

About turn

Having transitioned from being the Royal British Legion's finance director to its pension trustee, John Graham tells Natalie Tuck why the scheme is keeping its growth assets while working towards self-sufficiency, rather than the popular option of de-risking

With so many pension scheme buy-ins and buyouts making the headlines, and talk of 2018 as yet another record-breaking year for that sector, it's rare to hear from a pension scheme that has made an 'about turn' from the fashionable de-risking options, and is instead keeping its growth assets while working towards self-sufficiency.

The Royal British Legion's (Legion) pension scheme, however, is one of those schemes. John Graham, who was appointed as the charity's finance director in 2008, but now represents the charity on its pension fund trustee board, set out to "radically change" the scheme when he joined the charity.

"I felt that when I joined the Legion, the fund was too much in the hands of the advisers, so I wanted, as an organisation, to take more control of it, to take charge of the decisions. One of those decisions was to close it to future accrual, which we did in 2010, and set up a defined contribution scheme, which is

with Standard Life," he explains.

Having previously closed to new members in 2002, Graham's radical change began in 2010. Despite the fund closing to future accrual, the active members in the Legion didn't become normal deferred members.

Instead, they became known as 'employed deferred' members, so that any future pay rises during their time at the Legion are reflected in their future pension. At the moment there are around 1,600 employees working for the Legion, and fewer than 100 are still members of the DB scheme.

In terms of the scheme's membership, it had 1,224 total members as of 31 March 2018; Graham notes that the number stays quite static, dropping by around 30 members a year. He says this is because of members' spouses' eligibility for a pension if the member passes away before their partner.

When the scheme closed, Graham says that it became apparent that the pension scheme was becoming "divorced" from the operations of the charity. For example, it was no longer promoted to new employees, nor was it an incentive for people to stay at the organisation.

"It went off the HR agenda and it came very much firmly onto the finance agenda; it became a question of honouring the commitment that had been made to the pensioners as part of the DB scheme. That's where the principle of self-sufficiency came from," he says.

Self-sufficiency

Graham explains that the Legion, likely due to it being a charity, has very strong cash reserves – of around £100 million. This value is greater than the amount of assets that the pension scheme has, worth £91 million. The scheme's most recent actuarial valuation revealed a deficit of £10 million (compared to £5 million in 2014), with the increase being a reflection of the scheme's strategy to work towards self-sufficiency. However, under the latest recovery plan, the Legion is not currently required to pay any deficit contributions and only contributes around £300,000 a year to the scheme to cover the expenses of running the scheme.

Buyout, or any sort of de-risking, is not on the cards for the scheme for the foreseeable future. This is because the Legion's covenant is so strong that it doesn't want to pay a premium that would be required to go to buyout, Graham explains. Therefore, the goal for self-sufficiency, Graham says, is to get to a situation over the next 10-15 years whereby the pension scheme is in a strong enough position to meet its liabilities without going back to the charity.

In order to achieve this, the scheme has reviewed its investment portfolio and recognises that in time, it will be geared towards bonds. "If we want to be self-sufficient, we have to have a lower



risk portfolio,” Graham states, adding that this was the reason for the deficit increase.

“When we decided to target self-sufficiency, we think that up to 80 per cent of our portfolio will need to be in matching assets. The classic matching assets are investment in gilts. At the moment, we are in a mixture of funds, some of which are very vanilla, but some that are trying to do bond plus. They are using investment techniques to make a greater return that you get from straightforward bonds. Our investment consultant is Aon.”

Graham says that the Legion has told the trustee board that, for now, it would like the scheme’s investments to remain at 50 per cent in matching and 50 per cent in growth assets, and the charity is prepared to put its covenant behind that.

“Although we have a target of 10-15 years of being somewhere like 80 per cent of matching assets, we aren’t going in a linear line there. We are seeking to take opportunities up from the growth assets. We have done a Monte Carlo scenario analysis that shows that if the growth assets perform, we’ll get there sooner, and if they don’t perform well we’ll get there later, hence the 10-15 year time frame,” he notes.

However, the Legion very much lets the trustee get on with the running of the scheme, Graham says. It gets involved every three years for the actuarial valuation, and is updated annually by the trustees.

“What we have set out with the Legion is our target of where we want to be. That target is self-sufficiency and we have a map of how we get from where we are now to where we want to be. We are essentially reporting back against that map but that map is on a 10-15 year time horizon,” he says.

ESG

As well as incorporating a strategy that targets self-sufficiency, the trustees are in the process of developing an environmental,

social and governance policy (ESG), following warnings from The Pensions Regulator that not doing so could have a detrimental financial impact.

“We are working on our ESG policy at the moment in the Legion. I was very taken at the *Pensions Age* conference in September 2018, when the regulator stood up and said it is paying attention to ESG because it believes ESG has financial impact. That has woken us all up I think, and on the pension scheme we are applying ESG, and we get reports from our fund managers,” he states.

However, Graham notes that on a member level, the pension scheme isn’t facing any pressures to take up a particular ESG policy. “If you look at what they stand for, they are ex armed forces, so you wouldn’t exclude arms manufacturers from it...And in the past smoking was encouraged in the armed forces.”

As a result, the current debate the trustees are having is on striking the right balance of taking on board the regulator’s warnings on ESG, whilst also keeping the members’ preferences in mind.

Behind the scenes

Graham credits his actuary, First Actuarial founder, Peter Shellswell, and fellow trustee, Punter Southall Governance Services (PSGS) client director, Mark Fletcher, with getting the fund to its current position. “They have played a major part in getting the fund to where it is today, and we couldn’t have got there without them,” Graham states.

Fletcher joined the scheme in 2010, when Graham, as finance director, and the chairman of the Legion, were both trustees. When they sought to close the scheme to future accrual the member trustees were concerned that they had a conflict of interest.

“The chairman and I were removed from the pension scheme, and Mark Fletcher was brought in as an

independent chairman to oversee the closure. He has stayed with us the help us reformulate the governance. We are down to three trustees now. I represent the Legion, there is a member-nominated trustee and there is [Fletcher] as a professional trustee,” he notes.

But what was it like making the switch from finance director to pension trustee? “I’ve had a few chuckles with my fellow trustees,” Graham says. “As finance director my job was to try get the liabilities as the lowest figure on the accounts. As a pension trustee, my responsibility is now very clearly to do the best for the scheme members. I do wear a different hat, but at the same time I still have a commitment to the charity.”

Written by Natalie Tuck

