SOUTH YORKSHIRE PENSIONS AUTHORITY

Medium Term Financial Strategy

2020/21 to 2022/23

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1. Foreword

1.1 Foreword to the Medium Term Financial Strategy 2020/21 to 2022/23

1.1.1 This Medium Term Financial Strategy (MTFS) has been produced by the South Yorkshire Pensions Authority to cover the period from April 2020 to March 2023. This period will see the implementation of the results from the 2019 Actuarial Valuation as well as the continuing transition of the Authority's remaining investment assets into the pooling structures provided by the Border to Coast Pensions Partnership.

1.1.2 The strategy covers both the costs of running the Authority's operations and the income and expenditure of the pension fund, although this is significantly more difficult to forecast than routine running costs such as staff salaries.

1.1.3 Any financial strategy is based on a series of key assumptions and throughout this document these assumptions are highlighted, and will be subject to ongoing review as the process of producing this strategy develops over time.

1.1.4 The financial strategy (and the budget which is the annual expression of the strategy) is, put simply, the financial expression of the policy position set out in the corporate strategy. Hence this strategy will be updated each year as the Corporate Strategy is updated to reflect changed circumstances.

1.1.5 While SYPA is less exposed to the wider constraints on the public sector financial environment than our colleagues in the major employing organisations within the Pension Fund, we still have a responsibility to manage the resources for which we are responsible in such a way that our expenditure does not negatively impact on the overall performance of the Pension Fund. This strategy sets out how we aim to achieve this in as transparent a way as possible.

2. Setting the context for the medium term financial strategy

1.1 Public Sector Finance

1.1.1 The public sector financial environment is probably the most significant factor defining the context in which this strategy is developed. Key issues, like the level of pay awards, have an impact both on some aspects of the Fund's liabilities as well as upon elements of the Authority's cost base.

1.1.2 The main factors affecting the Authority and the Fund are concerned with local government finance. In general terms, growth in local government spending tends to lag growth in the generality of government spending, although pay tends to mirror the headline change in public sector pay.

1.1.3 The most recent pay agreement ends in March 2020 and negotiations to determine any award for the period from April 2020 are in their very early stages. The consensus view of forecasters and treasurers seems to be that there is unlikely to be any significant widening of the financial envelope for local government in the forthcoming period following the outcome of the General Election in December 2019.

1.1.4 What this means for the Authority and the Fund is that it is likely that headline pay increases in the medium term will be at around, or possibly below, the level of the last agreement at 2%, and that major employers (and probably schools and colleges as well) will continue to need to identify significant year on year savings. This has wider effects on a number of areas, including the affordability of contribution rates, the balance of membership between active, deferred and pensioner members, and the number of early retirements on grounds of redundancy. These factors will influence the value of benefits in payment, the average lifetime in retirement and the value of lump sum "strain" payments into the Fund. All of these factors will need to be reflected in forecasts of income and expenditure and in the debate over contribution rates at each valuation.

1.2 The Pensions Sector

1.2.1 What is happening in the wider pensions sector impacts the Authority and the Fund in a less direct way, although no less significantly. For example a significant change in the funding level of the remaining private sector defined benefit schemes could change the value of certain assets classes used to address the results of the change (e.g. a search for index linked gilts if funding levels increased). This could impact on the potential rate of growth in the value of the Fund or could make it harder to deploy capital into specific types of asset if other funds take up the supply of assets.

1.2.2 In addition, trends in the wider pensions sector tend, over time, to influence developments within LGPS and in the public sector pensions' space. These trends may arise from regulatory emphasis, such as the continuing focus on data quality, or from changes in technology such as the growing emphasis on various forms of e-communication, and methods of engaging with scheme members.

1.3 The Economic Environment

1.3.1 The wider economic environment impacts the Fund in terms of both its assets and its liabilities. Clearly the underlying economic environment impacts the performance of investments in the financial markets while key metrics such as inflation and interest rates feed in to the actuarial calculations which determine the Fund's liabilities.

1.3.2 It remains incredibly difficult to forecast the movements in key economic indicators therefore it makes sense for this strategy to use assumptions based on key factors already reflected in the financial framework such as the assumed level of investment return included in the actuarial valuation. This is not a protection against any forecast being wrong

– it almost certainly will be – but it means that the strategy is based on an underlying set of assumptions that have been subject to a more rigorous set of testing than it would be possible to achieve internally.

1.4 The Starting Point

1.4.1 The starting point has a significant impact on any strategy. In this case, the starting point is reflected in the current cost base for the Authority's operations and its fund management arrangements and the level of funding within the scheme, which based on the 2019 valuation results reflects a significant improvement on the 2016 position.

1.4.2 In some senses the starting point is possibly more influential than other aspects of the context, for example achieving full funding, or close to full funding would lead to an alteration to the strategic asset allocation moving funds out of equities into less volatile, preferably income generating assets. Unfortunately these tend to be more expensive assets to manage thus a change in the cost base is almost inevitable. Whether the focus is on net of fees return or gross fees is irrelevant because both will ultimately have the same impact on the value of and performance of the Fund.

1.4.3 For the South Yorkshire Pension Fund, the starting point is, based on the 2019 valuation results very close to full funding. This impacts employers' deficit recovery contributions. At this stage no change in the strategic asset allocation can be assumed as the investment strategy review is due to be completed in March 2020. At this stage while there are likely to be some changes in asset mix it is not anticipated that these will fundamentally change the balance between different types of asset.

3. Financial objectives

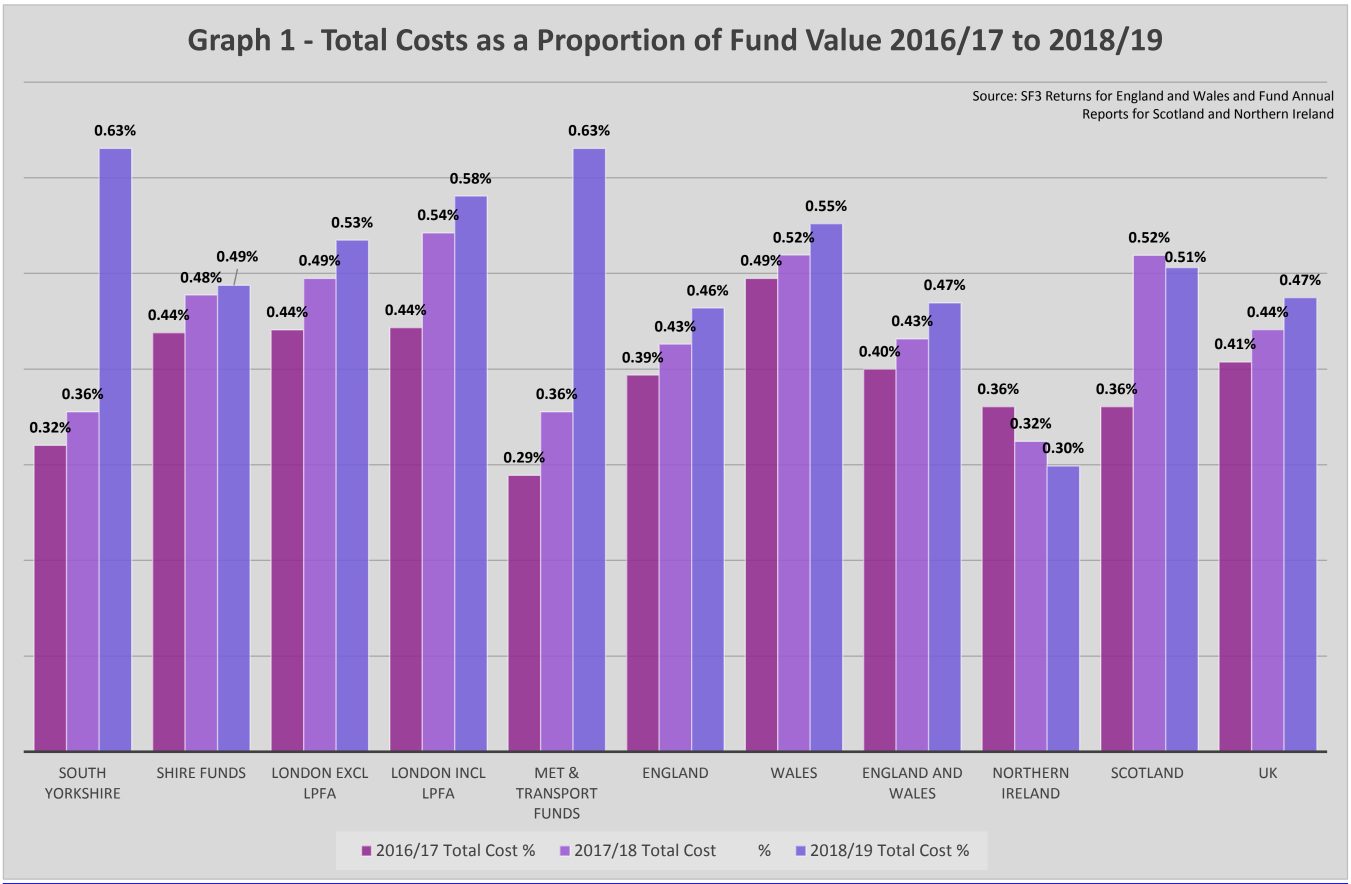
1.5 Financial Objectives

1.5.1 For any strategy it is important to understand what you are aiming to achieve. This is no less true of this MTFS and this section sets out objectives in relation to the control of costs in the overall context of the Fund. In order to set these objectives we need to understand how SYPA's costs compare to the rest of the LGPS funds.

1.6 Comparative Costs

1.6.1 The only real source of data to compare SYPA with other LGPS funds is the annual SF3 return completed by all English and Welsh funds and submitted to MHCLG. Similar data for the Scottish and Northern Irish funds can be added to this from fund annual reports to give a UK wide comparison. There are flaws with this data, particularly with regard to the disclosure of non-invoiced investment costs, which are gradually being worked out of the system. However, it is the only comprehensive data set available and does give a broad indication of how SYPA compares with other LGPS funds.

1.6.2 Graph 1 below shows how SYPA's total costs compare with those of both the totality of other LGPS funds and of particular types of fund for the last three financial years from 2016/17 to 2018/19.



1.6.3 This appears to show that South Yorkshire's costs as a proportion of Fund value increased significantly in 2018/19, resulting in us moving from being one of the lowest cost to being one of the highest cost Funds in this comparison. However, it is important to note that the largest part of the difference in South Yorkshire between 2017/18 and 2018/19 represents an increase in *reported* investment costs, rather than actual costs. Therefore, these statistics must be set in the context of the drive to greater cost transparency and improved reporting of investment management expenses that are not invoiced but deducted at source from Net Asset Value (NAV). In 2018/19 SYPA, with the aid of Border to Coast, made significant progress in this regard, enabling the separate identification and reporting of an additional £19 million of such costs compared to the prior year. It is evident from the national results that our progress has out-paced that of the majority of other Funds. It is anticipated that over the next couple of years, a similar impact will be seen within the other Funds and that will make these comparisons more useful as they will be on a more 'like-for-like' basis.

1.6.4 The 2018/19 total costs for SYPA also include non-recurrent Pooling implementation and transition costs of almost £4 million in total.

1.6.5 The following table presents more detail of the investment costs and this demonstrates the impact of the enhanced reporting of these external management costs that are deducted at source.

Investment Management Expenses - Breakdown	2017/18 £000	2018/19 £000	Year on Year Change £000
Pooling Implementation Costs	406	1,935	1,529
Internal Management Costs	974	672	(302)
External Management Costs - Invoiced	3,764	5,335	1,571
External Management Costs - Deducted at Source	18,741	37,884	19,143
Pooling Transition Costs - Deducted at Source	0	2,370	2,370
VAT Liability	255	516	261
Total Investment Management Expenses	**24,140**	**48,712**	**24,572**
Fund Value at 31 March: £000	8,030,353	8,439,965	409,612
Investment Costs as Percentage of Fund Value	0.30%	0.58%	0.28%
If Pooling Implementation and Transition Costs Are Excluded:			
Total Investment Management Costs: £000	23,734	44,407	20,673
Investment Costs as Percentage of Fund Value	0.30%	0.53%	0.23%

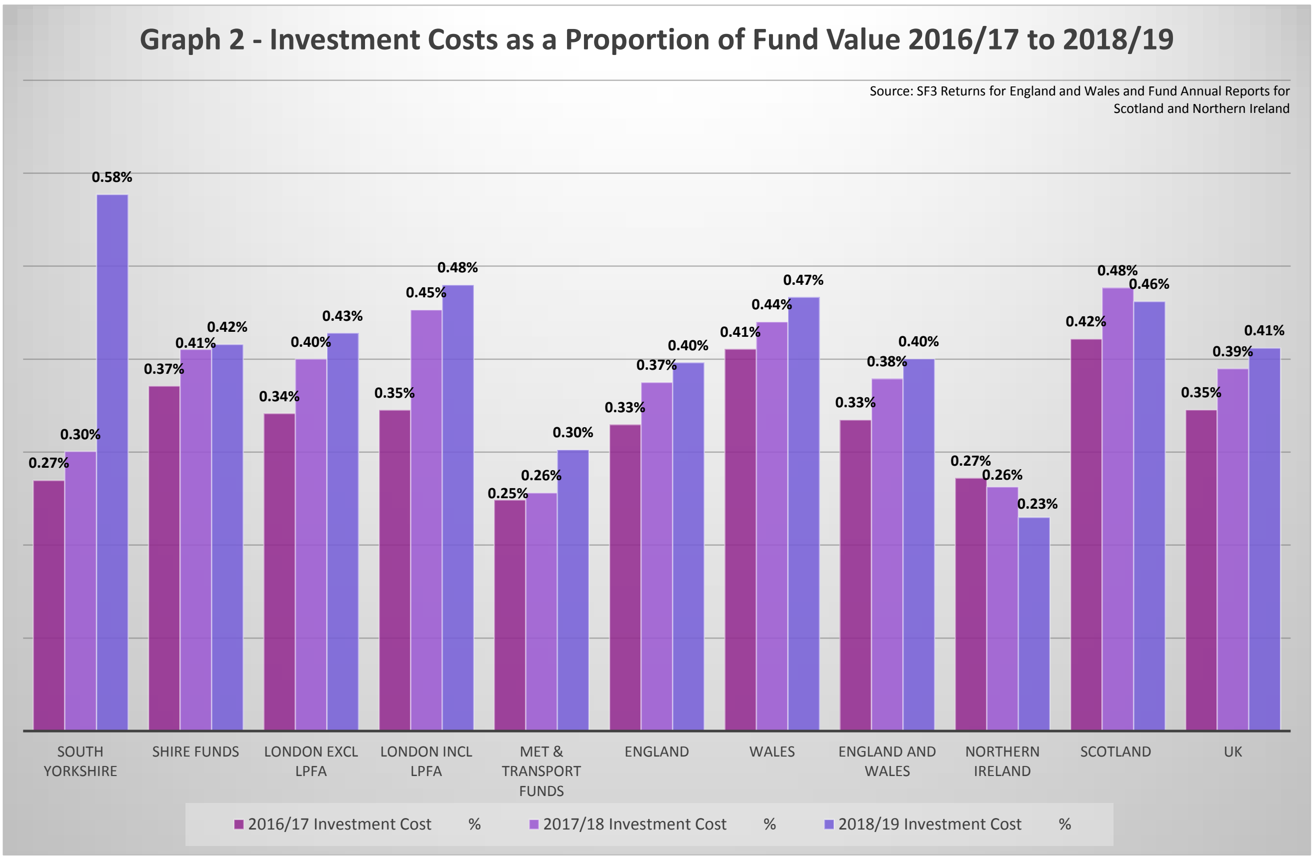
1.6.6 The Authority is confident that our performance in controlling actual costs overall remains strong; but there is no room for complacency and we continue to closely monitor this area in light of the following factors that are driving cost increases:

- The Fund's strategic asset allocation is moving more of the portfolio into unlisted assets such as private equity and infrastructure which in general tend to be more expensive to manage.

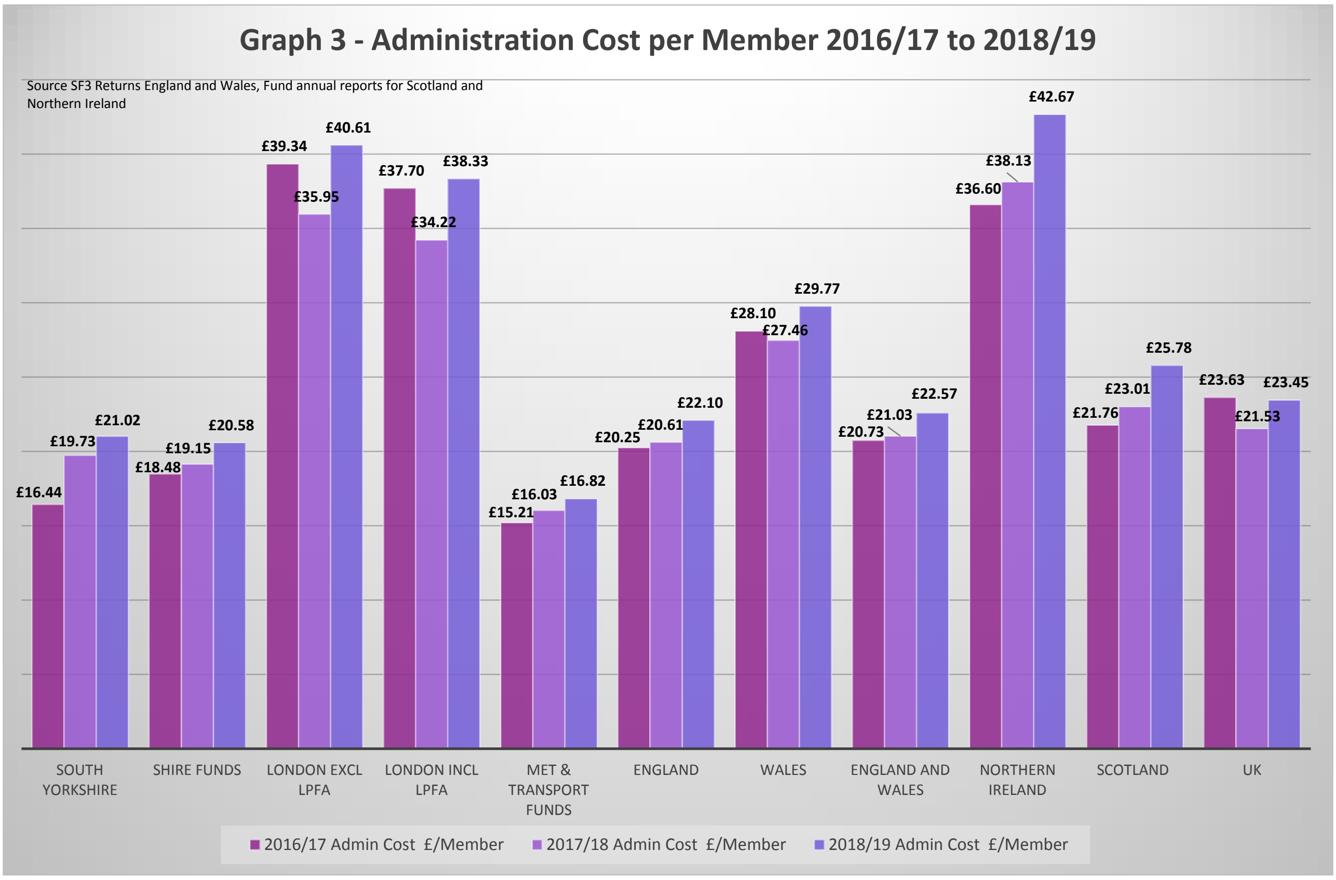
- The Government's pooling initiative results in SYPA's listed assets in future being managed within pooled structures provided by Border to Coast which, while cheap in comparison to external managers, are more expensive than the previous, admittedly unsustainable, in-house arrangements.

1.6.7 There are specific factors which might be expected to give rise to SYPA having a higher than average cost base, in particular the fact that it is a stand-alone pension organisation bearing its own corporate overheads, rather than sharing them with a council. This has not been borne out by the data in recent years but will be kept under review as part of the budget process going forward, particularly as the Authority continues to invest in the development of the organisation and governance.

1.6.8 The total cost shown in Graph 1 can be analysed in more detail by looking at the following two graphs which separate out SYPA's Investment and Administration costs and how these compare with the rest of the Local Government Pension Scheme across the UK.



3.2.9 While these investment costs show a significant increase and a divergence from the previous position this is, as explained above, a result both of improved disclosure and transition and pool set up costs. The level of under reporting across LGPS is made clearer when the CEM benchmarking data is examined which gives a peer group median investment costs of 61.5bps which compares to South Yorkshire's 58bps shown above and the 60.4bps included in the CEM report which reflects a slightly different reporting basis. Given this it is clear that until the issues of under-reporting investment costs are addressed that the use of a pure LGPS comparator based on published accounts is unlikely to add any value.



3.2.10 It is evident from Graph 3 that Administration costs for the Authority, whilst increasing slightly from 2017/18, remain at the lower end of the spectrum of costs.

3.2.11 In regard to Administration, SYPA is benefitting from the economy of scale that comes from serving a large fund, while the much smaller London funds clearly see the diseconomies which arise from servicing much smaller funds. It is evident that all classes of funds have seen an increase in the administration cost per member in 2018/19, including ourselves. Therefore it is important that we continue to monitor the cost base and comparing our costs with other pension funds is a useful tool to inform this. However, it is important to assess this in a holistic way by benchmarking not only the cost but also the quality of service provision. During the current financial year, we have therefore participated for the first time in an additional benchmarking exercise for Pensions Administration provided by CEM, an independent provider with wider involvement in supporting the pensions sector outside of the LGPS. This form of benchmarking differs from the comparisons above, and the CIPFA benchmarking that we continue to use, in that it examines our performance from a scheme member perspective rather than focusing purely on cost.

3.2.12 The Authority will continue to make use of benchmarking in order to inform an on-going assessment of how we are performing in relation to the achievement of value for money. The challenge is how to use this information to set some clear objectives which will assist the Authority in managing its cost base while continuing to facilitate investment in the continued development and improvement of services to scheme members.

3.3 Financial Objectives

3.3.1 The Authority needs to set financial objectives which focus on the key streams of activity within its operations, administration and investment while bringing these together to focus on total cost. These objectives will mirror the financial constraint imposed on the district councils by the grant system, thus ensuring that SYPA is taking no more from the pension fund for its running costs than is absolutely necessary.

3.3.2 At the same time the Authority must be careful, as a small organisation, not to “shoot itself in the foot” by setting unachievable financial objectives which generate relatively large scale savings targets, which could not be delivered without impacting the customer experience.

3.3.3 For Pensions Administration, the financial objective may be framed as follows:

“The annual increase in the budgeted cost per member for administration functions will be limited to an index made up of 70% local government pay and 30% August CPI.”

3.3.4 This limits the rate of increase in costs while allowing the benefits of any increase in productivity to be re-invested in the quality of the service provided to members, which is broadly in line with the Authority’s overall objectives. Such an approach also provides some buoyancy in the level of resources available in order to address the rising number of members and employers within the Fund. A similarly expressed objective could be placed on the Authority’s overall operating budget, which would place a helpful constraint on corporate costs. These two objectives are illustrated in the table below.

Cash Limits for Operational Budget	2020/21 Baseline[1] £ / Member	2021/22 Cash Limit[2] £ / Member	2022/23 Cash Limit[2] £ / Member
Administration Service	£20.57	£21.01	£21.46
Authority Operational Budget	£33.18	£33.88	£34.60

Notes

1. The 2020/21 cost per member is based on the relevant totals included within the Authority's operational budget as presented for approval at the Authority's January 2020 meeting. The equivalent figures for SF3 reporting purposes will be slightly higher because they additionally include non-recoverable VAT which is not part of the Authority's total operating budget.

2. The future years' cash limits are calculated by applying an inflationary increase of 2.12% which comprises 2% Local Government Pay Inflation in line with the assumptions in the budget, and 2.4% CPI Inflation in line with the Actuary's assumptions; both weighted in accordance with the financial objective set out above.

3. Membership is assumed to increase at 2.5% per year in line with recent trends.

3.3.5 Following the transfer of staff in 2018/19 to Border to Coast, the Authority incurs a much smaller investment-related cost within its operating budget. The vast majority of these costs will be incurred within the Fund either within legacy investments or the pooling structures. Given that broadly investment costs have a relationship to the value of invested assets it would be sensible to have an objective which recognised this, but also recognises the fact that the Authority’s investment strategy is to move out of listed into unlisted and more expensive assets and also that the Authority’s overall objective is to achieve the best possible net of fees risk adjusted returns meeting the actuarial return objective (currently c. 4.2%pa). This means that any financial objective around investment costs should not place an artificial constraint which prevents the Authority from making the right investment decisions.

3.3.6 Given the information set out above framing an objective in relation to investment costs is quite difficult. However, something along the following lines could be appropriate:

> *"In any financial year, the Authority will seek to limit investment management expenses to a level less than the median in the CEM benchmarking comparator group."*

3.3.7 Given the limitations to an LGPS comparator set out above this metric provides a more realistic target which is based on a much wider international peer group and reflects full cost transparency for all participants, thus there will be a like for like comparison. Using the CEM measure also means that the Authority will have access to data which will allow it to understand how and why its costs differ from others within the peer group.

3.3.8 The targets set out in these financial objectives will be reviewed each year in the context of their impact on the Authority's overall financial position and their impact on the ability of the Authority to deliver its corporate objectives, while still driving improvements in efficiency. In addition to these objectives which can easily be measured in budget setting and which in effect place cash limits on the Authority's budget, a number of financial performance measures related to comparative costs will be part of the suite of Corporate Strategy measures.

4. Financial forecasts

4.1 Forecast Assumptions

4.1.1 Any financial forecast is based on a series of assumptions. This is the first time that the Authority has produced a longer term financial forecast for its activities, hence the assumptions related to a number of highly volatile items (such as investment returns and transfer values) will need to be refined over time. The key assumptions are set out below:

- **Pay -** Pay awards will average 2% over the period in line with the headline increase in the most recent local government pay award.
- **Prices -** CPI inflation will be 2.4% over the period in line with Actuary's assumptions for the 2019 valuation. This impacts a small portion of the operational budget but is a key driver for the cost of benefits in payment.
- **Contribution Income –** The forecast is based on the preliminary actuarial results of the 2019 Valuation for Future Service Rates and Deficit recovery payments that will apply from April 2020.
- **Volume Driven Benefits and Transfers Costs/Income -** These are based on four year moving averages, adjusted where relevant for known large one off items such as the transfer of the Probation Service's portion of the Fund to the Greater Manchester Fund.
- For the operational budget, the forecast is based on the pay and prices assumptions shown above and has been re-set to take account of wider changes in the organisation.
- Investment returns are assumed to be in line with actuarial assumptions.
- External investment management costs have been separately analysed in order to produce the forecast based on experience to date plus known changes and estimated changes as a result of continued transition to Pooling.

4.1.2 Based on current knowledge, these assumptions are reasonable. We will continue to develop and refine our forecasting techniques over the period to provide a robust basis for resource planning.

4.2 Operational Budget Forecast

4.2.1 The forecast for the operational budget is summarised in the table below:

Operational Budget	2020/21 Budget £	2021/22 Estimate £	2022/23 Estimate £
Employees	3,550,990	3,582,735	3,638,495
Running Costs	1,963,010	1,971,910	1,992,960
Subtotal: Gross Expenditure	**5,514,000**	**5,554,645**	**5,631,455**
Income	(115,000)	(115,000)	(115,000)
Subtotal: Net Expenditure	**5,399,000**	**5,439,645**	**5,516,455**
Contribution to Reserves	46,600	12,005	4,005
Total Charge to Pension Fund	**5,445,600**	**5,451,650**	**5,520,460**
Membership	164,100	168,200	172,410
Cost Per Member	**£33.18**	**£32.41**	**£32.02**

4.2.2 The operational budget for 2020/21 has been prepared on the basis of a comprehensive, line-by-line review of the cost base of the Authority and includes a reallocation of resources in order to direct the resources available to support a number of areas of growth required to underpin the delivery of the Corporate Strategy. Full details are provided in the Budget report being presented to the Authority for approval. Some of the key cost pressures that have been addressed in this budget are as follows:

- Employee Learning & Development – Investment in developing individuals, including induction, annual programmes of mandatory training, e-learning, professional training and management skills.
- Corporate Governance – Investment in additional resources to ensure timely review of organisational policy framework, to support the democratic process and to monitor compliance and risk.
- Communications & Engagement - as part of ensuring a continuing focus on the needs of our customers, we will invest resources to ensure that suitable processes, tools and technology are in place to enable a greater understanding of the quality and quantity of customer interactions, and to ensure we communicate effectively with all our stakeholders.
- Back Office – Investment to modernise the Authority's back office systems as investment pooling changes the nature of the back office, to become more of a traditional support service than an adjunct to the investment function.
- ICT Infrastructure – Resources have been allocated to support continued development in this area, including the upgrade of MS Office software and back-up solutions as well as investment in the hardware replacement programme with an emphasis on enabling agile working.

4.2.3 The estimates for the remainder of the Medium Term set out above are based on projecting the 2020/21 budget forward, including inflationary increases as necessary.

4.2.4 There will be a continuing pressure for investment and there is equally a need for the Authority to look to deliver savings and efficiencies. These will come through the delivery of work already in hand such as moves to reduce the volume of printing and postage and moves to online interaction with scheme members. However, savings do not always come as direct reductions in the budget. For example, if the administration team does not increase its total head count over the planning period this, all other things being equal, is a productivity improvement (based on the ongoing increase in membership) that equates to a little over 2 FTE each year. These sorts of improvements will be captured and reported in future iterations of this strategy.

4.2.5 The key risks and uncertainties in relation to this forecast are as follows:

- Pay settlements and inflation running at a higher level than assumed in the forecast. This is clearly a risk, and in the case of pay there is significant pent up pressure in the system following a prolonged period of pay restraint. The forecasts used are prudent and reflect a broad consensus view. In the event of higher costs than forecast, managers will seek to absorb the in-year impact through the management of vacancies and seeking to either defer one off expenditure or avoid aspects of running cost expenditure. This is the usual process of budgetary control and it seems unlikely that any cost increases would be on a scale beyond that which measures of this sort could address.
- Deterioration in budgetary control. There has been some change in managerial personnel at senior management level over the last year and work has since been undertaken to strengthen budgetary control processes and procedures. There is therefore no indication of any likelihood of deterioration. The controls in this regard will be subject to internal audit review in the forthcoming financial year.
- Loss of external income. This is mitigated through prudent budgeting, for example not including any assumptions around additional software sales which tend to be sporadic and through securing longer term agreements with customers with staggered end dates so that not all agreements come to an end at the same time.

4.2.6 The operational budget is relatively low risk and is relatively simple in comparison to the Fund Budget being many times smaller and much less volatile. Consequently while it understandably receives specific scrutiny as a cost that, in effect, has to be borne by participants in the Fund, variations are unlikely to have a material impact on the overall standing of the Fund.

4.3 Pension Fund Forecast

4.3.1 The table below presents a summary of the forecast for the Pension Fund for the current and coming three years.

South Yorkshire Pension Fund Financial Forecast	Forecast 2019/20 £	Forecast 2020/21 £	Forecast 2021/22 £	Forecast 2022/23 £
Dealings with members, employers and others directly involved in the scheme:				
Contributions receivable & transfers in from other pension funds	(255,821,120)	(302,703,900)	(313,150,410)	(324,147,290)
Benefits payable and payments to or on account of leavers	342,618,290	332,368,930	349,491,090	365,962,070
Net withdrawals from dealings with members	**86,797,170**	**29,665,030**	**36,340,680**	**41,814,780**
Management expenses	50,769,020	65,388,510	67,587,450	74,122,500
Net returns on investments	(483,604,750)	(455,279,670)	(478,923,530)	(506,307,500)
Net increase in the Fund during the year	**(346,038,560)**	**(360,226,130)**	**(374,995,400)**	**(390,370,220)**
Net Assets of the Fund At 1 April	(8,439,964,660)	(8,786,003,220)	(9,146,229,350)	(9,521,224,750)
Net Assets of the Fund At 31 March	**(8,786,003,220)**	**(9,146,229,350)**	**(9,521,224,750)**	**(9,911,594,970)**

4.3.2 In the first year of the forecast, investment costs (including those within the operational budget) are at 52 bps, which is within the limit of the CEM benchmark as set out elsewhere in this strategy, and are expected to rise up to 69 bps by 2022/23. As the CEM benchmark is only available annually in arrears forward looking forecasts are not available.

4.3.3 The forecast for the Pension Fund is much more susceptible to forecast error than that for the operational budget. In particular, while there is some consistency in terms of data from previous years the Authority cannot control the numbers of members retiring in any year or the decisions which they make in relation to commutation of pension to lump sum. Similarly, the numbers of deaths amongst the membership of the Fund and the numbers of members transferring either into or out of the Fund are changeable and outside the control of the Authority. While the forecasts are based on the best information available using both actuarial results and historic information as adjusted for known one off events and inflation where appropriate, there is a significant amount of variability from year to year which it is extremely difficult to forecast.

4.3.4 The important message in the above forecast is the anticipated net withdrawal from the Fund in each year for dealings with members, this results in a significant increase in the requirement for the harvesting of investment income (at least £20m pa). This will have an impact on the review of the Investment Strategy probably resulting in a prioritisation of investment in assets which generate a consistent long term income stream.

4.3.5 The key risks and uncertainties in the Fund Forecast include the following:

- Financial market volatility, which will impact on both the asset value of the Fund and on the level of investment income and large swings in asset value will result in significant variation from the forecast. This is a constant risk for pension funds and while steps have been taken both through the broad asset allocation and through equity protection to reduce the potential volatility in the Fund the risk of events which might cause significant market dislocation remains and, if anything, is at the current time heightened as a result of tensions around international trade and Brexit.

- A further significant wave of service reductions across major employers resulting in workforce reductions which have the effect of reducing the number of active members contributing and further increase the imbalance between contributions received and benefits paid. Other than changes in the Strategic Asset Allocation to focus on income generation and delivering investment returns above actuarial assumptions to build resilience into the Fund there are limited options available to the Fund in this area, although structuring contribution cash flows may provide some further assistance in dealing with the issue. Political and fiscal uncertainty heightens this risk.
- Failure of pooling to contain investment costs. While SYPA is not expecting to make any significant savings as a result of pooling, in the short to medium term the expectation is that the process of pooling will contain costs. However, should the Pool fail to achieve its objectives in this area there will be an impact on net of fees returns. To date, the evidence is that in this respect Border to Coast are delivering in line with their plan, and should the initial moves of partner funds into the range of internally managed funds continue or increase, there may well be the opportunity for costs in relation to listed assets to reduce towards the pre-pooling levels. If the Pool were to fail to deliver cost savings as anticipated, then further mitigation will come through the collective action of the 12 partner funds to address any underperformance.

4.3.6 This forward forecast indicates a challenging position when viewed in the context of market conditions and uncertainty as at the time of writing. All economic forecasts indicate that we are moving into a somewhat lower return environment which is reflected in the actuarial assumptions used in producing the forecast. This results in the need for the Fund and the Pool to focus on securing good assets and sustained income streams within its revised strategic asset allocation.

5. Policy on reserves

4.4 Reserves

4.4.1 Reserves are funds that are set aside for two main reasons:

- A 'just in case' risk materialises that requires additional resources; or
- To save up for a particular project.

4.4.2 All of SYPA's costs are met by the Pension Fund therefore, unlike a local authority, the first contingency argument for holding reserves does not hold as costs incurred, for example, as a result of a building fire, would simply fall to the Pension Fund which is about 1,000 times the size of the Authority's budget and such costs are therefore unlikely to be material.

4.4.3 The argument for holding reserves to save up for things does, though hold. In order to save up in this way managers will have had to underspend their budgets and thus the ability to use money thus saved acts as an incentive to manage within the available resources.

4.4.4 However, there is a balance to be struck as reserves could be allowed to accumulate to a level where they became significant in the context of the Authority's budget at which point they would in effect be depriving the Fund of cash to invest. Consequently some limitation on the level of reserves is necessary to maintain this balance. The Authority therefore have the following policy in relation to reserves:

"The Authority will maintain its operational revenue reserves at a level equivalent to no more than 7.5% of its operational budget, the establishment of new reserves will be approved by the Authority on the recommendation of the Treasurer, and the level of reserves will be reviewed by the Treasurer each year as part of his report on the final accounts of the Authority."

4.4.5 During 2018/19 and in the current 2019/20 financial year, there have been significant underspends against the budget and these have created an opportunity to set aside these unused funds specifically for use towards financing of some major capital projects that need to be resourced in the medium term period. These projects include:

- The acquisition of new and integrated software systems for Finance, HR and Staff Payroll;
- Re-procurement of Pensions Administration System - funding will be needed for the procurement and evaluation support and, depending on the result of the process, acquisition and licensing costs together with implementation support; and
- Initial scoping of options for long term accommodation which will require external specialist support.

4.4.6 The capital costs of the above projects are expected to be in the region of several hundred thousand pounds and will need to be financed from reserves to the extent these are available, and from 'internal borrowing' from the Pension Fund for the remainder, which would have to be repaid to the Fund over an appropriate timescale. Therefore, Members have been asked to agree a proposal for a new 'Capital Projects' reserve to be created from the 2019/20 underspend and for some of the existing Corporate Strategy reserve to be transferred here as well.

4.4.7 If the proposals are approved by the Authority, the forecast level of reserves are as shown in the following table.

South Yorkshire Pensions Authority Earmarked Reserves	Forecast Balance at 31 March 2020 £	Forecast Balance at 31 March 2021 £	Forecast Balance at 31 March 2022 £	Forecast Balance at 31 March 2023 £
Operational Revenue Reserves:				
Corporate Strategy Reserve	232,831	232,831	232,831	232,831
ICT Development Reserve	113,633	117,633	121,638	125,643
Subtotal - Revenue Reserves	**346,464**	**350,464**	**354,469**	**358,474**
Revenue Reserves as % of Budget	*6.36%*	*6.44%*	*6.50%*	*6.49%*
Capital Projects Reserve	660,000	702,600	710,600	710,600
Total Reserves	**1,006,464**	**1,053,064**	**1,065,069**	**1,069,074**

4.4.8 The above forecast does not include any forecast drawdown of these reserves at this stage and so the figures shown represent the maximum expected balances. The reserves will be drawn upon during the period but we do not currently have enough information to estimate the amounts and timing of these. This will be kept under review and reported to the Authority for approval based on a recommendation from the Treasurer as required through the quarterly reporting of management accounts and financial forecasts.