimate investments. That means there is an additional layer of due diligence between the Fund and the private equity managers who have to some degree been criticised in the press over the last few years. The Trustees rely on Partners Group in their selection of these underlying funds and their managers and ensuring that their investment partners are acceptable from the perspective of good corporate governance, is a key objective set by the Trustees. For the two major Partners Group funds in which we are invested, The Fund also has representation on their investor advisory groups which provides further opportunity to review the activities of the underlying managers.

Questions received in advance of the AMM

Q14 With the increase in the value of Fund it would be nice if this could be used to give pensioners a £150 Christmas bonus.

A14 While the assets of the Fund have increased, so have its liabilities. The Trustees can only consider making benefit improvements if the Fund was in surplus. As it has a substantial deficit currently there is no scope to consider this sort of payments you have suggested.