London Borough of
Barking & Dagenham
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Notice of Meeting

PENSIONS PANEL

Wednesday, 15 March 2017 - 6:00 pm
Committee Room 2, Barking Town Hall

Members: Cllr Dominic Twomey (Chair), Cllr Faraaz Shaukat (Deputy Chair), Cllr Sade Bright, Cllr Edna Fergus, Cllr James Ogungbose, Cllr Jeff Wade and Cllr John White

Independent Advisor: John Raisin

Observers: Bern Hanreck, Gavin Palmer and David Tyndall

Date of publication: 7 March 2017

Chris Naylor
Chief Executive

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AGENDA

1. **Apologies for Absence**

2. **Declaration of Members' Interests**

   In accordance with the Council's Constitution, Members are asked to declare any interest they may have in any matter which is to be considered at this meeting.

3. **Minutes (14 December 2016) (Pages 3 - 8)**

4. **Independent Advisor (Pages 9 - 13)**

5. **Pension Fund Quarterly Monitoring 2016/17 - September to December 2016 (Pages 15 - 45)**

6. **Administration and Governance report (Pages 47 - 52)**

7. **Business Plan Update 2017 (Pages 53 - 56)**

8. **Draft Funding Strategy Statement and Investment Strategy Statement (Pages 57 - 129)**

9. Any other public items which the Chair decides are urgent

10. To consider whether it would be appropriate to pass a resolution to exclude the public and press from the remainder of the meeting due to the nature of the business to be transacted.

Private Business

The public and press have a legal right to attend Council meetings except where business is confidential or certain other sensitive information is to be discussed. The item below contains commercially confidential information which is exempt under paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972 (as amended) and the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

11. Any other confidential or exempt items which the Chair decides are urgent

Our Vision for Barking and Dagenham

One borough; one community; London's growth opportunity

Our Priorities

Encouraging civic pride

- Build pride, respect and cohesion across our borough
- Promote a welcoming, safe, and resilient community
- Build civic responsibility and help residents shape their quality of life
- Promote and protect our green and public open spaces
- Narrow the gap in attainment and realise high aspirations for every child

Enabling social responsibility

- Support residents to take responsibility for themselves, their homes and their community
- Protect the most vulnerable, keeping adults and children healthy and safe
- Ensure everyone can access good quality healthcare when they need it
- Ensure children and young people are well-educated and realise their potential
- Fully integrate services for vulnerable children, young people and families

Growing the borough

- Build high quality homes and a sustainable community
- Develop a local, skilled workforce and improve employment opportunities
- Support investment in housing, leisure, the creative industries and public spaces to enhance our environment
- Work with London partners to deliver homes and jobs across our growth hubs
- Enhance the borough's image to attract investment and business growth

Well run organisation

- A digital Council, with appropriate services delivered online
- Promote equalities in the workforce and community
- Implement a smarter working programme, making best use of accommodation and IT
- Allow Members and staff to work flexibly to support the community
- Continue to manage finances efficiently, looking for ways to make savings and generate income
- Be innovative in service delivery

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MINUTES OF
PENSIONS PANEL

Wednesday, 14 December 2016
(6:03 - 7:06 pm)

Members Present: Cllr Faraaz Shaukat (Deputy Chair in the Chair), Cllr Sade Bright, Cllr James Ogungbose and Cllr John White

Observers Present: Bernie Hanreck

Advisors Present:

Apologies: Cllr Dominic Twomey, Cllr Edna Fergus and Cllr Jeff Wade

18. Declaration of Members' Interests

There were no declarations of interest.

19. Minutes (14 September 2016)

The minutes of the meeting held on 14 September 2016 were confirmed as correct.

20. Triennial Valuation Draft Results

Every three years the Pension Fund was required to have a full valuation of its liabilities carried out by its actuary. The Fund's actuary, Hymans Robertson, would provide a presentation to Members at this Panel on the Triennial Valuation process, the draft results and the process that needed to be followed prior to the valuation being signed off in March 2017.

Officers had discussed the valuation assumptions with the actuary and agreed the main assumptions, including the deficit contributions rate, the discount rate and salary increase assumptions. As a result of these discussions, the actuary could produce the whole fund valuation calculations. The results show that, at a whole Fund level, the deficit has reduced from £266m to £228m and the funding level has improvement to 77.2% from the 2013 level of 70.6%.

Overall the fund has adopted a prudent discount rate of 4.1%. This was lower than the 4.7% used in the 2013 valuation. Members are asked to note that if the Fund used a discount rate of 5%, as used by the government's actuary, that its funding level would be 91%. The deficit recovery period had reduced from 20 years to 17 years and this reflected improvements within the performance of the Fund.

The actuary is in the process of finalising the contribution rates for the borough and all the admitted and scheduled bodies. The actuary and officers will produce a draft Funding Strategy Statement that will then be distributed to Fund employers for their views as part of a consultation.

Once this has been completed the final report can be prepared and the

contribution rates certified. Any agreed changes to the Funding Strategy Statement can also be made. Both documents will then be reported back to the Committee's meeting in March 2017 for agreement.

The Panel noted:

i. The initial results of the actuarial valuation, including the improved funding level and reduced deficit recovery period;

ii. That the Funding Strategy Statement will be updated where necessary for the assumptions made by the actuary and consulted with admitted and scheduled bodies together with their proposed employer contribution rates; and

iii. That the final actuarial valuation results be reported to the March 2017 Pension Panel meeting.

21. Presentation by Hymans Robertson- Triennial Valuation

The Panel received a presentation from Barry McKay, Hymans Robertson and he covered the following areas:

2016 Actuarial Valuation

- Overview of a valuation
- Key funding assumptions (funding level up, deficit down by approximately £100m)
- Experience since 2013
- Whole fund valuation results (funding level improved, deficit reduced)

The National Picture

- so far up to 2016 (for comparison)
- Typical results and summary (contribution rates have remained generally stable or slightly decreased and the recovery period had reduced to seventeen years from twenty)

The Future

- future expectations for asset returns (the outlook is for lower returns)
- LGPS success story (reduced asset dependence and funds holding more assets than before to meet future benefit payments)

Dr McKay summarised by stating that it had been a very challenging actuarial period but was a very positive result with an increased funding level and reduced deficit contributions although there was potentially an increased future cost. Proposed contributions remained broadly the same but would vary by employer.

22. Pension Fund Quarterly Monitoring- July to September 2016

This report provided information for employers, members of London Borough of Barking and Dagenham Pension Fund ("the Fund") and other interested parties on how the Fund had performed during the quarter 1 July 2016 to 30 September 2016 ("Quarter 3"). The report updated the Panel on the Fund's investment

strategy and its investment performance. Due to the technical nature of this report, Appendix 2 provided a definition of terms used in this report and Appendix 3 set out roles and responsibilities of the parties referred to throughout this report.

The Fund's externally managed assets closed Quarter 3 valued at £844.2m, an increase of £53.4m from its value of £790.8m as at 30 June 2016. The cash value held by the Council as at 31 March 2016 was £19.6m giving a total Fund value of £863.8m.

For Quarter 3 the Fund returned 5.3%, net of manager and custodian fees, outperforming its benchmark return of 4.4% by 0.9%. Over one year the Fund returned 17.4%, outperforming its benchmark of 16.6% by 0.8%. Over three years the Fund trails its benchmark by 0.7%, providing a return of 9.4, which exceeds the actuarial return target for the fund of 4.7%.

The Fund's 2014, 2015 and Q3 2016 quarterly returns, its 1, 2, 3 and year returns were provided in table 1 to the report.

A verbal update on the unaudited performance of the Fund for the period 1 October to 12 December 2016 was provided to Members at the Pension Panel.

The GMPT advised that in terms of fund asset allocation, 48.8% were in equities holdings, which is higher than the strategic allocation of 45% and higher than the highest range value of 47%. The increase above the limit is due to the significant devaluation of sterling against most currencies which has significantly increased the value of the Fund's unhedged equities. In addition, infrastructure is currently around 3% below its strategic allocation, with all other allocations within the allocation range bandings. Officers will be looking at the possibility of linking the equities held to the future funding of infrastructure or whether a better option would be to reduce equities to under 47%. As part of the strategy review, Aon Hewitt have been asked to put forward a recommendation of the best approach to both hold assets to fund infrastructure but also to maintain assets within their strategic allocation bandings.

Colin Cartwright (Aon Hewitt) gave his views on the current and future markets situation. He highlighted that asset class returns had done very well although global growth remained weak and the outlook on returns were depressed. Equity markets were volatile at present and interest rates remained low.

The Panel noted:

(i) The progress on the strategy development within the Pension Fund;

(ii) The currency hedges that were placed on the Fund's passive equity mandate on the 30th of September and 7th of October 2016;

(iii) The daily value movements of the Fund's assets and liabilities outlined in Appendix 1; and

(iv) The quarterly performance of pension funds collectively and the performance of the fund managers individually;

23. Administration and Governance Report

It was best practice for Members to receive regular administration data and governance updates. Administration data includes cash flow, member numbers, governance and consultations. This paper covered three main areas including:

i. Pension Fund Budget 1 April 2016 to 31 March 2019;
ii. Cash flow to 31 July 2016; and
iii. Pension Fund Stakeholder Meeting.

The Group Manager, Pensions and Treasury (GMPT) also highlighted that there had been a Pension Fund stakeholder meeting on 17 November 2016 and 24 stakeholders had attended including current members, employers and members of the Pension Board.

The GMPT also advised that an Actuary meeting was held on 17 November 2016 with the Fund's employers to discuss the Triennial results.

The Panel noted that there was no link shown at item 4.4 in the report and this would be e-mailed to Members by the Democratic Services Officer.

The Panel noted:

i. that the Fund is cash flow positive;
ii. the Fund's three-year budget for the period 1 April 2016 to 31 March 2019; and
iii. the Fund's 2016/17 cash flow was forecast to be significantly higher than the budgeted cash flow, predominantly due to investment returns.

24. London Borough of Barking and Dagenham Admission Policy

At present, the Pension Fund had a number of Admitted Bodies, some of which have been members of the London Borough of Baking and Dagenham Pension Fund ("the Fund") for a number of years.

As Administering Authority, the Council had the discretion to allow Admission Agreements with organisations that fit the criteria within the Local Government Pension Scheme ("the LGPS").

To ensure potential admitted bodies were aware of the requirements prior to joining the Fund an Admissions Policy had been drafted. The Admissions Policy would provide the structure and the governance requirements necessary to ensure the risks associated with allowing Admitted Bodies into the Fund were reduced.

The Panel were asked to agree a revised Admissons Policy, in light of changes to the Council's structures as a result of Ambition 2020 and the increase in Academies and Free Schools.

All applications to be an Admitted body within the Fund would be required to be agreed by the Pension Panel, with the recommendation that the due diligence and implementation of the Admission Policy was delegated to the Finance Director.

The Panel:

- Agreed the Pension Fund's Admission Policy for 2017; and

- Delegated responsibility to the Finance Director to carry out the due diligence and implementation of the Admission Policy.

25. Business Plan Update 2016

The purpose of this report updated the Pension Panel on progress regarding the Pension Fund's 2016 business plan.

Appendix 1 provided a summary of the Business Plan actions from 1 January 2016 to 30 November 2016 and the actions for the remainder of the year.

The Panel noted progress on the delivery of the 2016 Business Plan at Appendix 1 to the report.

26. London Borough of Barking and Dagenham Pension Fund Business Plan 2017

The Local Government Pension Scheme ("the LGPS) was an occupational pension scheme that had been established by Act of Parliament and was governed by regulations made under the Superannuation Act 1972. The London Borough of Barking and Dagenham Pension Fund ("the Fund") is maintained under the Act.

The Fund was responsible for providing retirement and other benefits to employees of The London Borough of Barking and Dagenham ("the Council"). Fund membership was approaching 17,500 with 27 employers, including admitted and scheduled bodies. Administration of the Fund was the responsibility of the Council, which also had overall responsibility for the investment of the Fund's assets and pension administration services to members of the Fund and their employers.

The publication of the Myners Report and the subsequent CIPFA "Principles for Investment Decision Making in the LGPS in the United Kingdom" (CIPFA's Investment Code of Practice) and "Investment Decision Making and Disclosure", recommended that the Section 151 officer prepare and submit to the Pension Panel ("the Panel") an annual business plan ("the BP") for the Fund.

The Business Plan identified and outlined the key tasks for 2017, with progress reported on at each quarterly Panel. The key tasks identified reflected the Panel's commitment to developing a suitable investment strategy and monitoring procedures for the coming year which met the Fund's objectives and complies with best practice.

The Business Plan outlined the operation of the Fund and included provision for training and development. The proposed training and development would equip Panel Members with the necessary skills to make informed decisions on the Fund's investments. A list of key tasks and milestones were outlined in Appendix 1 to this Business Plan.

CIPFA recommended that all Panel Members should have the necessary skills and knowledge to adequately fulfil their governance and fiduciary duties to the Fund Members. Training requirements and proposed training were outlined in section 10 to the report.

Further training for the Panel would be held on 2 February 2017 on the Pension Fund Strategy and Strategy review and following a questionnaire to Members at the March 2017 Panel, a 2017/18 training plan will be presented for Member approval at the June 2017 meeting.

The Panel agreed the Business Plan 2017.

27. Vote of thanks

The Chair, on behalf of the Panel, accorded thanks to the Strategic Director, Finance and Investment, who was leaving the Council at the end of December 2016. In particular they extended their good wishes and thanked him for his support to the Panel over the years.

PENSIONS PANEL

15 March 2017

Title: Independent Advisor	
Report of the Chief Operating Officer	
Public Report	**For Information**
Wards Affected: None	**Key Decision:** No
Report Author: David Dickinson, Group Manager Pensions and Treasury	**Contact Details:** Tel: 020 8227 2722 E-mail: david.dickinson@lbbd.gov.uk
Accountable Director: Kathy Freeman, Director of Finance	
Accountable Strategic Director: Claire Symonds, Chief Operating Officer	
Summary: This report outlines the role of the London Borough of Barking and Dagenham Pension Fund's Independent Advisor. The report includes a review of the work the Independent Advisor's work during the past year.	
Recommendations Members are asked to agree to extend agree to extend the Independent Advisors role, currently carried out by John Raisin Financial Services Limited, as the Panel's investment advisors for one year based on the revised job description included as appendix 1 of this report.	

1. Introduction and Background

1.1 At the December 2014 Pension Panel, Members requested officers to start the procurement of an Independent Advisor (“IA”) to support the Panel Members.

1.2 On 11 February 2015 a sub-group of six Members interviewed three candidates, with the sub-group Members agreeing to appoint John Raisin, operating as John Raisin Financial Services Limited (“JFRS”), subject to formal agreement by Panel.

1.3 At the 23 March 2015 Pension Panel Members agreed to award John Raisin a one year contract to 23 March 2016.

1.4 At the 15 March 2016 Pension Panel Members agreed to award John Raisin a one year contract to 23 March 2017.

2. Review of Independent Advisor during 2016/17

2.1 Throughout 2016/17 John Raisin has provided support in several key areas including:

i. additional expertise at Panel Meetings;
ii. Advice on Fund Managers and Strategy;
iii. Updates on regulation and legislation changes; and
iv. training to both Pension Panel and Board Members.

3. Contract Renewal and Recommendation

3.1 The IA contract is subject to an annual review. It can be terminated by either not renewing the contract, or by providing three months’ notice of the contract termination.

3.2 It is expected, were the contract with JRFS extended, that it is would continue to include additional support with Member Training and as the Fund transitions to a more collaborative investment approach. JRFS will also be asked to provide Members a short summary, prior to each Pension Panel, of the main issues covered within the Panel Papers. The summary will also include questions that Member can ask of officer, fund managers and the advisors.

3.3 In addition, the IA is expected to actively participate in the implementation of the Fund’s strategy review.

3.4 The IA contract has therefore been amended to include these changes and is included as appendix 1 of this report for reference.

3.5 Members are recommended to agree to extend the contact with JRFS as the Panel’s independent advisor for an additional one year contract to 31 March 2018.

List of appendices:

Appendix 1 - Independent Advisor Specifications for 2017/18

Independent Advisor Specifications 2017/18

Independent Advisor ("IA")– Role Specifications

Knowledge and Personal Attributes

The responsibilities of the Investment Advisor include, but are not limited to:

1. Providing input and advice on the London Borough of Barking and Dagenham Pension Fund's ("the Fund") Strategic Asset Allocation Review and the Fund's de-risking and currency hedging strategy and support members to consider this.
2. Attending quarterly pension panel meetings, including interpreting and reporting on fund performance.
3. Support Members at Pension Panel and Fund Manager meetings to enable Members to sufficiently and suitably interrogate the advice and explanations given by the Fund managers, officers, advisors and the actuary.
4. Advising on the development of Fund Governance arrangements taking into consideration recent and future legislation and regulation changes.
5. Supporting, where required, in the preparation and provision of training, to the Panel.
6. Advising the Panel on changes and compliance in relation to all statutory documents.

Knowledge, skills and attributes

The IA is expected to have all the essential Knowledge, skills and attributes:

Essential:

- worked at a senior level in the investments/pensions industry;
- an understanding of the implications for pension funds of developments in the economy and financial markets;
- broad-ranging knowledge of the pension environment, in particular the LGPS;
- a good understanding and experience of asset allocation strategies suited to improve long-term investment returns; and
- an ability to communicate and explain economic and investment concepts simply in both verbal and written form.

Desirable:

- an investment-related qualification; and
- experience of interacting with Councillors, acting as Trustees, and an appreciation of the local government environment within which the Fund operates.

This is a one year appointment; however, it can be terminated by either party with three months' notice. In addition each year the contract will be reviewed and extended where required.

Remuneration and Expenses:

The annual remuneration for the position of IA is £15k, paid quarterly in arrears. The remuneration will be based on experience, and the requirements outlined below:

The IA is expected to make themselves available to attend:

1. Up to five Panel meetings per year (meetings may take place in Barking and currently start at 18:00 on weekdays);
2. An annual meeting with Fund Managers which may be split over two half days;
3. Two training half sessions of three hours each; and
4. Two ad hoc meetings of no more than 3 hours each a year as required.

It is expected that the IA will sufficiently prepare for the quarterly Pension Panel meetings. The IA is not expected to provide any reports for Members consider but may do so after prior agreement from the Chair.

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PENSIONS PANEL

15 March 2017

Title: Pension Fund Quarterly Monitoring 2016/17 – September to December 2016	
Report of the Chief Operating Officer	
Public Report	**For Information**
Wards Affected: None	**Key Decision:** No
Report Author: David Dickinson, Group Manager Pensions and Treasury	**Contact Details:** Tel: 020 8227 2722 E-mail: david.dickinson@lbbd.gov.uk
Accountable Director: Kathy Freeman, Director of Finance	
Accountable Strategic Director: Claire Symonds, Chief Operating Officer	

Recommendations

The Panel is recommended to note:

(i) the progress on the strategy development within the Pension Fund;

(ii) the daily value movements of the Fund's assets and liabilities outlined in Appendix 1; and

(iii) the quarterly performance of pension funds collectively and the performance of the fund managers individually;

1. Introduction and Background

1.1 This report provides information for employers, members of London Borough of Barking and Dagenham Pension Fund ("the Fund") and other interested parties on how the Fund has performed during the quarter 1 October 2016 to 31 December 2016 ("Q4"). The report updates the Panel on the Fund's investment strategy and its investment performance. Due to the technical nature of this report, Appendix 2 provides a definition of terms used in this report and Appendix 3 sets out roles and responsibilities of the parties referred to throughout this report.

1.2 A verbal update on the unaudited performance of the Fund for the period 1 January to 12 March 2017 will be provided to Members at the Pension Panel.

2. Third Quarter Market Performance

The final quarter of 2016 was dominated by the US presidential election and the surprise victory for Donald Trump, a result which confounded polls, commentators and markets alike. Volatility ensued as investors tried to glean policy cues and implications from a distinctly non-traditional campaign. Overall, equity markets were net winners and bond markets were net losers. The US dollar strengthened, inflation expectations were revised up and additional US federal borrowing was factored in to fund more expansionary fiscal policy.

Equity markets performed strongly albeit with considerable divergence between Developed and Emerging Markets, with the latter struggling in the face of the rising dollar and increasing Treasury yields. While the MSCI World Index advanced 7.2% to a UK investor during the final quarter, the MSCI Emerging Market returned a lesser 0.8%. Within Emerging Markets, indices that did perform well were typically those with a heavy oil influence, brent oil prices rose 15.8% during the quarter to end the year at $56.82.

US equities rallied strongly following the elections and in the final quarter the S&P 500 was up 9%. Financials led the charge with higher interest rates seen as positive for the sector, as was the possibility of a more favourable regulatory landscape. Brexit remained to the fore in the UK with the High Court ruling Parliamentary approval is needed to trigger Article 50. Despite the uncertainty surrounding Brexit, the UK economy performed well: GDP growth was a solid 0.5% and the FTSE All Share Index rose 3.9%. In sterling terms, the FTSE Europe index returned 4.8%; in Japan the Nikkei rose 6.1% (Yen weakness dampened returns for Uk investors) and the FTSE Pacific ex Japan returned 1.7%.

Fixed income markets began the quarter with yields still close to record lows but the surprise US presidential election outcome had a pronounced impact on global bond markets. The JPM Global Index was down 3.6% over the period; within UK markets the BAML Broad UK Index was down 3.4% and UK Index Linked >5 years down 3.0%.

Dollar strength defined the fourth quarter as it advanced versus all the major currencies. Sterling lost about 5% against the US Dollar but gained over 1% against the Euro and nearly 9% against a weak Japanese Yen. Property returned 2% over the quarter.

3. Overall Fund Performance

3.1 The Fund's externally managed assets closed Q4 valued at £869.6, an increase of £25.4m from its value of £844.2m as at 30 September 2016. The cash value held by the Council at 31 December 2016 was £12.7m giving a total Fund value of £882.3m.

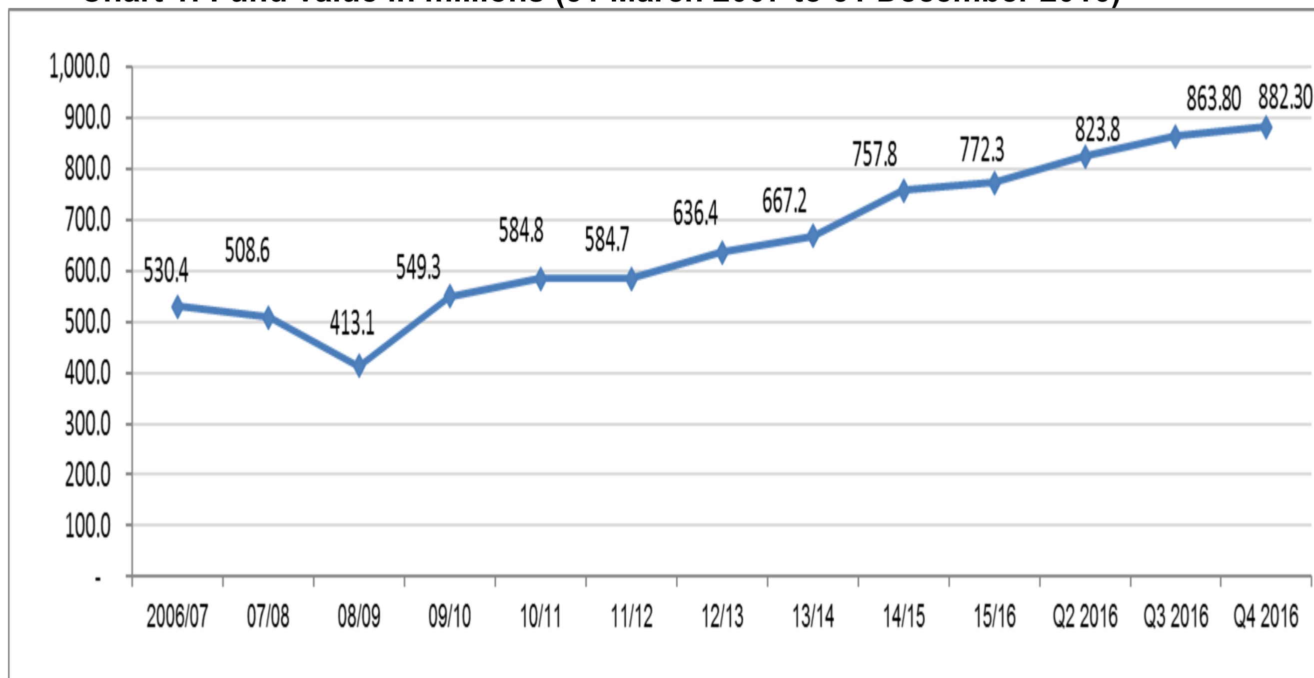
3.2 For Q4 the Fund returned 3.7%, net of manager and custodian fees, outperforming its benchmark by 0.1%. Over one year the Fund returned 16.7%, outperforming its benchmark of by 1.1%. Over three years the Fund trails its benchmark by 0.3%, providing a return of 9.8. The Fund's quarterly and annual returns are provided below:

Table 1: Fund's Q3 2016, 2015 and 2014 Quarterly Returns and yearly returns

Year	2016				2015				1	2	3	5
Period	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1	yr	yrs	yrs	yrs
Actual Return	3.7	5.3	4.2	2.5	4.4	(2.5)	(3.3)	10.0	16.7	12.2	9.8	9.6
Benchmark	3.6	4.4	4.7	2.0	4.5	(1.4)	(1.8)	10.7	15.6	13.3	10.1	10.2
Difference	0.1	0.9	(0.5)	0.5	(0.1)	(1.1)	(1.5)	(0.7)	1.1	(1.1)	(0.3)	(0.6)

3.3 Appendix 1 illustrates changes in the market value, the liability value, the Fund's deficit and the funding level from 31 March 2013 to 25 November 2016. Members are asked to note the significant changes in value and the movements in the Fund's funding level. Chart 1 below shows the Fund's value since 1 July 2007.

Chart 1: Fund value in millions (31 March 2007 to 31 December 2016)



3.4 Stock selection was not a factor in the overall above benchmark, with asset allocation contributing 0.1% for the quarter. The fund manager's performance has been scored using a quantitative analysis compared to the benchmark returns, defined below.

	RED- Fund underperformed by more than 75% below the benchmark
Δ	AMBER- Fund underperformed by less than 75% below the benchmark.
O	GREEN- Fund is achieving the benchmark return or better

3.5 Q4, (table 2 below), highlights the best performers were equities, with most other assets providing positive returns. Newton and UBS bonds provided negative returns, with Newton's return of -5.0% significant. Property showed a small bounce following the negative returns immediately following the referendum results.

Table 2 – Fund manager Q4 performance

Fund Manager	Actual Returns (%)	Benchmark Returns (%)	Variance (%)	Ranking
Aberdeen	0.5	1.1	(0.6)	Δ
Baillie Gifford	3.9	6.5	(2.6)	Δ
BlackRock	1.5	2.3	(0.8)	Δ
Hermes GPE	1.8	1.4	0.4	O
Kempen	10.9	7.1	3.8	O
M&G	0.9	1.1	(0.1)	Δ
Newton	(5.0)	1.0	(6.0)	□
Pyrford	0.6	2.0	(1.4)	Δ
Schroders	2.7	2.3	0.4	O
Standish	0.7	1.1	(0.4)	Δ
UBS Bonds	(3.3)	(3.4)	0.1	O
UBS Equities	6.6	6.4	0.2	O

3.6 Over one year, (table 3 below), equities have provided good returns of between 23.2% and 32.8%, with Kempen's return is particularly welcome. Infrastructure, Pyrford and bonds have also provided near double digit returns. Standish remains behind its benchmark but has met its target over the three quarters.

Table 3 – Fund manager performance over 12 months

Fund Manager	Actual Returns (%)	Benchmark Returns (%)	Variance (%)	Ranking
Aberdeen	1.6	4.4	(2.8)	Δ
Baillie Gifford	23.2	26.7	(3.5)	□
BlackRock	0.5	2.8	(2.3)	Δ
Hermes GPE	11.8	5.6	6.2	O
Kempen	32.8	26.9	5.9	O
M&G	4.4	4.4	0.0	O
Newton	4.8	4.3	0.5	O
Pyrford	9.3	7.3	2.0	O
Schroders	2.0	2.8	(0.8)	Δ
Standish	1.1	4.8	(3.7)	□
UBS Bonds	10.2	10.1	0.0	O
UBS Equities	25.9	25.7	0.2	O

3.9 Over two years, (table 4 below), most mandates are positive, with returns ranging from (0.4%) with Standish to 18.3% with Kempen. Only Standish has significantly underperformed its benchmark, with a negative return of 5.8% over the two-year period. The property correction following the referendum result has had an impact on

property but the returns over two years remain positive and are in line with most other asset classes, with the exception of equities.

Table 4 – Fund manager performance over two years

Fund Manager	Actual Returns (%)	Benchmark Returns (%)	Variance (%)	Ranking
Baillie Gifford	16.0	15.7	0.3	O
BlackRock	5.3	7.3	(2.0)	Δ
Hermes GPE	8.1	5.6	2.5	O
Kempen	18.3	16.3	1.9	O
M&G	4.4	4.4	0.0	O
Newton	3.4	4.4	(1.0)	Δ
Pyrford	5.6	6.7	(1.1)	Δ
Schroders	6.4	7.2	(0.8)	Δ
Standish	(0.4)	5.4	(5.8)	□
UBS Bonds	5.5	5.4	0.0	O
UBS Equities	16.1	15.8	0.3	O

4. Asset Allocations and Benchmark

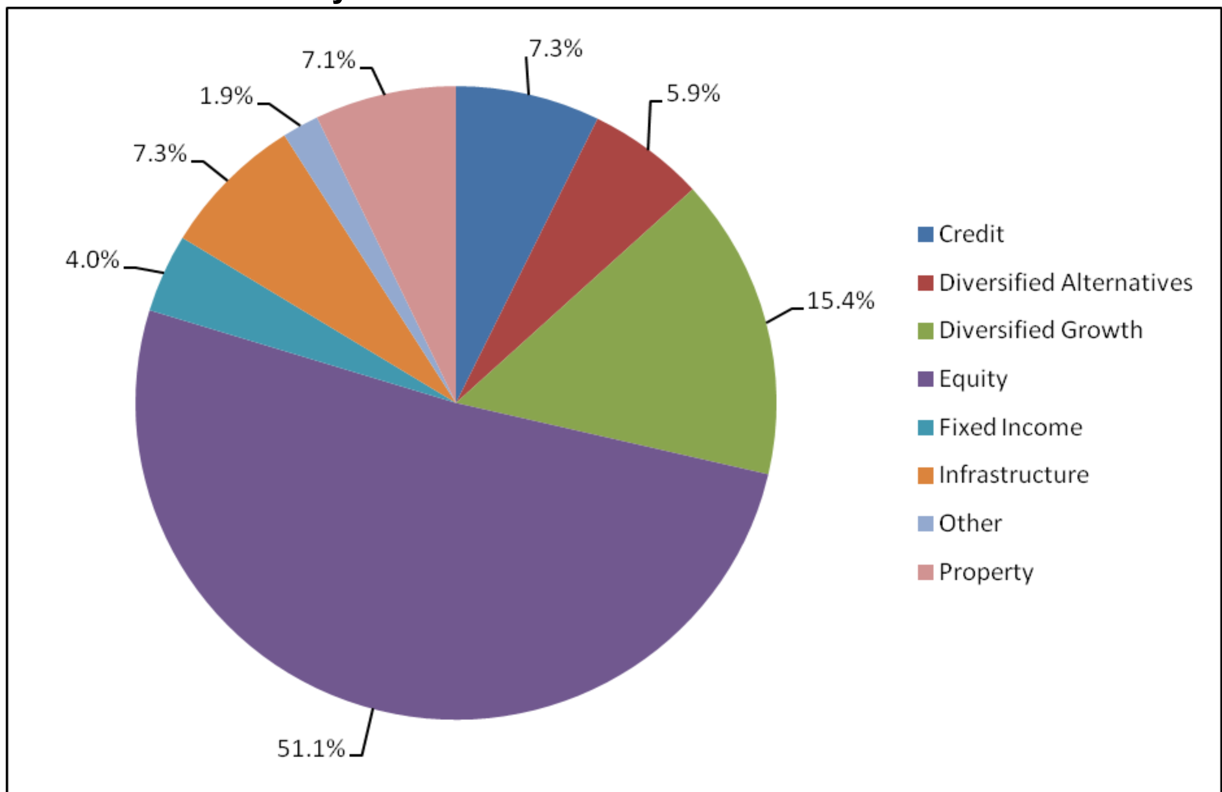
4.1 Table 5 below outlines the Fund's strategic asset allocation, asset value and benchmarks:

Table 5: Fund Asset Allocation and Benchmarks as at 31 December 2016

Fund Manager	Asset (%)	Market Values (£000)	Benchmark
Aberdeen	5.9%	52,362	Libor + 4% (net of fees)
Baillie Gifford	17.3%	153,011	MSCI AC World Index
BlackRock	4.5%	39,840	IPD PPF All Balanced Property Funds
Hermes GPE	7.3%	64,252	Target 5.9% per annum
Kempen	16.6%	146,391	FTSE All World Developed
M&G	0.4%	3,489	None
Newton	6.2%	55,097	Libor + 4% (net of fees)
Pyrford	9.2%	80,950	One month LIBOR plus 4%
Schroders	2.6%	23,039	RPI plus 5%
Standish	7.3%	64,139	IPD PPF All Balanced Property Funds
UBS Bonds	4.0%	35,305	6% Target Return
UBS Equities	17.2%	151,542	FTSE All Stock Gilt Index
Cash & other	1.4%	12,841	One month LIBOR
Total Fund	100.0%	882,258	

4.2 The percentage split between managers is graphically shown in the pie chart below.

Chart 2: Fund Asset by Asset as at 31 December 2016



5. Fund Manager Performance

5.1 Kempen

	2016				2015				One	Two	Since
Kempen	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£146,391	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	10.9	10.2	5.8	5.9	7.5	(5.8)	(5.7)	7.7	32.8	18.3	7.6
Benchmark	7.1	7.9	9.7	2.2	8.4	(4.8)	(5.3)	7.5	26.9	16.3	12.1
Difference	**3.8**	**2.3**	**(3.9)**	**3.7**	**(0.9)**	**(1.0)**	**(0.4)**	**0.2**	**5.9**	**1.9**	**(4.5)**

Reason for appointment

Kempen were appointed as one of the Fund's global equity managers, specialising in investing in less risky, high dividend paying companies which will provide the Fund with significant income. Kempen holds approximately 100 stocks of roughly equal weighting, with the portfolio rebalanced on a quarterly basis. During market rallies Kempen are likely to lag the benchmark.

Performance Review

The quarter was very positive for Kempen, with a return of 10.9%, an outperformance against its benchmark of 3.8%. For the one and two-year return Kempen have outperformed their benchmark by 5.9% and 1.9%. Kempen's outperformance over the past year is particularly welcome as Kempen have previously attended the Pension Panel to provide an explanation for their underperformance and Members agreed to maintain the holding with Kempen.

Overall the quarterly rebalancing of the portfolio provided a significant positive return, with sector allocation and stock selection also providing positive returns for the quarter. The strategies sector allocation, mainly relating to emerging market exposure, also provided some of the outperformance, however the strategies underweight exposure to the US did provide a negative attribution for the quarter.

Outlook

Kempen have seen high volatility among their holdings despite there being limited changes the firms intrinsic value. Kempen believe that their rebalancing process continues to add value by taking advantage of this volatility. Overall market multiples remain elevated, but the dispersion both within and between sectors has increased.

Kempen's focus is on finding companies with sustainable dividends that can be bought at a discount to their estimate of intrinsic value. Kempen base their estimate on the Earnings Power Value (EPV) framework of the Columbia Business School. EPV allows us to separate the three valuation components: asset value, earnings power and growth value. This framework improves their ability to analyse what Kempen are paying for, and gives insight into whether a stock is priced with a margin of safety.

The Fund now has a forward yield of around 4.7% compared to the MSCI world average of 2.5%

5.2 Baillie Gifford

	2016				2015				One	Two	Since
Baillie Gifford	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£153,011	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	3.9	12.1	6.9	0.3	10.4	(5.8)	(4.9)	9.1	23.2	16.0	13.0
Benchmark	6.5	8.5	8.8	2.9	8.1	(5.9)	(5.1)	7.6	26.7	15.7	11.5
Difference	**(2.6)**	**3.6**	**(1.9)**	**(2.6)**	**2.3**	**0.1**	**0.2**	**1.5**	**(3.5)**	**0.3**	**1.5**

Reason for appointment

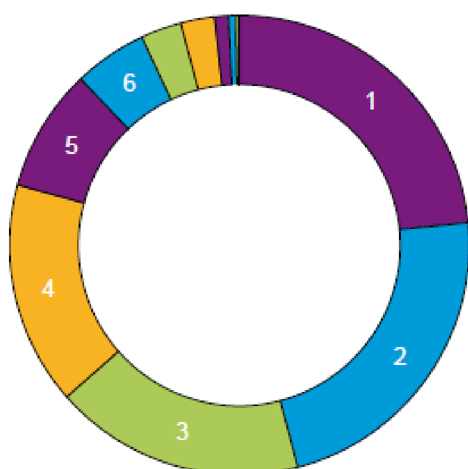
Baillie Gifford (BG) is primarily a bottom-up, active investor, seeking to invest in companies that it believes will enjoy sustainable competitive advantages in their industries and which will grow earnings faster than the market average. The aim of the Global Alpha investment process is to produce above average long term performance by picking the best growth stocks available around the world by combining the specialised knowledge of BG's investment teams with the experience of their most senior investors. BG holds approximately 90-105 stocks.

Performance Review

Over the quarter the Fund underperformed against Benchmark by 2.6%, which whilst disappointing, does cover an extremely volatile period in markets covering the Brexit vote in the UK and the election of Trump in the US and follows a very strong quarter in Q3 of 3.6% against Benchmark. Since inception Fund has outperformed it's benchmark by 1.5% per year.

Whilst the portfolio benefitted from an overweight position in financials during the quarter, underweight positions in energy and consumer staples would have had a negative impact, particularly given the bounce in resource stocks towards the end of the year. Performance was disappointing from the perspective of what the fund didn't hold rather than what it did as oversold cyclical and resource stocks rallied. In terms of the outlook, the fund is positioned to take advantage of continued recovery in the US economy as a result of the US election and the prospects for fiscal stimulus.

The sector breakdown of the portfolio is set out below:



Sector Weights		(%)
1	Financials	23.4
2	Information Technology	22.5
3	Consumer Discretionary	17.6
4	Industrials	15.7
5	Health Care	8.6
6	Materials	5.2
7	Energy	2.9
8	Consumer Staples	2.4
9	Cash	1.0
10	Real Estate	0.5
11	Telecommunication Services	0.2
	Total	100.0

5.3 UBS Equities

	2016				2015				One Year	Two Years	Since Start
UBS Equities	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**			
£151,542	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	6.6	8.2	8.7	2.4	8.6	(4.8)	(5.2)	7.7	25.9	16.1	14.6
Benchmark	6.4	8.2	8.7	2.4	8.6	(5.0)	(5.3)	7.6	25.7	15.8	14.6
Difference	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**	**0.2**	**0.1**	**0.1**	**0.2**	**0.3**	**0.0**

Reason for appointment

UBS were appointed as the Fund's passive equity manager to reduce the risk from underperforming equity managers and provides a cost-effective way of accessing the full range of developed market equity growth. UBS track the developed world market benchmark and there will only be an issue with performance were the manager to vary significantly from the benchmark, either positively or negatively.

Performance

2016 ended with global equities entering a bull market from the low point seen in February. After an initial fall upon the US election results, developed equity markets quickly recovered and advanced on the anticipation of fiscal stimulus under the new administration. The prevailing mood was not broken by Italian referendum voters rejecting proposed constitutional reform or the decision by the US Federal Reserve to increase interest rates in December. The renewed focus on fiscal rather than monetary stimulus helped drive government bond yields higher from the low levels seen during the third quarter.

Equity markets worldwide had another strong quarter, with benchmark indices in the UK and US hitting all-time highs. In local currency terms, the FTSE All-World index returned almost 10% for the year, despite the weakness seen early 2016.

US markets had seen volatility in October due to perceived likelihood of a Trump administration. After the initial shock, US stocks rallied sharply on the prospect of fiscal stimulus, a lighter regulatory regime and reduced corporate taxes. The outlook for US corporate profits has been upgraded for 2017.

However, there was more nervousness around the outlook for emerging markets given the tone of Trump's comments during the campaign and a stronger US dollar. But improving oil prices boosted markets such as Russia and Brazil.

European equities fared well during Q4, despite continued speculation over the health of the Italian banking sector. The ECB's decision to extend its QE programme until at least December 2017, albeit at a gentler pace, was welcomed, with EU stocks enjoying a strong quarter. In the UK, previously unfavoured sectors such as mining and banks strengthened, aided by support from the Prime Minister for an 'implementation phase' to allow Britain to exit the EU smoothly after 2019.

Following weakness earlier in the year, Japan was the best performing major market as 2016 ended. The boost from the continuing recent weakness in the yen was sufficient to offset weak domestic economic data in December.

5.4 UBS Bonds

	2016				2015				One	Two	Since
UBS Bonds	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£35,305	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	(3.3)	2.3	6.2	5.0	(1.2)	3.1	(3.4)	2.2	10.2	5.5	8.3
Benchmark	(3.4)	2.3	6.2	5.0	(1.2)	3.1	(3.4)	2.2	10.1	5.4	8.3
Difference	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.1**	**0.1**	**0.0**

Reason for appointment

UBS were appointed as the Fund's passive bond manager to allow the Fund to hold a small allocation (5%) of UK fixed income government bonds.

Market Update

The surprise election of Donald Trump as the 45th President of the United States back in November has had a significant impact on the economic outlook and the financial markets. With the support of a Republican controlled Congress, Trump is likely to enact inflationary and pro-growth policies through tax cuts and infrastructure spending.

In contrast, the decision by the US Federal Reserve's Open Markets Committee (FOMC) to increase the Fed Funds range's target rate by 25bps has been widely discounted by the market. This decision means rising inflation risks, higher employment and, an overall demand growth that has been expanding at a moderate pace since mid-year.

Economic data over the quarter reflected improvements in key economies, raising further doubts about the outlook for monetary policy. Following fears of a slowdown in China at the beginning of 2016, year-end trade data surprised economists as higher export and import flows indicated stronger demand in Chinese products globally.

Performance

The rising trend seen in government bond yields seen towards the end of the third quarter continued into the final three months of the year. The election of a Trump administration was just the most evident of a series of shifts in the discussions on how best to stimulate growth and inflation, with the likelihood of less reliance on monetary policy in isolation in future. The result was increasing doubt on the sustainability of 'lower for longer' policies.

Prices for fixed income securities fell almost across the board. US Treasuries saw the sharpest falls, with the yield on the 10-year bond rising by over 0.8% and inflation expectations spiking higher.

Yields on both fixed and index linked gilts also rose from the record lows seen in August. US high yield was one of the few fixed income asset classes to see a positive return over the quarter, with higher oil prices helping drive prices higher in December.

5.5 BlackRock

	2016				2015				One	Two	Since
BlackRock	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£39,840	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	1.5	(3.5)	1.3	1.2	2.5	2.5	2.9	2.2	0.5	5.3	11.3
Benchmark	2.3	(0.7)	0.1	1.1	3.0	3.0	3.1	2.8	2.8	7.3	12.5
Difference	**(0.8)**	**(2.8)**	**1.2**	**0.1**	**(0.5)**	**(0.5)**	**(0.2)**	**(0.6)**	**(2.3)**	**(2.0)**	**(1.2)**

Reason for appointment

In March 2012, a large portion of the Fund's holdings with Rreef were transferred to BlackRock (BR). The transfer to BR provides the Fund with access to a greater, more diversified range of property holdings within the UK.

Summary of Fund Activity

In Q4 liquidity returned to the market and BlackRock took advantage of this by selling a portfolio of 11 smaller, secondary assets. This sorted out most of the remaining non-core holdings in the Fund and removed assets vulnerable in a falling market. Letting activity remained reasonably strong for assets outside the Central London Office sector. A number of key lettings were completed, most notably:

- Tor Maidenhead: Lease agreement signed with Rank Group; and
- Leicester Distribution Park: 20 year pre-let to Samworth Brothers.

The returns for Q4 surprised on the upside with an unexpectedly strong capital value uplift for Central London and South East Offices. BlackRock believe this "bounce" is unlikely to be sustained and this will be proven out over the coming quarters. The Fund's overweight to the defensive Alternatives and underweight Offices held back performance in Q4. BlackRock believe that in line with their forecasts for a decline in capital values for Central London and South East Offices over the next 12 – 24 months, that the Fund's structure is well placed. Alongside a belief in allocations, the portfolio also has numerous asset management opportunities to drive performance.

Following the completion of c. £98m of sales in Q4, BUKPF held an overweight cash position which dragged performance by c. 20bps. Within the BUKPF portfolio there is a pipeline of significant capital projects that this cash is being deployed into, and it will also enable the Fund to take advantage of investment opportunities that emerge from the expected market volatility.

Referendum Result Impact on UK Property

As Article 50 is triggered and negotiations for the UK's exit from the EU begin, there will be times of optimism and pessimism, which creates volatility. As Brexit plays out it will entail challenges for the economy and the financial services sector. With this back drop, BlackRock continues to believe that the Fund's overweight to Industrials and Alternatives, and underweight Retail and Central London Offices mean it is well placed. The countercyclical nature of our favoured sectors and the structural change driving their returns, mean that BlackRock are confident of their performance even in the lower return environment.

5.6 Schroders Indirect Real Estate

	2016				2015				One	Two	Since
Schroder	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£23,039	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	2.7	3.7	(5.2)	0.8	2.4	3.0	2.6	2.8	2.0	6.4	6.0
Benchmark	2.3	(0.7)	0.1	1.1	2.8	3.0	3.1	2.8	2.8	7.2	8.5
Difference	**0.4**	**4.4**	**(5.3)**	**(0.3)**	**(0.4)**	**0.0**	**(0.5)**	**0.0**	**(0.8)**	**(0.8)**	**(2.5)**

Reason for appointment

Schroders is a Fund of Fund manager appointed to manage a part of the Fund's property holdings. The mandate provides the Fund with exposure to 210 underlying funds, with a total exposure to 1,500 highly diversified UK commercial properties.

Market summary

Although the UK economy performed better than expected in the six months following the EU referendum, it was dependent on consumer spending. For 2017, consumption is likely to lose momentum, as inflation overtakes annual wage awards. Inflation is forecast to rise to 3% by the end of 2017 partly due to the rebound in oil prices, but mainly because of the 18% fall in sterling's trade weighted index over the last 12 months. While that should help UK exports, history suggests the impact will be limited and the uncertainty over the future terms of trade with the EU may depress investment. Schroders expects GDP growth to slow to around 1.0-1.5% in 2017.

The mixed outlook for the economy is reflected in occupier demand. Brexit has not so far deterred tech companies from taking more office space in central London and the volatility in financial markets has supported demand from hedge funds for offices in Mayfair and St James's. Similarly, there is continued demand for regional offices from professional service firms and the government's plan to consolidate the civil service outside London into 13 hubs will provide further support to office markets in cities such as Birmingham, Bristol, Leeds and Manchester. In addition, the industrial and distribution sectors continue to benefit from the growth of online retail, parcel deliveries.

In the investment market, initial yields rose 0.25% following the EU referendum, as investors downgraded expectations for rental growth and as the authorised open ended retail funds sold assets to meet redemptions. However, Q4 saw a partial return to normality and real estate yields were broadly stable. The key unknown in 2017 is real estate yields. Theory suggests yields should increase, given the upturn in long dated UK and international bond yields since August and the growing prospect of a fall in London office rents and retail rents outside London. In 2017 Schroders' base case is for the all property initial yield to rise 0.25-0.5%, mostly in the secondary property.

Performance

Schroders still remain behind their benchmark over most periods and there is an expectation that they will outperform the market in 2017 as the strategies diversification into alternatives provides support.

5.7 Hermes

	2016				2015				One	Two	Since
Hermes	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£64,252	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	1.8	1.6	2.5	5.9	0.3	1.7	1.1	1.3	11.8	8.1	11.6
Benchmark	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	5.6	5.6	5.9
Difference	**0.4**	**0.2**	**1.1**	**4.5**	**(1.1)**	**0.3**	**(0.3)**	**(0.1)**	**6.2**	**2.5**	**5.7**

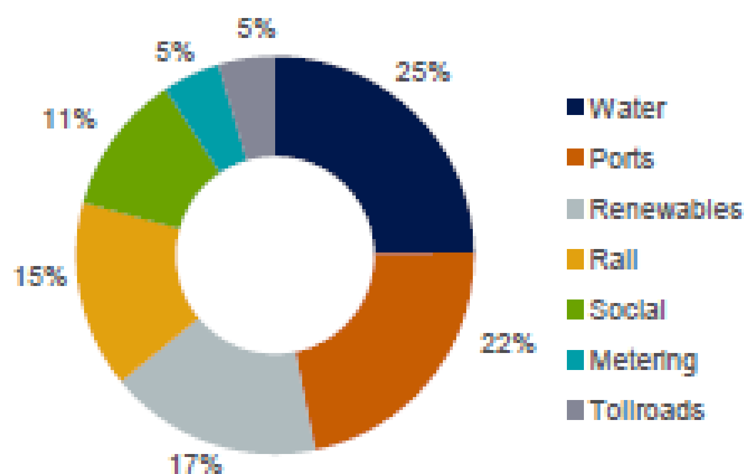
Reason for appointment

Hermes were appointed as the Fund's infrastructure manager to diversify the Fund away from index linked fixed income. The investment is in the Hermes Infrastructure Fund I (HIF I) and has a five-year investment period and a base term of 18 years. At the March 2015 Panel, Members agreed to increase the Fund's allocation to Hermes to 10%. As the investment is illiquid and valuations have to calculated, performance activity and investment activity relates to the end of September 2016 (Q2).

Q2 Key activities: On 19 July 2016 HIF I obtained a 25.6% stake in Energy Assets Group (EAG) as part of a consortium with Alinda Capital Partners. This investment increased the number of direct investments held by HIF I to nine, with two primary investments and two secondary investments. Distributions were received from Anglian Water, Fallago Rig, Braes of Doune, GSIP I and RREEF.

New investments: On 8 December 2016, National Grid plc announced the sale of 61% of National Grid Gas Distribution ('NGGD') to a consortium of UK and international infrastructure investors, including HIF I. The Transaction is subject to regulatory clearance, is expected to be completed in the first quarter of 2017, with a capital call value of £11m. HIF I will hold an 8.5% indirect ownership interest in NGGD, with the Fund acquiring a 2.9% indirect ownership interest.

Holdings at 31/09/2016: The holdings, split by asset type, are provided below:



Renewable Investments:

Audit: KPMG LLP are to replace Deloitte LLP as the Partnership's auditor.

5.8 Aberdeen Asset Management

	2016				2015				One	Two	Since
Aberdeen	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£52,362	%	%	%	%	%	%	%	%	%	%	%
Actual Return	0.5	0.3	(1.4)	2.2	(0.1)	0.4	(0.6)	1.4	1.6	1.4	2.1
Benchmark	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	4.4	4.4	3.9
Difference	**(0.6)**	**(0.8)**	**(2.5)**	**1.1**	**(1.2)**	**(0.7)**	**(1.7)**	**0.3**	**(2.8)**	**(3.0)**	**(1.8)**

Reason for appointment

As part of the Fund's diversification away from equities Members agreed to tender for a Diversified Alternatives Mandate. Aberdeen Asset Management (AAM) were appointed to build and maintain a portfolio of Hedge Funds and Private Equity. All positions held within the portfolio are hedged back to Sterling.

Market Update and Performance Summary

Inflation expectations across developed markets rose during the quarter. 10-year US treasury yields rose and the steepening move, combined with a number of better than expected earnings announcements, provided some welcome relief for the banking sector, particularly in Europe.

In the UK, the outlook for the economy in the wake of the referendum is unclear and volatility in UK related assets remains high. Confirmation that the British government would seek to formally initiate the exit procedure from the European Union early next year weighed on sterling during the month. The pound fell more than 5% versus the US dollar in October, and as of month-end is now down more than 15% year-to-date versus both the US dollar and the euro. 10-year gilt yields rose by 50 basis points in October in recognition that there is limited scope for continued monetary easing in the UK given that inflation is likely to accelerate sharply over the coming quarters.

December was for equity markets with the MSCI World Index rising over 2%. European equities experienced a strong relief rally despite Prime Minister Renzi resigning after being defeated in the Italian constitutional referendum. Italian 10 year government bond yields declined by 17 basis points and the Italian FTSE MIB index surged 14%. The broader European Stoxx 600 index also rallied strongly, finishing the month up 6%.

In the United States the Federal Reserve hiked rates by 0.25% as expected. Updated forecasts from the FOMC, however, suggested a more hawkish outlook from the committee for 2017, which led US bond yields to rise relative to other developed markets and the US dollar to strengthen versus the euro, yen, and sterling.

The yield differential between 10-year US treasuries and 10-year German bunds increased to more than 220bps in December, the widest level on record. Emerging markets, however, had mixed performance over the period. A strengthening US dollar and rising bond yields put pressure on Asian markets, with the Shanghai Composite falling close to 5%, while rising oil prices provided support for energy exporters such as Russia (MICEX Index +7%). WTI crude prices rose a further 9% in

December, continuing the positive momentum seen since OPEC reached an agreement to curb production levels.

Heading in to 2017, market expectations are high that the incoming US administration will announce a raft of measures to boost corporate profitability, including cutting taxes and rolling back regulations, but at the same time there are growing concerns that the imposition of trade tariffs may negatively impact larger multi-national companies.

As at the end of December 2016 the portfolio held the following allocation to Hedge Fund's and Private Equity:

Fund	Strategy / Style
Hedge Funds	
Field Street Fund	Fixed Income, Global Macro
Horizon Portfolio Ltd	Market Neutral
Kohinoor Series Three	Tail-risk protection
Obsidian Fund	Fixed Income Relative Value
Pharo Gaia Fund	Discretionary global macro, invests in emerging markets
Alteaus Overseas Fund	Discretionary global macro, focused on FX / commodities
Complus Asia Macro	Discretionary macro fund focused on Asia
Renaissance IDA	Statistical Arbitrage
BlackRock Fixed Income	Relative Value
Private Equity	
PAI Europe VI	Buyout Midcap
MML Capital Partners VI	Lower Mid-Market

5.9 M&G / Prudential UK

	2016				2015				One	Two	Since
M&G / Prudential	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£3,489	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.2	4.4	4.5	4.8
Benchmark Return	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	4.4	4.4	4.4
Difference	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.1**	**0.0**	**0.1**	**0.4**

Reason for appointment

This investment seeks to maximise returns using a prudent investment management approach with a target return of Libor +4% (net of fees) and provides diversification from active bond management by holding the loans until their maturity. The strategy continues to meet its objectives and there were no issues in the quarter.

The portfolio maintained its seven senior loan investments with several medium sized institutions, with no changes to their respective credit ratings. The date of the last loan maturity is 2021, after which the investment will be wound up and the final distributions made.

5.10 Pyrford

	2016				2015				One	Two	Since
Pyrford	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£80,950	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	0.6	3.1	3.2	2.4	2.2	(0.5)	(2.5)	2.8	9.3	5.6	4.4
Benchmark	2.0	1.9	2.0	1.4	1.6	1.5	1.9	1.1	7.3	6.7	6.0
Difference	**(1.4)**	**1.2**	**1.2**	**1.0**	**0.6**	**(2.0)**	**(4.4)**	**1.7**	**2.0**	**(1.1)**	**(1.6)**

Reason for appointment

Pyrford were appointed as the Fund's absolute return manager (AR) to diversify from equities. The manager's benchmark is a fixed benchmark, which means that the manager is likely to outperform the benchmark significantly during market rallies.

AR managers can be compared to equities, which have a similar return target. When compared to equities, absolute return is likely to underperform when markets increase rapidly and to outperform equities during periods when markets suffer a sharp fall. 2013 and into 2014 could be classified as a significant market rally and therefore, in comparison to equities, Pyrford have underperformed.

Performance

Pyrford generated a return of 0.6% in Q4. The Fund has delivered five positive quarters of return and finished the year with a total return of 9.3%.

Market

In the final quarter, the US election dominated the news. Donal Trump's victory sent the US stock market to a record high whilst depressing bond prices. The potential for substantial spending on infrastructure and a reduction in corporate taxes were the main drivers. The Federal Reserve increased the Fed Funds rate by 25 basis points and indicated that there may be as many as three increases in 2017. European and Asian markets were strong in local currency, with Italy, Greece and Japan leading the way.

The portfolio's allocation to bonds and equities contributed positively to Q4 returns. The portfolio's bonds performed well relative to the market, particularly in a rising yield environment, due to the short duration positioning held.

Pyrford's UK bonds were flat compared to the UK average bond index (5 to 15-year) of -3.6% and the UK long bond Index (over 15 years) of -6.0%. The portfolio's overseas bonds returned +0.9%, compared with the global bond index of -3.6%. Overseas bond returns were increased by sterling weakness against the Canadian dollar as the portfolio holds a portion of unhedged Canadian Government bonds.

Overseas equities performed well, +3.3%, aided by a weaker pound, however Pyrford's UK equities lost ground, -1.8% and underperformed the market, +3.9%. The portfolio, positioned in defensive sectors, suffered as the market reacted to rising yields by rotating out of utilities. Currency management added to returns in the final quarter as sterling strengthened against the Aussie dollar.

5.11 Newton

	2016				2015				One	Two	Since
Newton	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£55,097			**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	(5.0)	1.5	4.3	4.0	1.5	(1.3)	(2.7)	4.4	4.8	3.4	4.9
Benchmark	1.0	1.1	1.1	1.1	1.1	1.1	1.1	1.1	4.3	4.4	4.5
Difference	**(6.0)**	**0.4**	**3.2**	**2.9**	**0.4**	**(2.4)**	**(3.8)**	**3.3**	**0.5**	**(1.0)**	**0.4**

Reason for appointment

Newton was appointed as the Fund's absolute return (AR) manager to diversify away from equities. The manager has a fixed benchmark of one month LIBOR plus 4%. AR managers have a similar return compared to equity but are likely to underperform equity when markets increase rapidly and outperform equity when markets suffer a sharp fall. The years 2013 and 2014 could be classified as a significant market rally and therefore, in comparison to equities, Newton has underperformed. The Newton strategy is invested through the London CIV from 16 December 2016.

Performance

2016 proved to be yet another rollercoaster ride in financial markets. Investors started the year in a panic and appeared to end it in euphoria.

Financial Markets, post-US elections, quickly moved to a pro-growth, pro-inflation stance; bond yields have risen sharply and, in equity markets, the rotation out of consumer staples and utilities and into financials and materials that began in the late summer has accelerated significantly.

This does not suit Newton's positioning, which, is cautious and as a result the strategy returned -5.0% compared to a benchmark return of 1.0%. The Q4 underperformance was predominantly due to bond yields rising, stable equities selling off and gold also falling, which was counter to the positions held by this strategy.

A meeting was held with Newton in January 2017 to discuss the underperformance and sufficient assurance was obtained that the strategy remains a good one for the markets and for the Fund, although there would be some repositioning.

Over 2016, the Real Return Fund outperformed its benchmark return by 0.5% and since inception has outperformed its benchmark by 0.4%.

Outlook

Once again, the US-centric consensus is declaring not only that central bank policy appears to have worked for the US economy, but that it has paved the way for an improved global outlook. As a result, risk-asset prices have taken another turn upward, led this time by economically sensitive sectors. Valuations also imply that conditions will remain rosy into 2017, and beyond. Newton suggest that the geopolitical and economic uncertainties ahead do not match this view.

5.12 BNY Standish

	2016				2015				One	Two	Since
Standish	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**	**Year**	**Years**	**Start**
£64,139			**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Actual Return	0.7	1.4	0.9	(1.9)	(1.4)	(2.7)	(1.5)	3.7	1.1	(0.4)	0.4
Benchmark	1.1	1.1	1.1	1.5	1.5	1.5	1.5	1.5	4.8	5.4	5.8
Difference	**(0.4)**	**0.3**	**(0.2)**	**(3.4)**	**(2.9)**	**(4.2)**	**(3.0)**	**2.2**	**(3.7)**	**(5.8)**	**(5.4)**

Reason for appointment

Standish were appointed to achieve a 6% total return from income and capital growth by investing in a globally diversified multi-sector portfolio of transferable fixed income securities including corporate bonds, agency and governments debt.

Performance

US Treasury yields were higher in Q4. Performance across spread sectors was mostly up, except for general underperformance in the asset-backed sector. The US corporate component of the Barclay's US Aggregate (representative of investment-grade credit) was up slightly. US high-yield corporates (specifically the Barclay's US High Yield Index) posted positive performance as well. Emerging-markets hard currency posted a positive total return, as did emerging-market local currency. Conversely, performance in the securitised sector was mostly negative in December, with underperformance in asset-backed securities and commercial mortgage-backed securities and neutral performance in mortgage-backed securities.

Standish is virtually flat against Benchmark for the past 3 quarters (3% against a 3.3% benchmark). Following the significant underperformance in 2015 and Q1 of 2016, Standish still have a significant gap to close and will continue to be monitored. Since inception, Standish have now provided a positive, annualised, real return of 0.4%.

Outlook

While uncertainties about economic policy remain high, we have nudged up the outlook for global economic growth over the next two and a quarter years, mostly on improved performance in the US this year and the promise of additional fiscal impetus in 2017 from the Trump administration.

Few adjustments have been made to growth and inflation forecasts in the major developed economies, except for marking up real GDP growth in Japan. This performance in advanced economies, along with China anchoring the expansion of other emerging-market economies, should support commodity prices. We expect oil prices to trade in a narrow range.

The implications for markets are that long rates rise and the yield curve steepens, and breakevens are still inexpensive, but not as much as before. There will likely be opportunities in high-yield and emerging-market sovereigns. Mortgage-backed securities will likely come under pressure.

5.13 Currency Hedging

No new currency hedging positions were placed in Q4.

6. Consultation

6.1 Council's Pension Fund monitoring arrangements involve continuous dialogue and consultation between finance staff, external fund managers and external advisers. The Strategic Director, Finance & Investment and the Fund's Chair have been informed of the approach, data and commentary in this report.

7. Financial Implications

Implications completed by: Kathy Freeman, Director of Finance

7.1 The Council's Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. Investment decisions are taken based on a long-term investment strategy. The investment performance has a significant impact on the General Fund. Pensions and other benefits are statutorily calculated and are guaranteed. Any shortfall in the assets of the Fund compared to the potential benefits must be met by an employer's contribution.

7.2 This report updates the Panel on developments within the Investment Strategy and on scheme administration issues and provides an overview of the performance of the Pension Fund during the period.

8. Legal Implications

Implications completed by: Paul Feild, Senior Governance Solicitor

8.1 The Council operates the Local Government Pension Scheme which provides death and retirement benefits for all eligible employees of the Council and organisations which have admitted body status. There is a legal duty fiduciary to administer such funds soundly according to best principles balancing return on investment against risk and creating risk to call on the general fund in the event of deficits. With the returns of investments in Government Stock (Gilts) being very low they cannot be the primary investment. Therefore to ensure an ability to meet the liability to pay beneficiaries the pension fund is actively managed to seek out the best investments. These investments are carried out by fund managers as set out in the report working with the Council's Officers and Members.

8.2 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (SI 2009/3903) ("the 2009 Regulations") are the primary regulations that set out the investment framework for the Pension Fund. These regulations are themselves amended from time to time. The Regulations are made under section 7 of and Schedule 3 to the Superannuation Act 1972. They set out the arrangements which apply to the management and investment of funds arising in relation to a pension fund maintained under the Local Government Pension Scheme.

9. Other Implications

9.1 **Risk Management** - Investment decisions are taken based on a long-term investment strategy. Investments are diversified over several investment vehicles (equities – UK and overseas, bonds, property, infrastructure, global credit and cash) and Fund Managers to spread risk.

Performance is under constant review, with this focused on how the Fund has performed over the past three months, one year and three years.

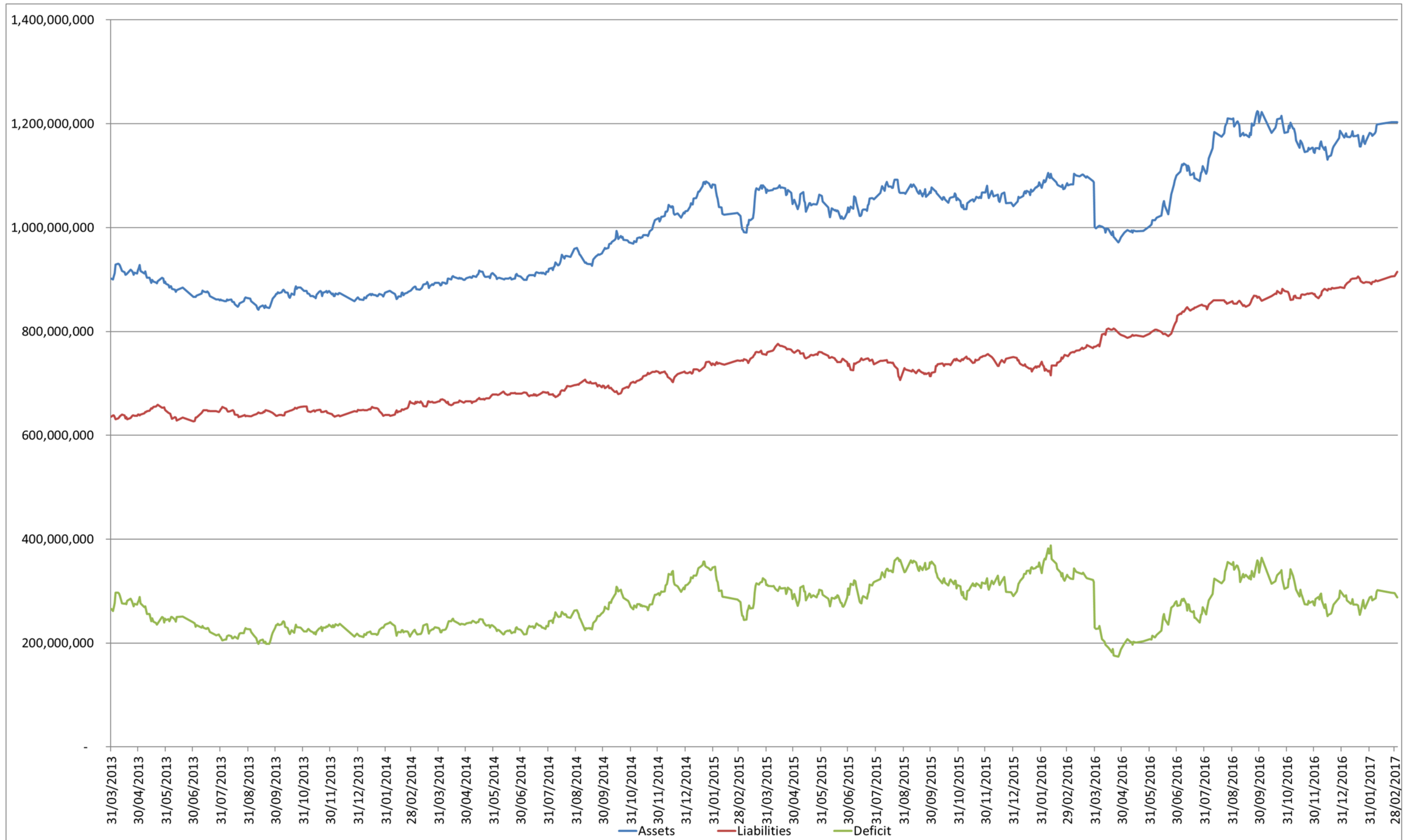
Background Papers Used in the Preparation of the Report:

- WM Quarterly Q4 2016 Report; and
- Fund Manager Q4 2016 Reports.

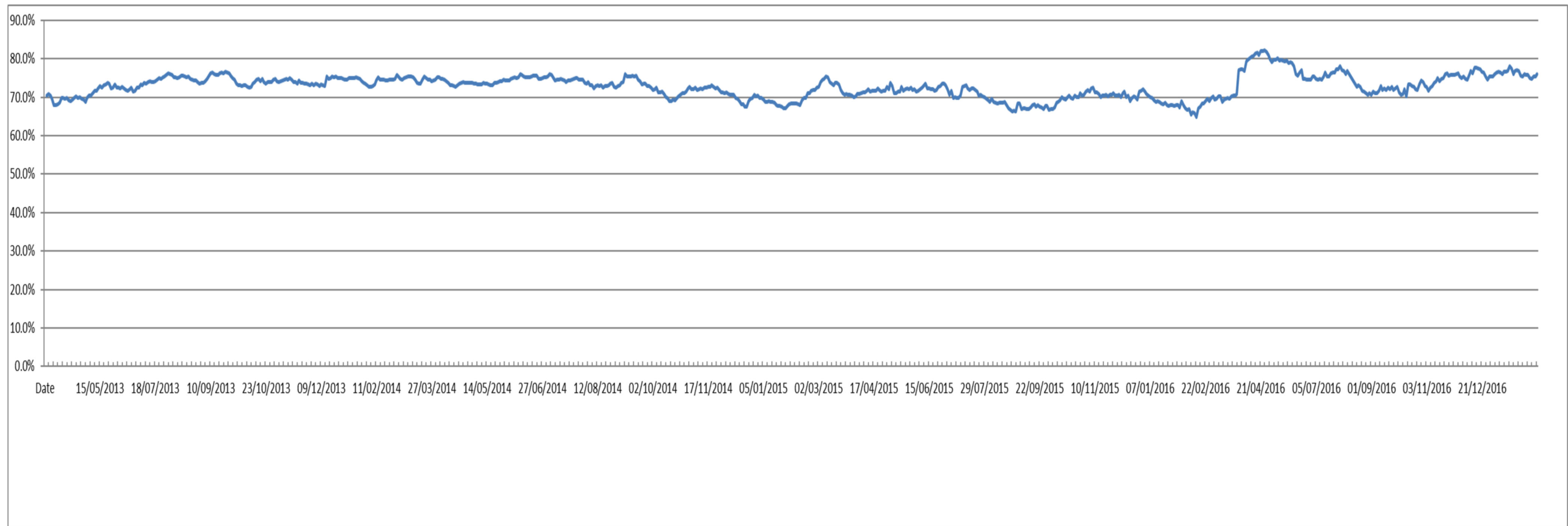
List of appendices:

Appendix 1 - Fund Asset and Liability Values 31 March 2013 to 24 February 2017
Appendix 2 - Definitions
Appendix 3 - Roles and Responsibilities

APPENDIX 1 - Fund Asset Values 31 March 2013 to 28 February 2017



Funding Level between 31 March 2013 to 28 February 2017



APPENDIX 2

A Definitions

A.1 Scheduled bodies

Scheduled bodies have an automatic right, and requirement, to be an employer in the LGPS that covers their geographical area. Therefore, scheduled bodies do not need to sign an admission agreement

Scheduled bodies are defined in the LGPS Regulations 2008 (Administration) in schedule 2, part 1. Common examples of scheduled bodies are Unitary Authorities, Police and Fire Authorities and Academies.

A.2 Admitted bodies

Admitted Bodies either become members of the LGPS as a result of a TUPE transfer, or following an application to the Fund to become an employer in the scheme. In both cases, their admission is subject to the body meeting the eligibility criteria and an admission agreement being signed by all relevant parties.

A.3 Schedule of Admitted and Scheduled bodies

A list of scheduled and Admitted Bodies is provided below

Scheduled bodies

University of East London
Magistrates Court
Barking College
Thames View Infant Academy
Thames View Junior School
Sydney Russell Academy
Riverside Academy
Riverside Bridge
Riverside Primary
Dorothy Barley Academy
Warren Academy
Goresbrook Free School
Elutec (from April 2016)

Admitted Bodies

Age UK
Abbeyfield Barking Society
Barking and Dagenham Citizen's Advice Bureau
Council for Voluntary Service
Disablement Association of Barking and Dagenham
East London E-Learning
Elevate
Kier
London Riverside
Laing O'Rourke
RM Education
CRI

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APPENDIX 3

B Roles & Responsibilities

B.1 Investment or Pensions Committee

This is the decision-making body within the LGPS scheme. It will probably meet quarterly and could have sub-committees for examining more detailed aspects i.e. investment performance, audit etc.

Membership of the committee will reflect the constitutional nature of the committee within the local authority and the multi–employer nature and size of the local scheme. A county scheme might have the leader of the council, four other councillor members from the host local authority, two district councillors and a staff representative.

As another example, the London Pension Fund Authority, which has separate legal responsibility for certain pensions' administration and investment within London, has a membership of seven to eleven members appointed by the Mayor of London. The Mayor is required to consult local government representatives in London on at least half of the appointments excluding the chairman.

Although appointments from host local authorities will be made on a political basis, a key feature of pensions or investments committees is the non-political nature of much of the decision-making. While sitting on the pensions or investments committee, members will be exercising a duty of care and have a fiduciary responsibility to the fund, employers and potential beneficiaries of the fund.

Responsibilities

The responsibility of an investments or pensions committee may include:

- ensuring all investment activity complies with the requirements of current regulations and best practise;
- approving the statement of investment principles, funding strategy statement, communications strategy and governance policy;
- reviewing and taking action on actuarial valuations;
- appointing investment managers, a fund actuary, custodian(s) and professional advisers;
- agreeing asset allocation strategies following asset liability modelling and a policy for investment in different assets with the investment managers;
- agreeing a rebalancing strategy between different portfolios when asset allocations change due to different market movements of different sectors;
- regularly reviewing investment managers' performance and expertise against agreed benchmarks and determining any action required;
- ensuring that the fund investments are sufficiently diversified and that the fund is investing in suitable investments;
- monitoring budgets for the fund ensuring there is adequate budgetary control;
- promoting the fund within the authority; and
- ensuring the administration of the fund is appropriately resourced, is effective and meets performance standards.

The committee will also have responsibility for selecting and appointing external additional voluntary contribution (AVC) providers for use by members in purchasing additional benefits. At retirement the accumulated value of the members AVC fund is used to purchase an annuity on the appropriate market, or the value may be taken as a cash sum under specific circumstances.

CLG has reminded administering authorities that elected councillors have a legal responsibility for the prudent and effective stewardship of LGPS funds, and in more general terms, have a fiduciary duty in the performance of their functions.

Under Section 101 of the Local Government Act 1972, a local authority can choose to delegate their pension investment functions to the council, a committee, a sub-committee or to officers. CLG guidance states that under the Local Authorities (Functions and Responsibilities) (England) Regulations 2000 and the Local Authorities Executive Arrangements (Functions and Responsibilities) (Wales) Regulations 2001, statutory decisions, taken under schemes made under Sections 7, 12 or 24 of the Superannuation Act 1972, are not the responsibility of the executive arrangements introduced by the Local Government Act 2000.

This means that the executive arm of the council cannot make decisions in relation to discretions to be exercised under the LGPS, or make decisions relating to the investment of the pension fund and related matters.

B.2 Quasi Trustees

As the LGPS has a different background, in comparison to corporate pension schemes, members of investments or pensions committees do not have the legal responsibilities of a trustee in a corporate scheme. Nevertheless they still have considerable responsibilities and a general duty of care. Investments or pension's committee members are often referred to as quasi trustees. Due to the complexity of investment practises, pension benefits, actuarial and funding issues, a high level of knowledge and skills is required and continual training is essential.

LGPS quasi-trustees are responsible for the:

- oversight of the management and resourcing of all fund activities;
- achieving the requirements set out by The Pensions Regulator's codes of practice;
- ensuring the best possible outcome for the fund, employers and members; and
- taking decisions in accordance with the standing orders of the investments or pensions committee.

B.3 Fund Administrator

The Strategic Director, Finance & Investment is responsible as fund administrator for:

- ensuring compliance with the statutory rules governing the investment of LGPS assets, including the various policy documents and statements required under the regulations;
- acting as a professional advisor to the fund;

- as section 151 officer alerting the investments or pensions committee or the council to any problems with the funding level or the administration of the fund in accordance with section 151 responsibilities;
- ensuring effective audit and governance arrangements; and
- ensuring the effective administration and preparation of the accounts including the annual statement of accounts.

B.4 Administering Authority

There will be a separate pension's function within a host local authority with responsibility for investment and scheme administration. With a few exceptions, it will not be a separate legally constituted body.

Consequently, subject to LGPS regulations, the legal and administrative processes of the local authority will apply to the fund i.e. employees of the fund will be employees of the local authority and be subject to the local authorities pay and conditions of employment.

Although not a separate body in law, good practice would suggest that the fund should have a title relating to the overall fund, rather than the host authority.

The responsibilities of the administering authority include:

- collecting and accounting for employer and employee contributions;
- investing monies not required for payment benefits, transfers and administration costs;
- paying pension benefits and ensuring cash is available to meet the funds future liabilities;
- managing the fund valuation process;
- preparing and maintaining the statutory statements;
- monitoring and managing all aspects of the fund's performance; and
- Managing communications with employers, members and pensioners.

B.5 Employers

These will range from the host local authority, which in a county scheme will be the county council, to many other employers, both large and small. Following out-sourcing by local authorities, an increasing feature of LGPS schemes is the extent to which commercial companies are becoming employers (as admitted bodies) within the scheme.

Employers fall into three categories:

- Scheduled

  These are the organisations listed in the Local Government Pension Scheme (Administration) Regulations 2008 (Schedule 2, Part 1) and include county councils and district councils.

- Designated (resolution) bodies

  These are employers that have the power to decide if an employee or a group of employees can belong to the LGPS and they pass a resolution accordingly. They are

listed in the Local Government Pension Scheme (Administration) Regulations 2008 (Schedule 2, Part 2).

- Admitted bodies

  These are bodies whose staff can become members of an LGPS fund, if the administering body agrees, under provisions of governing regulations by virtue of an admission agreement between the administering authority and the relevant body.

  Responsibilities of employers include:
  - deducting pension contributions and together with employer contributions, remitting to the administering authority in accordance with the required timescale;
  - exercising benefit discretions in accordance with the agreed policy and keeping the administering authority informed;
  - notifying the administering authority of all relevant membership changes (e.g. retirement etc) and other required issues; and
  - Complying with the valuation timetable.

Employers have a particular responsibility for notifying the administering authority as soon as it becomes evident that an outsourcing or external partnership arrangement might be a possibility. There are many complex issues to be considered by the administering authority which could involve seeking actuarial and financial advice. Employers need to ensure that tender documents clarify pension funding obligations which should be covered subsequently in a commercial contract.

Contact should be made at an early stage with the administering authority if consideration is being given to an employee retiring early or being made redundant. When considering early retirement, employers need to ensure that they identify the need to make a payment to the pension fund for the early release of pension benefits. This is called the pension fund strain; it can be a significant cost and normally needs to be funded immediately by the employer.

B.6 Investment Managers

With some exceptions, in larger LGPS funds most investment managers are external appointments. A feature of the LGPS is the extent to which the majority of mandates are held by a relatively few managers. In 2006 over 50 percent of LGPS funds were managed by the top five managers. In total there were over 80 different external managers involved with LGPS funds.

Investment manager responsibilities include:

- investment of pension fund assets in compliance with current LGPS legislation, any constraints set by the investments or pensions committee in the statement of investment principles and investment management agreement;
- asset allocation if a balanced manager, otherwise as directed by the investments or pensions committee;
- selection of securities within asset classes;
- attending meetings and presenting reports to the investments or pensions committee as required, including regular reports on performance, voting and transactions;
- active management of any cash balances (unless this responsibility is delegated to the custodian); and

- engaging with companies and taking shareholder action in accordance with the fund's policy.

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 contain clauses on:

- the requirements for being an investment manager;
- choice of investment manager;
- terms of appointment for an investment manager; and
- Reviewing the performance of an investment manager.

B.7 Custodian(s)

The custodian(s) is responsible for the safekeeping of the fund's securities. This function may be carried out by a custodian appointed directly by the fund, or via appointed fund managers. Current best practice is for funds to appoint their own custodian(s).

The duties may include:

- settlement of purchases and sales;
- advising managers of cash available for investment;
- safe custody of securities and cash;
- acting as banker to the fund;
- cash reconciliations;
- collection of dividends, income and overseas tax reclaims;
- ensuring correct actions including rights issues, bonus issues and acquisitions are correctly dealt with;
- ensuring the necessary approvals are in place to invest in certain overseas markets; and
- Providing (monthly) valuations of scheme assets, details of all transactions and accounting reports.

The custodian may also offer access to commission recapture, security lending programmes, comparative performance measurement and voting of shares in accordance with an agreed policy.

The appointment of a custodian might require specialist advice to be obtained. The risks to be addressed include:

- financial risk around the financial viability and stability of the custodian including ability to support long term investment in the business and withstand operational losses;
- asset risk including risk that in the event of default, client securities are treated as part of the assets of the bank which has gone into default and belong to creditors rather than clients, and cash risk that in the event of default clients are exposed to losses of cash placed with the bank; and
- Asset servicing risk such that a client is exposed to a loss due to a weakness in the custodian's operations.

Funds need to consider the importance of ensuring that all these areas are considered. This might involve using specialist advisers. Particular consideration should be given to risks if a sub-custodian is involved.

B.8 Actuary

The scheme actuary is an independent and appropriately qualified adviser who carries out statutorily required fund valuations and other valuations as required and who will also provide general actuarial advice.

The actuary will:

- prepare fund valuations, including setting employers contribution rates, after agreeing valuation assumptions with the administering authority;
- agree a timetable for the valuation with the administering authority; and
- Prepare timely advice and calculations in connection with bulk transfers and benefit matters.

The results of the valuation determine the rate of the employer's contribution for the subsequent three years. The actuary is required to certify employer's contribution rates that will achieve full solvency over the longer term, while keeping contribution rules as stable as possible.

The contribution rate will consist of a common rate for the fund and an individual employer rate. To achieve this, the actuary needs to ensure compliance with legislative requirements, assess current solvency levels, monitor actual experience compared with previous assumptions, and assess reserves needed for accrued liabilities. In carrying out this work, the actuary must have regard to the funding strategy statement, which might need to be revised to incorporate any new approach to be followed in the valuation.

The administering authority may also instruct the actuary to carry out an interim valuation if stock market conditions change, or if the characteristics of the membership changes e.g. as a result of a large transfer of staff.

The actuary will advise on other scheme matters, e.g. funding levels and the funding strategy statement and asset liability reviews. The most recent valuation of LGPS funds in England and Wales was at 31 March 2013 with revised employer contribution rates payable from April 2014.

The Myner's report (Institutional Investment in the United Kingdom: A Review) highlighted the need for funds to consider whether the roles of actuary and investment adviser should be held by separate companies. Notwithstanding this, many continue to have these roles provided by the same company, although there will be separate contracts.

B.9 Professional Advisers

Professional advisers should be appointed to advise the pensions or investments committee and the fund administrator on scheme matters. As in the case of investment managers, these appointments tend to be held by a relatively few appointees. Professional advisors should not be committee members.

Funds usually have a sole investment adviser. Consideration might be given to using a framework list of consultants, in order to use specific advisers to reflect each firm's strength and fees. In comparison with the usual approach of advertising in the EU journal, subject to the size of the fee, framework lists afford much more flexibility in procuring these services.

Advisers may be needed for advice on:

- asset allocation strategies;
- the selection of new managers and custodians;
- the preparation of the various strategy documents required under LGPS regulations; and
- To assist in reviewing and monitoring managers' performance.

Legal advice will need to be available to the fund, which might involve the appointment of specialist legal advisers for particular aspects of fund management i.e. appointing a private equity manager.

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PENSIONS PANEL

15 March 2017

Title: Administration and Governance Report	
Report of the Chief Operating Officer	
Public Report	**For Information**
Wards Affected: None	**Key Decision:** No
Report Author: David Dickinson, Group Manager Pensions and Treasury	**Contact Details:** Tel: 020 8227 2722 E-mail: david.dickinson@lbbd.gov.uk
Accountable Director: Kathy Freeman, Director of Finance	
Accountable Strategic Director: Claire Symonds, Chief Operating Officer	

Recommendations

The Panel is recommended to note:

i. that the Fund is cash flow positive;
ii. the Fund's three-year budget for the period 1 April 2016 to 31 March 2019;
iii. the Fund's 2016/17 cash flow is forecast to be significantly higher than the budgeted cash flow, predominantly due to investment returns;
iv. that as part of the Council's transformation process, several arms lengths service delivery units (Delivery Unit) will be agreed over the coming year, with a full report to be presented to the June 2017 Panel;
v. the update on the LGPS reforms; and
vi. the Fund has to pay £25k (+ VAT) as a service change and £75k (+VAT) development funding charge to the London CIV in April 2017.

1. Introduction

1.1 It is best practice for Members to receive regular administration data and governance updates. Administration data includes cash flow, member numbers, governance and consultations. This paper covers three main areas including:

i. Pension Fund Budget 1 April 2017 to 31 March 2020;
ii. Cash flow to 31 January 2017; and

2. Pension Fund Budget 1 April 2017 to 31 March 2020

2.1 Table 1 provides Members with the Fund's three-year budget to 31 March 2020. The revised forecast for 2016/17 is included for comparison.

Table 1: Pension Fund Budget 1 April 2017 to 31 March 2020

Contributions	2016/17	2017/18	2018/19	2019/20
Employee Contributions				
Council	6,700	6,000	5,500	5,000
Admitted bodies	400	800	1,200	1,500
Scheduled bodies	2,300	2,400	2,500	2,800
Employer Contributions				
Council	24,500	22,500	20,000	18,200
Admitted bodies	1,000	2,000	3,000	3,750
Scheduled bodies	8,500	8,900	9,300	10,500
Pension Strain	3,000	1,000	1,000	1,000
Transfers In	2,500	2,500	2,500	2,500
Total Member Income	48,900	46,100	45,000	45,250
Expenditure				
Pensions	- 29,000	- 30,000	- 31,000	- 32,000
Lump Sums and Death Grants	- 10,000	- 6,000	- 6,000	- 6,000
Payments to and on account of leavers	- 3,500	- 3,500	- 3,500	- 3,500
Administrative expenses	- 600	- 550	- 550	- 500
Total Expenditure on members	- 43,100	- 40,050	- 41,050	- 42,000
Net additions for dealings with members	5,800	6,050	3,950	3,250
Returns on Investments				
Investment Income	5,000	6,000	7,000	7,500
Profit (losses)	115,000	35,000	35,000	35,000
Investment management expenses	- 3,500	- 3,300	- 3,100	- 3,000
Net returns on investments	**116,500**	**37,700**	**38,900**	**39,500**
Net increase (decrease) in the net assets	**122,300**	**43,750**	**42,850**	**42,750**
Asset Values	**895,000**	**938,750**	**981,600**	**1,024,350**

2.2 The cash flow forecast shows a movement from members being directly employed by the Council to some members being funded by admitted bodies and academies.

2.3 A significant increase in lump sum payments has been projected but this will be mitigated by an increase in pension strain contributions. Pension strain costs reflect the payment of early retirements over a 5-year period rather than as a one off lump sum payment.

2.4 Overall the Fund is expected to remain cash flow positive for the duration of the three years but for the net dealing with members to reduce to £3.25m by 2020. Fund manager fees are forecast to drop from £3.5m to £3.0m by 2020 as a result of savings obtained from pooling investments via the London CIV.

3. Cash flow to 31 January 2017

3.1 Table 2 below provides Members with the Fund's Cash flow to 31 January 2017.

Table 2: 2016/17 Forecast Pension Fund Cash Flow

	2016/17 Budget £000's	2016/17 Forecast £000's	Over / Under £000's
Contributions			
Employee Contributions			
Council	6,700	6,803	103
Admitted bodies	400	330	(70)
Scheduled bodies	2,300	2,611	311
Employer Contributions			
Council	24,500	24,905	405
Admitted bodies	1,000	944	(56)
Scheduled bodies	8,500	9,421	921
Pension Strain	3,000	1,000	(2,000)
Transfers In	2,500	4,323	1,823
Total Member Income	**48,900**	**50,336**	**1,436**
Expenditure			
Pensions	(29,000)	(29,723)	(723)
Lump Sums and Death Grants	(10,000)	(11,525)	(1,525)
Payments to and on account of leavers	(3,500)	(2,500)	1,000
Administrative expenses	(600)	(690)	(90)
Total Expenditure on members	**(43,100)**	**(44,438)**	**(1,338)**
Net additions for dealings with members	**5,800**	**5,898**	**98**
Returns on Investments			
Investment Income	5,000	6,000	1,000
Profit (losses)	35,000	110,000	75,000
Investment management expenses	(3,500)	(3,000)	500
Net returns on investments	36,500	113,000	76,500
Net increase (decrease) in the net assets	**42,300**	**118,898**	**76,598**
Asset Values	**814,597**	**891,195**	
Liabilities	**(1,100,000)**	**(1,135,000)**	
Funding Level	**74.1%**	**78.5%**	

3.2 Contributions, including transfers in and pension strain are expected to end the year £1.4m higher than the budget, with expenditure £1.3m lower than budgeted. The net additions for dealing with members are forecast to end the year £0.1m lower than budgeted. The decrease in income is due to pension strain being paid over a five-year period rather than a one-off lump sum payment. The increase in cost is predominantly due to the significant lump sum payments being made as part of the voluntary redundancy scheme implemented by the Council and Elevate.

3.3 Fund management fees are forecast to be £3.0m, which is lower than the budget due to savings made by investing through the London CIV. These savings are summarised in Appendix 1 of this report but at a summary level this saving equates to £127k for 2016/17 and £232.4k for 2017/18.

3.4 Administration costs are forecast to be £90k higher than budget as a programme of converting paper files to electronic records is completed.

3.5 Both returns and liabilities are forecast to be higher, with the returns better due to fund manager performance and the weakening of Sterling against all major currencies. Liabilities are higher due to a decrease in gilt yields.

3.6 Overall the Fund is forecast to end the financial year at around 78.5% funded based on a prudent gilt plus model. This compares favourably with the triennial valuation results where the fund is 77.6% funded.

4. Pension Options for Arms Lengths Service Delivery Units

4.1 As part of the Council's transformation process, several arms lengths service delivery units (Delivery Unit) will be agreed over the coming year. The setting up of each Delivery Unit will require the TUPE (Transfer of Undertakings - Protection of Employment) transfer of staff and as a result each Delivery Unit will need to be admitted as a separate employer to the Fund.

4.2 The Council is looking to create several different service delivery vehicles including, transferring its Leisure Services and establishing a company, Be First, to manage the implementation of its investment and regeneration strategy. In addition, a number of Traded Services will be set up.

4.3 Currently the Council is reviewing several options available to it under the Fund's Admissions Policy and these will be reported back for Panel agreement in June 2017.

5. LGPS reform update

5.1 On 2 February a Special Panel meeting was held to discuss the response to the government's criteria for the reform of LGPS investments. The release of the criteria for collaborative investment across the LGPS follows months of discussion and debate about how to pool the LGPS investments into six pools of around £25bn.

5.2 At the Special Panel Meeting Members received a presentation from the London CIV's Chief Executive and Chief Investment Officer.

5.3 On 15 July 2016 a proposal was submitted by the London CIV detailing plans at both an individual and collective level, with the Fund's submission included as one of the appendices.

5.4 On 12 December 2016 the London CIV met with the MP Marcus Jones, to discuss the submission. Overall the response was positive but there was an emphasis on ensuring the speed of the transfer of assets into the pool was increased and that the deadline for pools to become operational remained April 2018.

5.5 As outlined in table 3 below, as at 31 December 2016 the Fund has three investments with the pool, totalling nearly a third of assets. A further 21.2% of the Fund's holdings are also in exempt Life Funds (passive investments). Of the remaining 46% that still potentially could be invested in the London CIV, only 15.1% will be difficult to transfer. The timing of investing the other 31% will be dependent on the London CIV providing suitable alternatives.

Table 3: Fund Holdings at 31 December 2016 split by access to the London CIV

Fund Manager	Mandate	Value at 31/12/2016 £000s	Value at 31/12/2016 £000s
Invested in the London CIV			
Baillie Gifford	Global Equities	153,011	Invested via the London CIV
Newton	Absolute Return	55,097	Invested via the London CIV
Pyrford	Absolute Return	80,950	Invested via the London CIV
London CIV	Equity	150	
	Total	**289,208**	**32.8%**
Life Funds			
UBS Bonds	Passive Bonds	35,305	Life Fund's Exempt from Pooling
UBS Equities	Passive Equities	151,542	Life Fund's Exempt from Pooling
	Total	**186,847**	**21.2%**
No Option provided by London CIV			
BlackRock	Property	39,840	London CIV asked to include in Pool
Kempen	Global Equities	146,391	Discussion with London CIV
Schroders	Property	23,039	No Option Provided by London CIV
Standish	Global Credit	64,139	No Option Provided by London CIV
	Total	**273,409**	**31.0%**
Illiquid / Cash – unlikely to be transferred to London CIV			
M&G	Senior Loans	3,489	Alternative, no other Option available
Hermes GPE	Infrastructure	64,252	Alternative, no other Option available
Aberdeen	Alternatives	52,362	Alternative, no other Option available
	Cash	12,691	
	Total	**132,794**	**15.1%**
Total Fund		882,258	882,258

6. London Collective Investment Vehicle Budget Requirements

6.1 On 8 February 2017 the Joint Committee agreed the 2017/18 London CIV budget. As a result, the Fund has to pay £25k (+ VAT) as a service change and £75k (+VAT) development funding charge. This charge will significantly reduce the savings the Fund is expected to make from the reduced Fund manager fees it is paying.

6.2 There is an expectation that these costs will reduce over time and will be replaced by a service charge on the assets invested through the CIV but this is unlikely to happen before 2020.

7. Consultation

7.1 Council's Pension Fund governance arrangements involve continuous dialogue and consultation between finance staff and external advisers.

The Strategic Director, Finance & Investment and the Fund's Chair have been informed of the commentary in this report.

8. Financial Implications

Implications completed by: Kathy Freeman, Director of Finance

8.1 The Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. The management of the administration of benefits and governance of the Fund rests with the Pension Panel.

9. Legal Implications

Implications completed by: Paul Feild Senior Governance Solicitor

9.1 The Council operates the Local Government Pension Scheme which provides death and retirement benefits for all eligible employees of the Council and organisations which have admitted body status. There is a legal duty fiduciary to administer such funds soundly according to best principles balancing return on investment against risk and creating risk to call on the general fund in the event of deficits. With the returns of investments in Government Stock (Gilts) being very low they cannot be the primary investment. Therefore, to ensure an ability to meet the liability to pay beneficiaries the pension fund is actively managed to seek out the best investments. These investments are carried out by fund managers as set out in the report working with the Council's Officers and Members.

10. Other Implications

10.1 There are no other immediate implications arising from this report though the Public Service Pensions Act changes will have an impact on the short and long term workload of the Pension Fund. This will continue to be monitored.

Background Papers Used in the Preparation of the Report: None

List of appendices: None

PENSIONS PANEL

15 March 2017

Title: Business Plan Update 2017	
Report of the Chief Operating Officer	
Public Report	Public Report
Wards Affected: None	**Wards Affected:** None
Report Author: David Dickinson, Group Manager Pensions and Treasury	**Report Author:** David Dickinson, Group Manager Pensions and Treasury
Accountable Director: Kathy Freeman, Director of Finance	
Accountable Strategic Director: Claire Symonds, Chief Operating Officer	
Recommendations The Panel is asked to note progress on the delivery of the 2017 Business Plan at Appendix 1 to the report	

1. Introduction and Background

1.1 The purpose of this report is to update the Pension Panel on progress regarding the Pension Fund's 2017 business plan.

1.2 Appendix 1 provides a summary of the Business Plan actions from 1 January 2017 to 28 February 2017 and the actions for the remainder of the year.

2. Comments of the Finance Officer

2.1 Regulation 59 of the Local Government Pension Scheme Regulations 2013 sets out the framework to produce a Pensions Administration Strategy which would include business planning.

2.2 The Business Plan includes the major milestones and issues to be considered by the Panel and includes financial estimates for the investment and administration of the fund and appropriate provision for training.

2.3 The key actions, the date they were completed and by whom are summarised in the Business Plan Update report.

3. Comments of the Legal Officer

3.1 The Panel has been constituted by the Council to perform the role of administering authority to manage the Fund and as such has legal authority to make the decisions sought by the recommendations. Panel Members have a legal responsibility for the prudent and effective stewardship of LGPS funds, and in more general terms, have a fiduciary duty in the performance of their functions.

List of appendices:

Appendix 1 - Business Plan Update

Appendix 1: 2017 Business Plan

Month	Action Scheduled	By	Actual Activity
Jan 17	Review: Actuarial Contract	Officers	Contract reviewed. Will tender as part of the national framework.
	Fund Manager Meetings: • Equities: Kempen • Equities: BlackRock • Equities & Bonds: UBS • Infrastructure	Officers	 2 February 2017 26 January 2017 Moved to March 6 January 2017
	Training: Strategy Development (Aon / In-house)	Officers / Advisors	Moved to 13 March 2017
Feb 17	Pension Board Meeting	Officers / Pension Board	Done – 27 February 2017
Mar 17	IAS 19 Calculations	Officers	To be completed by the end of April 2017
	Review: Independent Advisor	Officers / Members	Contract Recommendation to extend for one year
	Quarterly Pension Panel Meeting	Officers / Advisors / Members	This Panel
	Cash Flow Update (Report to March Pension Panel)	Officers	This Panel
	Fund Manager Meetings: • Absolute Return: Pyrford and Newton • Global Credit: BNY Standish • Diversified Alternatives: Aberdeen • Equities: Baillie Gifford • Equities: UBS	Officers	
	Closure of Accounts	Officers	
Apr 17	Framework Tender for Custodian (Report to June Panel)	Officers / Members	
	Provide Triennial Valuation data to the Actuary	Officers	
	Fund Manager Meetings: • Infrastructure: Hermes Property Manager: BlackRock	Officers / Advisors	
May 17	Draft Annual report and annual accounts to June Panel	Officers	
	• Quarterly Pension Panel Meeting	Officers / Advisors / Members	
	Cash Flow Update- Report to September Pension Panel	Officers	
Jun 17	Pension Board Meeting	Officers / Pension Board	
	FRS17 Data Collection – UEL and Barking College	Officers	
Jul 17	Fund Manager Meetings:	Officers	

	• Property Manager: Schroders • Equities: Kempen • Equities: Baillie Gifford Equities & Bonds: UBS		
	Annual Benefit Statement (deadline of 31 August 2017)	Officers	
	• FRS17 Data Collection – Academies	Officers	
Aug 17	Provisional Triennial Valuation results available	Officers	
	Fund Manager Meetings: • Absolute Return: Pyrford and Newton • Global Credit: BNY Standish Diversified Alternatives: Aberdeen	Officers	
Sep 17	Quarterly Pension Panel Meeting	Officers / Members	
	• Fund Expenses Review (Report to December Panel)	Officers	
	Auto-enrolment	Officers / Members	
Oct 17	Meeting with Employers to discuss Triennial Results	Officers / Employers	
	Review Risk Register - Report to December Panel	Officers	
	Cash Flow Update- Report to December Pension Panel	Officers	
	Pension Fund Stakeholder Meeting	Officers / Members	
Nov 17	Quarterly Pension Panel Meeting	Officers / Members	
	Strategic Asset Allocation Review	All	
Dec 17			

PENSION PANEL

15 March 2017

Title: Draft Funding Strategy Statement and Investment Strategy Statement	
Report of the Chief Operating Officer	
Public Report	**For Information**
Wards Affected: None	**Key Decision:** No
Report Author: David Dickinson, Group Manager Pensions and Treasury	**Contact Details:** Tel: 020 8227 2722 E-mail: david.dickinson@lbbd.gov.uk
Accountable Director: Kathy Freeman, Director of Finance	
Accountable Strategic Director: Claire Symonds, Chief Operating Officer	

Summary:

The Pension Panel is required to agree the aims and objectives outlined within the Pension Fund's Governance and Investment strategies. Following the triennial valuation two key strategy documents need to be reviewed and updated. These documents are the Funding Strategy Statement (FSS) and Investment Strategy Statement (ISS). These documents outline the Fund's funding and investment strategy and have been updated to meet statutory requirements and guidance from the DCLG and the Scheme Advisory Board.

Both documents are summarised in this report, with the draft Statements included as appendices to this report. Both report have been reviewed and agreed by the Pension Board as part of its review of decision making within the Fund.

The Panel is recommended to agree:

i. the draft Funding Strategy; and
ii. the draft Investment Strategy Statement.

The Panel is recommended to note:

iii. that these final actuarial valuation results, along with the Rates and Adjustments Certificate will be provided by the actuary by 31 March 2017.

1. Introduction and Background

1.1 London Borough of Barking and Dagenham (the Council) is the statutory administering authority for the Local Government Pension Scheme (LGPS) through the London Borough of Barking and Dagenham Pension Fund (the Fund).

1.2 As Administering Authority, the Council has delegated responsibility for the administration of the Fund to the Section 151 officer, advised by the Pension Panel and after taking expert advice from the Fund's Investment Advisor (Aon Hewitt) and the Fund's Independent Advisor, John Raisin.

1.3 Every three years the Fund is required to carry out a full valuation of its liabilities, which is completed by the Fund's actuary, with results agreed by the Administering Authority and reported to the Pension Panel.

1.4 The latest Triennial Valuation was completed in 2016, with officers agreeing the valuation assumptions with the actuary, including the deficit contributions rate, the discount rate and salary increase assumptions. The results of the valuation show that, at a whole Fund level, the deficit reduced from £266m to £228m and the funding level improved to 77.2% from the 2013 level of 70.6%.

1.5 Overall the Fund has adopted a prudent discount rate of 4.1%. This is lower than the 4.7% used in the 2013 valuation. The deficit recovery period has reduced from 20 years to 17 years and this reflects improvements within the performance of the Fund.

1.6 Prior to agreeing the final Triennial Valuation Results, a consultation process needs to be followed. As part of this process a meeting was held on the 17th November 2016 with the actuary and the Fund's various employers to discuss the draft Triennial Results. Representatives from the University of East London, Barking College and a representative for many of the Fund's academies were present.

1.7 Draft results were sent to employers in January 2017 for agreement, with the final Triennial Valuation to be agreed by March 2017 when the actuary provides the final Rates and Adjustments Certificate.

2. Funding Strategy Statement (FSS)

2.1 After the triennial valuation is completed the FSS must be updated. The purpose of the FSS, as stated by the Department for Communities and Local Government (DCLG) is:

- *"to establish a **clear and transparent fund-specific strategy** which will identify how employers' pension liabilities are best met going forward;*
- *to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and*
- *to take a **prudent longer-term view** of funding those liabilities."*

2.2 These objectives are desirable individually, but may be mutually conflicting. Whilst the position of individual employers must be reflected in the statement, it must remain a single strategy for the Administering Authority to implement and maintain.

2.3 This statement sets out how the Administering Authority has balanced the conflicting aims of affordability of contributions, transparency of processes, stability of employers' contributions, and prudence in the funding basis.

2.4 The objectives of the Fund's funding policy are as follows:

i) to ensure the long-term solvency of the Fund and the long-term solvency of shares of the Fund attributable to individual employers;

ii) to ensure sufficient funds are available to meet all benefits as they fall due;

iii) not to restrain unnecessarily the investment strategy of the Fund so that the Administering Authority can seek to maximise investment returns (and hence minimise the cost of the benefits) for an appropriate level of risk;

iv) to help employers recognise and manage pension liabilities as they accrue;

v) to minimise the degree of short-term change in the level of each employer's contributions where the Administering Authority considers it reasonable to do so;

vi) to address the different characteristics of the disparate employers or groups of employers to the extent that this is practical and cost-effective; and

vii) to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

2.5 The actuary and officers have produced a draft FSS, which is included as appendix 1 of this report. This was distributed to all Fund employers and was taken to the Pension Board for comments.

2.6 All proposed amendments have been made to the FSS and therefore, subject to any amendments put forward by Panel Members, the report in Appendix 1 is included for agreement by Pension Panel Members.

3. Investment Strategy Statement (ISS)

3.1 The FSS and the ISS are inextricably linked, with the administering authority setting the strategy, after taking advice. The ISS must comply with regulatory requirements specified in The LGPS Regulations 2012.

3.2 The ISS replaces the Statement of Investment Principles and, although it is a similar document, there are several additional disclosures that need to be covered including:

- The removal of the investment restrictions contained in schedule 1;
- Fund's approach to pooling investments, including collective investment vehicles (CIVs) and shared services;
- How social, environmental and corporate governance considerations are considered in the selection, non-selection, retention and realisation of investments; and
- The Fund's assessment of the suitability of all major asset classes.

3.3 Aon Hewitt, in consultation with officers, the actuary and the Independent Investment Advisor, has completed an Investment Strategy review. A training session is scheduled to be held on 13 March 2017 for the Advisors and officers to go through the recommendations of the strategy review with Members as part of Member training.

3.4 The draft ISS is included with this report for agreement, subject to any changes agreed as part of the Investment training session and Members recommendations. The Strategy Review will be covered as part of the private

3.5 The regulations around what needs to be included in the ISS is included in a report from the Independent Advisor as Appendix 3 of this report.

4. Consultation

4.1 Council's Pension Fund strategy development involves continuous dialogue and consultation between finance staff and external advisers. For the FSS there is a 30-day consultation with all Fund employers. The consultation process for this FSS is:

i. A draft version of the FSS issued to all participating employers on 18 January 2017 for comment;
ii. Comments requested within 30 days (by 17 February 2017);

The Chief Operating Officer and the Pension Panel's Chair have been informed of the commentary in this report.

5. Financial Implications

Implications completed by: Kathy Freeman, Director of Finance

5.1 The Fund is a statutory requirement to provide a defined benefit pension to scheme members. The Pension Panel's role agreeing and monitoring the Fund's Governance and Administration strategies. This paper forms part of the reviewing process.

6. Other Implications

6.1 There are no other immediate implications arising from this report.

Background Papers Used in the Preparation of the Report:

- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009;
- The London Borough of Barking and Dagenham Annual Report 2015/16; and
- The London Borough of Barking and Dagenham Business Plan 2017.

List of appendices:

- Appendix 1 – draft Funding Strategy Statement
- Appendix 2 – draft Investment Strategy Statement
- Appendix 3 - Investment Strategy Statement Regulatory Requirements

London Borough of Barking and Dagenham Pension Fund

Funding Strategy Statement (draft) 2017 to 2018

DRAFT Funding Strategy Statement PAGE

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1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the London Borough of Barking and Dagenham Pension Fund ("the Fund"), which is administered by the London Borough of Barking and Dagenham, ("the Administering Authority"). It has been prepared by the Administering Authority in collaboration with the Fund's actuary, Hymans Robertson LLP, and after consultation with the Fund's employers and advisers. It is effective from 1 April 2017.

1.2 What is the London Borough of Barking and Dagenham Pension Fund?

The Fund is part of the national Local Government Pension Scheme (LGPS). The LGPS was set up by the UK Government to provide retirement and death benefits for local government employees, and those employed in similar or related bodies, across the whole of the UK. The Administering Authority runs the Fund to make sure it:

- receives the proper amount of contributions and any transfer payments;
- invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth; and
- uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives), and to their dependants (as and when members die), as defined in the LGPS Regulations. Assets are also used to pay transfer values and administration costs.

1.3 Why does the Fund need a Funding Strategy Statement?

Employees' benefits are guaranteed by the LGPS Regulations, and do not change with market values or employer contributions. Investment returns will help pay for some of the benefits, but probably not all, and certainly with no guarantee. Employees' contributions are fixed in those Regulations also, at a level which covers only part of the cost of the benefits.

Therefore, employers need to pay the balance of the cost of delivering the benefits to members and their dependants.

The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers pay for their own liabilities. This statement sets out how the Administering Authority has balanced the conflicting aims of:

- affordability of employer contributions;
- transparency of processes;
- stability of employers' contributions; and
- prudence in the funding basis.

The roles and responsibilities of the key parties involved in the management of the Fund are summarised in Appendix B.

The FSS is a summary of the Fund's approach to funding its liabilities, and this includes reference to the Fund's other policies; it is not an exhaustive statement of policy on all issues.

The FSS forms part of a framework which includes:

- the LGPS Regulations;
- the Rates and Adjustments Certificate (confirming employer contribution rates for the next three years) which can be found in an appendix to the formal valuation report;
- the Fund's policies on admissions, cessations and bulk transfers;
- actuarial factors for valuing individual transfers, early retirement costs and the costs of buying added service; and
- the Fund's Investment Strategy Statement (see Section 4)

1.4 How does the Fund and this FSS affect me?

This depends on who you are:

- a member of the Fund, i.e. a current or former employee, or a dependant: the Fund needs to be sure it is collecting and holding enough money so that benefits are always paid in full;

- an employer in the Fund (or which is considering joining the Fund): you will want to know how your contributions are calculated from time to time, that these are fair by comparison to other employers in the Fund, and in what circumstances you might need to pay more. Note that the FSS applies to all employers participating in the Fund;

- an Elected Member whose council participates in the Fund: you will want to be sure that the council balances the need to hold prudent reserves for members' retirement and death benefits, with the other competing demands for council money; and

- a Council Tax payer: your council seeks to strike the balance above, and also to minimise cross-subsidies between different generations of taxpayers.

1.5 What does the FSS aim to do?

The FSS sets out the objectives of the Fund's funding strategy, such as:

- to ensure the long-term solvency of the Fund, using a prudent long term view to ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due;

- to ensure that employer contribution rates are reasonably stable where appropriate;

- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (**NB** this will also minimise the costs to be borne by Council Tax payers);

- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and

- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

1.6 How do I find my way around this document?

In Section 2 there is a brief introduction to some of the main principles behind funding, i.e. deciding how much an employer should contribute to the Fund from time to time.

In Section 3 we outline how the Fund calculates the contributions payable by different employers in different situations.

In Section 4 we show how the funding strategy is linked with the Fund's investment strategy. In the Appendices we cover various issues in more detail if you are interested:

A. the regulatory background, including how and when the FSS is reviewed;
B. who is responsible for what;
C. what issues the Fund needs to monitor, and how it manages its risks;
D. some more details about the actuarial calculations required;
E. the assumptions which the Fund actuary currently makes about the future; and
F. a glossary explaining the technical terms occasionally used here.

If you have any other queries please contact David Dickinson, Group Manager – Treasury and Pensions in the first instance at e-mail address david.dickinson@lbbd.gov.uk or on telephone number 0208 227 2722.

2 Basic Funding issues

(More detailed and extensive descriptions are given in Appendix D).

2.1 How does the actuary measure the required contribution rate?

This is a three-step process:

1. Calculate the ultimate funding target for that employer, i.e. the ideal amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix E for more details of what assumptions we make to determine that funding target;

2. Determine the time horizon over which the employer should aim to achieve that funding target. See the table in 3.3 and Note (c) for more details;

3. Calculate the employer contribution rate such that it has at least a given probability of achieving that funding target over that time horizon, allowing for different likelihoods of various possible economic outcomes over that time horizon. See 2.3 below, and the table in 3.3 Note (e) for more details.

2.2 What is each employer's contribution rate?

This is described in more detail in Appendix D. Employer contributions are normally made up of two elements:

a) the estimated cost of benefits being built up each year, after deducting the members' own contributions and including administration expenses. This is referred to as the "*Primary rate*", and is expressed as a percentage of members' pensionable pay; plus

b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "*Secondary rate*". In broad terms, payment of the Secondary rate will aim to return the employer to full funding over an appropriate period (the "time horizon"). The Secondary rate may be expressed as a percentage of pay and/or a monetary amount in each year.

The rates for all employers are shown in the Fund's Rates and Adjustments Certificate, which forms part of the formal Actuarial Valuation Report and can also be found in Appendix G. Employers' contributions are expressed as minima, with employers able to pay contributions at a higher rate. Account of any higher rate will be taken by the Fund actuary at subsequent valuations, i.e. will be reflected as a credit when next calculating the employer's contributions.

2.3 What different types of employer participate in the Fund?

Historically the LGPS was intended for local authority employees only. However, over the years, with the diversification and changes to delivery of local services, many more types and numbers of employers now participate. There are currently more employers in the Fund than ever before, a significant part of this being due to new academies.

Participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst most members will be local authority employees (and ex-

employees), most participating employers are those providing services in place of (or alongside) local authority services: academies, contractors, housing associations etc.

The LGPS Regulations define various types of employer as follows:

Scheduled bodies - councils, and other specified employers such as academies and further education establishments. These must provide access to the LGPS in respect of their employees who are not eligible to join another public-sector scheme (i.e. Teachers Scheme). These employers are so-called because they are specified in a schedule to the LGPS Regs.

It is now possible for Local Education Authority schools to convert to academy status, and for other forms of school (such as Free Schools) to be established under the academies legislation. All such **academies (or Multi Academy Trusts)**, as employers of non-teaching staff, become separate new employers in the Fund. As academies are defined in the LGPS Regulations as “Scheduled Bodies”, the Administering Authority has no discretion over whether to admit them to the Fund, and the academy has no discretion whether to continue to allow its non-teaching staff to join the Fund. There has also been guidance issued by the DCLG regarding the terms of academies’ membership in LGPS Funds.

Designating employers - employers such as town and parish councils can participate in the LGPS via resolution (and the Fund cannot refuse them entry where the resolution is passed). These employers can designate which of their employees are eligible to join the scheme.

Other employers are able to participate in the Fund via an admission agreement, and are referred to as ‘admission bodies’. These employers are generally those with a “community of interest” with another scheme employer – **community admission bodies** (“CAB”) or those providing a service on behalf of a scheme employer – **transferee admission bodies** (“TAB”). CABs will include housing associations and charities, TABs will generally be contractors. The Fund can set its criteria for participation by these employers and can refuse entry if the requirements as set out in the Fund’s admissions policy are not met. (NB The terminology CAB and TAB has been dropped from recent LGPS Regulations, which instead combine both under the single term ‘admission bodies’; however, we have retained the old terminology here as we consider it to be helpful in setting funding strategies for these different employers).

2.4 How does the measured contribution rate vary for different employers?

All three steps above are considered when setting contributions (more details are given in Section 3 and Appendix D).

1. The **funding target** is based on a set of assumptions about the future, (e.g. investment returns, inflation, pensioners’ life expectancies). However, if an employer is approaching the end of its participation in the Fund then its funding target may be set on a more prudent basis, so that its liabilities are less likely to be spread among other employers after its cessation;

2. The **time horizon** required is, in broad terms, the period over which any deficit is to be recovered. A shorter period will lead to higher contributions, and vice versa (all other things being equal). Employers may be given a lower time horizon if they have a less permanent anticipated membership, or do not have tax-raising powers to increase contributions if investment returns under-perform; and

3. The **probability of achieving** the funding target over that time horizon will be dependent on the Fund's view of the strength of employer covenant and its funding profile. Where an employer is weaker, or potentially ceasing from the Fund, then the required probability will be set higher, which in turn will increase the required contributions (and vice versa).

For some employers, it may be agreed to pool contributions, see 3.4.

Any costs of non-ill-health early retirements must be paid by the employer, see 3.6.

Costs of ill-health early retirements are covered in 3.7 and 3.8.

2.5 How is a deficit (or surplus) calculated?

An employer's "funding level" is defined as the ratio of:

- the market value of the employer's share of assets (see Appendix D, section D5, for further details of how this is calculated), to
- the value placed by the actuary on the benefits built up to date for the employer's employees and ex-employees (the "liabilities"). The Fund actuary agrees with the Administering Authority the assumptions to be used in calculating this value.

If this is less than 100% then it means the employer has a shortfall, which is the employer's deficit; if it is more than 100% then the employer is said to be in surplus. The amount of deficit or shortfall is the difference between the asset value and the liabilities value.

It is important to note that the deficit/surplus and funding level are only measurements at a point in time, on a particular set of assumptions about the future. Whilst we recognise that various parties will take an interest in these measures, for most employers the key issue is how likely it is that their contributions will be sufficient to pay for their members' benefits (when added to their existing asset share and anticipated investment returns).

In short, deficits and funding levels are short term measures, whereas contribution-setting is a longer-term issue.

2.6 How does the Fund recognise that contribution levels can affect council and employer service provision, and council tax?

The Administering Authority and the Fund actuary are acutely aware that, all other things being equal, a higher contribution required to be paid to the Fund will mean less cash available for the employer to spend on the provision of services. For instance:

- Higher Pension Fund contributions may result in reduced council spending, which in turn could affect the resources available for council services, and/or greater pressure on council tax levels;
- Contributions which Academies pay to the Fund will therefore not be available to pay for providing education; and

- Other employers will provide various services to the local community, perhaps through housing associations, charitable work, or contracting council services. If they are required to pay more in pension contributions to the LGPS then this may affect their ability to provide the local services at a reasonable cost.

Whilst all this is true, it should also be borne in mind that:

- The Fund provides invaluable financial security to local families, whether to those who formerly worked in the service of the local community who have now retired, or to their families after their death;

- The Fund must have the assets available to meet these retirement and death benefits, which in turn means that the various employers must each pay their own way. Lower contributions today will mean higher contributions tomorrow: deferring payments does not alter the employer's ultimate obligation to the Fund in respect of its current and former employees;

- Each employer will generally only pay for its own employees and ex-employees (and their dependants), not for those of other employers in the Fund;

- The Fund strives to maintain reasonably stable employer contribution rates where appropriate and possible. However, a recent shift in regulatory focus means that solvency within each generation is considered by the Government to be a higher priority than stability of contribution rates;

- The Fund wishes to avoid the situation where an employer falls so far behind in managing its funding shortfall that its deficit becomes unmanageable in practice: such a situation may lead to employer insolvency and the resulting deficit falling on the other Fund employers. In that situation, those employers' services would in turn suffer as a result;

- Council contributions to the Fund should be at a suitable level, to protect the interests of different generations of council tax payers. For instance, underpayment of contributions for some years will need to be balanced by overpayment in other years; the council will wish to minimise the extent to which council tax payers in one period are in effect benefitting at the expense of those paying in a different period.

Overall, therefore, there is clearly a balance to be struck between the Fund's need for maintaining prudent funding levels, and the employers' need to allocate their resources appropriately. The Fund achieves this through various techniques which affect contribution increases to various degrees (see 3.1). In deciding which of these techniques to apply to any given employer, the Administering Authority takes a view on the financial standing of the employer, i.e. its ability to meet its funding commitments and the relevant time horizon.

The Administering Authority will consider a risk assessment of that employer using a knowledge base which is regularly monitored and kept up-to-date. This database will include such information as the type of employer, its membership profile and funding position, any guarantors or security provision, material changes anticipated, etc.

For instance, where the Administering Authority has reasonable confidence that an employer will be able to meet its funding commitments, then the Fund will permit options such as stabilisation (see 3.3 Note (b)), a longer time horizon relative to other employers, and/or a lower probability of achieving their funding target. Such options will temporarily produce lower contribution levels than would otherwise have applied. This is permitted in the expectation that the employer will still be able to meet its obligations for many years to come.

On the other hand, where there is doubt that an employer will be able to meet its funding commitments or withstand a significant change in its commitments, then a higher funding target, and/or a shorter deficit recovery period relative to other employers, and/or a higher probability of achieving the target may be required.

The Fund actively seeks employer input, including to its funding arrangements, through various means: see Appendix A.

3 Calculating contributions for individual Employers

3.1 General comments

A key challenge for the Administering Authority is to balance the need for stable, affordable employer contributions with the requirement to take a prudent, longer-term view of funding and ensure the solvency of the Fund. The Fund's three-step process identifies the key issues:

1. What is a suitably (but not overly) prudent funding target?
2. How long should the employer be permitted to reach that target? This should be realistic but not so long that the funding target is in danger of never actually being achieved.
3. What probability is required to reach that funding target? This will always be less than 100% as we cannot be certain of future market movements. Higher probability "bars" can be used for employers where the Fund wishes to reduce the risk to the Fund.

The Administering Authority recognises that there may occasionally be circumstances affecting individual employers that are not easily managed within the rules and policies set out in the FSS. Therefore, the Administering Authority may, at its sole discretion, direct the actuary to adopt alternative funding approaches on a case by case basis for specific employers.

3.2 The effect of paying lower contributions

In limited circumstances the Administering Authority may permit employers to pay contributions at a lower level than is assessed for the employer using the three-step process above. At their absolute discretion, the Administering Authority may:

- extend the time horizon for targeting full funding;
- adjust the required probability of meeting the funding target;
- permit an employer to participate in the Fund's stabilisation mechanisms;
- permit extended phasing in of contribution rises or reductions;
- pool contributions amongst employers with similar characteristics; and/or
- accept some form of security or guarantee in lieu of a higher contribution rate than would otherwise be the case.

Employers which are permitted to use one or more of the above methods will often be paying, for a time, contributions less than required to meet their funding target, over the appropriate time horizon with the required likelihood of success. Such employers should appreciate that:

- their true long term liability (i.e. the actual eventual cost of benefits payable to their employees and ex-employees) is not affected by the pace of paying contributions;
- lower contributions in the short term will incur a greater loss of investment returns on the deficit. Thus, deferring contributions may lead to higher contributions in the long-term; and
- it may take longer to reach their funding target, all other things being equal.

Overleaf (3.3) is a summary of how the main funding policies differ for different types of employer, followed by more detailed notes where necessary.
Section 3.4 onwards deals with various other funding issues which apply to all employers.

3.3 The different approaches used for different employers

Type of employer	Scheduled Bodies			Community Admission Bodies and Designating Employers		Transferee Admission Bodies
Sub-type	**Council**	**Colleges**	**Academies**	**Open to new entrants**	**Closed to new entrants**	**(all)**
Funding Target Basis used	Ongoing, assumes long-term Fund participation (see Appendix E)			Ongoing, but may move to "gilts basis" - see Note (a)		Ongoing, assumes fixed contract term in the Fund (see Appendix E)
Primary rate approach	(see Appendix D – D.2)					
Stabilised contribution rate?	Yes - see Note (b)	No	No	No	No	No
Maximum time horizon – Note (c)	17 years	17 years	17 years	Future working lifetime	Future working lifetime	Outstanding contract term
Secondary rate – Note (d)	% of payroll	% of payroll	% of payroll	% of payroll	% of payroll	% of payroll
Treatment of surplus	Covered by stabilisation arrangement	Preferred approach: contributions kept at Primary rate. However, reductions may be permitted by the Admin. Authority				Preferred approach: contributions kept at future service rate. However, contractors may be permitted to reduce contributions by spreading the surplus over the remaining contract term
Probability of achieving target – Note (e)	66%	70%	70%	66% if guaranteed, 75% otherwise	66% if guaranteed, 75% otherwise	66% if guaranteed, 75% otherwise
Phasing of contribution changes	Covered by stabilisation arrangement	At the discretion of the Administering Authority		None	None	None
Review of rates – Note (f)	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations					Particularly reviewed in last 3 years of contract
New employer	n/a	n/a	Note (g)	Note (h)		Notes (h) & (i)
Cessation of participation: cessation debt payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation debt principles applied would be as per Note (j).			Can be ceased subject to terms of admission agreement. Cessation debt will be calculated on a basis appropriate to the circumstances of cessation – see Note (j).		Participation is assumed to expire at the end of the contract. Cessation debt (if any) calculated on ongoing basis. Awarding Authority will be liable for future deficits and contributions arising.

Note (a) (Basis for CABs and Designating Employers closed to new entrants)

In the circumstances where:

- the employer is a Designating Employer, or an Admission Body but not a Transferee Admission Body, and
- the employer has no guarantor, and
- the admission agreement is likely to terminate, or the employer is likely to lose its last active member, within a timeframe considered appropriate by the Administering Authority to prompt a change in funding,

the Administering Authority may set a higher funding target (e.g. using a discount rate set equal to gilt yields) by the time the agreement terminates or the last active member leaves, to protect other employers in the Fund. This policy will increase regular contributions and reduce, but not eliminate, the possibility of a final deficit payment being required from the employer when a cessation valuation is carried out.

The Administering Authority also reserves the right to adopt the above approach in respect of those Designating Employers and Admission Bodies with no guarantor, where the strength of covenant is weak but there is no immediate expectation that the admission agreement will cease or the Designating Employer alters its designation.

Note (b) (Stabilisation)

Stabilisation is a mechanism where employer contribution rate variations from year to year are kept within a pre-determined range, thus allowing those employers' rates to be relatively stable. In the interests of stability and affordability of employer contributions, the Administering Authority, on the advice of the Fund Actuary, believes that stabilising contributions can still be viewed as a prudent longer-term approach. However, employers whose contribution rates have been "stabilised" (and may therefore be paying less than their theoretical contribution rate) should be aware of the risks of this approach and should consider making additional payments to the Fund if possible.

This stabilisation mechanism allows short-term investment market volatility to be managed so as not to cause volatility in employer contribution rates, on the basis that a long-term view can be taken on net cash inflow, investment returns and strength of employer covenant.

The current stabilisation mechanism applies to London Borough of Barking and Dagenham Council as a tax raising body.

Based on extensive modelling carried out for the 2016 valuation exercise (see Section 4), total contributions have been set to ensure that stabilised employers have at least a 66% chance of being fully funded in 20 years under the 2016 formal valuation assumptions.

The stabilisation criteria and limits will be reviewed at the 31 March 2019 valuation, to take effect from 1 April 2020. However, the Administering Authority reserves the right to review the stabilisation criteria and limits at any time before then, based on membership and/or employer changes as described above.

Note (c) (Maximum time horizon)

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2017 for the 2016 valuation). The Administering Authority would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative time horizons, for example where there were no new entrants.

Note (d) (Secondary rate)

For employers where stabilisation is not being applied, the Secondary contribution rate for each employer covering the three-year period until the next valuation will often be set as a percentage of salaries. However, the Administering Authority reserves the right to amend these rates between valuations and/or to require these payments in monetary terms instead, for instance where:

- the employer is relatively mature, i.e. has a large Secondary contribution rate (e.g. above 15% of payroll), or
- there has been a significant reduction in payroll due to outsourcing or redundancy exercises, or
- the employer has closed the Fund to new entrants.

Note (e) (Probability of achieving funding target)

Each employer has its funding target calculated, and a relevant time horizon over which to reach that target. Contributions are set such that, combined with the employer's current asset share and anticipated market movements over the time horizon, the funding target is achieved with a given minimum probability. A higher required probability bar will give rise to higher required contributions, and vice versa.

The way in which contributions are set using these three steps, and relevant economic projections, is described in further detail in Appendix D.

Different probabilities are set for different employers depending on their nature and circumstances: in broad terms, a higher probability will apply due to one or more of the following:

- the Fund believes the employer poses a greater funding risk than other employers,
- the employer does not have tax-raising powers;
- the employer does not have a guarantor or other sufficient security backing its funding position; and/or
- the employer is likely to cease participation in the Fund in the short or medium term.

Note (f) (Regular Reviews)

Such reviews may be triggered by significant events including but not limited to: significant reductions in payroll, altered employer circumstances, Government restructuring affecting the employer's business, or failure to pay contributions or arrange appropriate security as required by the Administering Authority.

The result of a review may be to require increased contributions (by strengthening the actuarial assumptions adopted and/or moving to monetary levels of deficit recovery contributions), and/or an increased level of security or guarantee.

Note (g) (New Academy conversions)

At the time of writing, the Fund's policies on academies' funding issues are as follows:

i. The new academy will be regarded as a separate employer and will not be pooled with other employers in the Fund. The only exception is where the academy is part of a Multi Academy Trust (MAT) in which case the academy's figures will be calculated as below but can be combined with those of the other academies in the MAT;

ii. The new academy's past service liabilities on conversion will be calculated based on its active Fund members on the day before conversion. For the avoidance of doubt, these liabilities will include all past service of those members, but will exclude the liabilities relating to any ex-employees of the school who have deferred or pensioner status;

iii. The new academy will be allocated an initial asset share from the ceding council's assets in the Fund. This asset share will be calculated using the estimated funding position of the ceding council at the date of academy conversion. The asset allocation will be based on market conditions and active Fund membership on the day prior to conversion;

iv. The new academy's initial contribution rate will be calculated using market conditions, the council funding position and membership data, all as at the day prior to conversion;

v. As an alternative to (iv), the academy will have the option to elect to pay contributions initially in line with the ceding LEA instead. However, this election will not alter its asset or liability allocation as per (ii) and (iii) above. Ultimately, all academies remain responsible for their own allocated deficit.

The Fund's policies on academies are subject to change in the light of any amendments to DCLG guidance. Any changes will be notified to academies, and will be reflected in a subsequent version of the FSS.

Note (h) (New Admission Bodies)

With effect from 1 October 2012, the LGPS 2012 Miscellaneous Regulations introduced mandatory new requirements for all Admission Bodies brought into the Fund from that date. Under these Regulations, all new Admission Bodies will be required to provide some form of security, such as a guarantee from the letting employer, an indemnity or a bond. The security is required to cover some or all the following:

- the strain cost of redundancy early retirements resulting from the premature termination of the contract;
- allowance for the risk of asset underperformance;
- allowance for the possible non-payment of employer and member contributions to the Fund;
- allowance for the risk of a fall in gilt yields; and/or
- the current deficit.

Transferee Admission Bodies: For all TABs, the security must be to the satisfaction of the Administering Authority as well as the letting employer, and will be reassessed on an annual basis. See also Note (i) below.

Community Admission Bodies: The Administering Authority will only consider requests from CABs (or other similar bodies, such as section 75 NHS partnerships) to join the Fund if they are sponsored by a Scheduled Body with tax raising powers, guaranteeing their liabilities and also providing a form of security as above.

The above approaches reduce the risk, to other employers in the Fund, of potentially having to pick up any shortfall in respect of Admission Bodies ceasing with an unpaid deficit.

Note (i) (New Transferee Admission Bodies)

A new TAB usually joins the Fund as a result of the letting/outsourcing of some services from an existing employer (normally a Scheduled Body such as a council or academy) to another organisation (a "contractor"). This involves the TUPE transfer of some staff from the letting employer to the contractor. Consequently, for the duration of the contract, the contractor is a new participating employer in the Fund so that the transferring employees maintain their eligibility for LGPS membership. At the end of the contract the employees revert to the letting employer or to a replacement contractor.

Ordinarily, the TAB would be set up in the Fund as a new employer with responsibility for all the accrued benefits of the transferring employees; in this case, the contractor would usually be assigned an initial asset allocation equal to the past service liability value of the employees' Fund benefits. The quid pro quo is that the contractor is then expected to ensure that its share of the Fund is also fully funded at the end of the contract: see Note (j).

Employers which "outsource" have flexibility in the way that they can deal with the pension risk potentially taken on by the contractor. There are three different routes that such employers may wish to adopt. Clearly as the risk ultimately resides with the employer letting the contract, it is for them to agree the appropriate route with the contractor:

i) Pooling
Under this option the contractor is pooled with the letting employer. In this case, the contractor pays the same rate as the letting employer, which may be under a stabilisation approach.

ii) Letting employer retains pre-contract risks
Under this option the letting employer would retain responsibility for assets and liabilities in respect of service accrued prior to the contract commencement date. The contractor would be responsible for the future liabilities that accrue in respect of transferred staff. The contractor's contribution rate could vary from one valuation to the next. It would be liable for any deficit at the end of the contract term in respect of assets and liabilities attributable to service accrued during the contract term.

iii) Fixed contribution rate agreed
Under this option the contractor pays a fixed contribution rate and does not pay any cessation deficit.

The Administering Authority is willing to administer any of the above options if the approach is documented in the Admission Agreement as well as the transfer agreement. The Admission Agreement should ensure that some element of risk transfers to the contractor where it relates to their decisions and it is unfair to burden the letting employer with that risk. For example, the contractor should typically be responsible for pension costs that arise from:

- above average pay increases, including the effect in respect of service prior to contract commencement even if the letting employer takes on responsibility for the latter under (ii) above; and
- redundancy and early retirement decisions.

Note (j) (Admission Bodies Ceasing)

Notwithstanding the provisions of the Admission Agreement, the Administering Authority may consider any of the following as triggers for the cessation of an admission agreement with any type of body:

- Last active member ceasing participation in the Fund (NB recent LGPS Regulation changes mean that the Administering Authority has the discretion to defer acting for up to three years, so that if the employer acquires one or more active Fund members during that period then cessation is not triggered. The current Fund policy is that this is left as a discretion and may or may not be applied in any given case);

- The insolvency, winding up or liquidation of the Admission Body;

- Any breach by the Admission Body of any of its obligations under the Agreement that they have failed to remedy to the satisfaction of the Fund;

- A failure by the Admission Body to pay any sums due to the Fund within the period required by the Fund; or

- The failure by the Admission Body to renew or adjust the level of the bond or indemnity, or to confirm an appropriate alternative guarantor, as required by the Fund.

On cessation, the Administering Authority will instruct the Fund actuary to carry out a cessation valuation to determine whether there is any deficit or surplus. Where there is a deficit, payment of this amount in full would normally be sought from the Admission Body; where there is a surplus it should be noted that current legislation does not permit a refund payment to the Admission Body.

For non-Transferee Admission Bodies whose participation is voluntarily ended either by themselves or the Fund, or where a cessation event has been triggered, the Administering Authority must look to protect the interests of other ongoing employers. The actuary will therefore adopt an approach which, to the extent reasonably practicable, protects the other employers from the likelihood of any material loss emerging in future:

(a) Where a guarantor does not exist then, to protect other employers in the Fund, the cessation liabilities and final deficit will normally be calculated using a “gilts cessation basis”, which is more prudent than the ongoing basis. This has no allowance for

potential future investment outperformance above gilt yields, and has added allowance for future improvements in life expectancy. This could give rise to significant cessation debts being required.

(b) Where there is a guarantor for future deficits and contributions, the details of the guarantee will be considered prior to the cessation valuation being carried out. In some cases the guarantor is simply guarantor of last resort and therefore the cessation valuation will be carried out consistently with the approach taken had there been no guarantor in place. Alternatively, where the guarantor is not simply guarantor of last resort, the cessation may be calculated using the ongoing basis as described in Appendix E;

(c) Again, depending on the nature of the guarantee, it may be possible to simply transfer the former Admission Body's liabilities and assets to the guarantor, without needing to crystallise any deficit. This approach may be adopted where the employer cannot pay the contributions due, and this is within the terms of the guarantee.

Under (a) and (b), any shortfall would usually be levied on the departing Admission Body as a single lump sum payment. If this is not possible then the Fund would spread the payment subject to there being a security in place for the employer (i.e. a bond indemnity or guarantee).

If the Fund is not able to recover the required payment in full, then the unpaid amounts fall to be shared amongst all the other employers in the Fund. This may require an immediate revision to the Rates and Adjustments Certificate affecting other employers in the Fund, or instead be reflected in the contribution rates set at the next formal valuation following the cessation date.

As an alternative, where the ceasing Admission Body is continuing in business, the Fund at its absolute discretion reserves the right to enter an agreement with the ceasing Admission Body. Under this agreement, the Fund would accept an appropriate alternative security to be held against any deficit, and would carry out the cessation valuation on an ongoing basis: deficit recovery payments would be derived from this cessation debt. This approach would be monitored as part of each triennial valuation: The Fund reserves the right to revert to a "gilts cessation basis" and seek immediate payment of any funding shortfall identified. The Administering Authority may need to seek legal advice in such cases, as the Body would have no contributing members.

3.4 Pooled contributions

From time to time, with the advice of the Actuary, the Administering Authority may set up pools for employers with similar or complementary characteristics. This will always be in line with its broader funding strategy. Currently the pools in place within the Fund are as follows:

- Schools generally are also pooled with their funding Council. However, there may be exceptions for specialist or independent schools.
- Smaller Transferee Admission Bodies may be pooled with the letting employer, provided all parties (particularly the letting employer) agree.

Those employers which have been pooled are identified in the Rates and Adjustments Certificate. Employers permitted to enter (or remain in) a pool at the 2016 valuation will not be advised of their individual contribution rate unless agreed by the Administering Authority.

Community Admission Bodies that are deemed by the Administering Authority to have closed to new entrants are not usually permitted to participate in a pool.

3.5 Additional flexibility in return for added security

The Administering Authority may permit greater flexibility to the employer's contributions if the employer provides added security to the satisfaction of the Administering Authority.

Such flexibility includes a reduced rate of contribution, an extended time horizon, or permission to join a pool with another body (e.g. the Local Authority).

Such security may include, but is not limited to, a suitable bond, a legally-binding guarantee from an appropriate third party, or security over an employer asset of sufficient value.

The degree of flexibility given may consider factors such as:

- the extent of the employer's deficit;
- the amount and quality of the security offered;
- the employer's financial security and business plan; and
- whether the admission agreement is likely to be open or closed to new entrants.

3.6 Non-ill health early retirement costs

It is assumed that members' benefits are payable from the earliest age that the employee could retire without incurring a reduction to their benefit (and without requiring their employer's consent to retire). (NB the relevant age may be different for different periods of service, following the benefit changes from April 2008 and April 2014). Employers are required to pay additional contributions ('strain') wherever an employee retires before attaining this age. The actuary's funding basis makes no allowance for premature retirement except on grounds of ill-health. With the agreement of the Administering Authority the payment is paid immediately:

3.7 Ill health early retirement costs

In the event of a member's early retirement on the grounds of ill-health, a funding strain will usually arise, which can be very large. Such strains are currently met by each employer, although individual employers may elect to take external insurance (see 3.8 below).

Admitted Bodies will usually have an 'ill health allowance'; Scheduled Bodies may have this also, depending on their agreement terms with the Administering Authority. The Fund monitors each employer's ill health experience on an ongoing basis. If the cumulative cost of ill health retirement in any financial year exceeds the allowance at the previous valuation, the employer will be charged additional contributions on the same basis as apply for non-ill-health cases. Details will be included in each separate Admission Agreement.

3.8 External Ill health insurance

If an employer provides satisfactory evidence to the Administering Authority of a current external insurance policy covering ill health early retirement strains, then:

- the employer's contribution to the Fund each year is reduced by the amount of that year's insurance premium, so that the total contribution is unchanged, and
- there is no need for monitoring of allowances.

The employer must keep the Administering Authority notified of any changes in the insurance policy's coverage or premium terms, or if the policy is ceased.

3.9 Employers with no remaining active members

In general an employer ceasing in the Fund, due to the departure of the last active member, will pay a cessation debt on an appropriate basis (see 3.3, Note (j)) and consequently have no further obligation to the Fund. Thereafter it is expected that one of two situations will eventually arise:

a) The employer's asset share runs out before all its ex-employees' benefits have been paid. In this situation the other Fund employers will be required to contribute to pay all remaining benefits: this will be done by the Fund actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;

b) The last ex-employee or dependant dies before the employer's asset share has been fully utilised. In this situation the remaining assets would be apportioned pro-rata by the Fund's actuary to the other Fund employers.

c) In exceptional circumstances the Fund may permit an employer with no remaining active members to continue contributing to the Fund. This would require the provision of a suitable security or guarantee, as well as a written ongoing commitment to fund the remainder of the employer's obligations over an appropriate period. The Fund would reserve the right to invoke the cessation requirements in the future, however. The Administering Authority may need to seek legal advice in such cases, as the employer would have no contributing members.

3.10 Policies on bulk transfers

The Fund has a separate written policy which covers bulk transfer payments into, out of and within the Fund. Each case will be treated on its own merits, but in general:

- The Fund will not pay bulk transfers greater than the lesser of (a) the asset share of the transferring employer in the Fund, and (b) the value of the past service liabilities of the transferring members;

- The Fund will not grant added benefits to members bringing in entitlements from another Fund unless the asset transfer is sufficient to meet the added liabilities; and
- The Fund may permit shortfalls to arise on bulk transfers if the Fund employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's Fund contributions to increase between valuations.

4 Funding strategy and links to investment strategy

4.1 What is the Fund's investment strategy?

The Fund has built up assets over the years, and continues to receive contribution and other income. All of this must be invested in a suitable manner, which is the investment strategy.

The administering authority sets the investment strategy, after consultation with the employers and after taking investment advice. The precise mix, manager make up and target returns are set out in the Statement of Investment Principles (being replaced by an Investment Strategy Statement under new LGPS Regulations), which is available to members and employers.

The investment strategy is set for the long-term, but is reviewed from time to time. Normally a full review is carried out as part of each actuarial valuation, and is kept under review annually between actuarial valuations to ensure that it remains appropriate to the Fund's liability profile. The same investment strategy is currently followed for all employers.

4.2 What is the link between funding strategy and investment strategy?

The Fund must be able to meet all benefit payments as and when they fall due. These payments will be met by contributions (resulting from the funding strategy) or asset returns and income (resulting from the investment strategy). To the extent that investment returns or income fall short, then higher cash contributions are required from employers, and vice versa Therefore, the funding and investment strategies are inextricably linked.

4.3 How does the funding strategy reflect the Fund's investment strategy?

In the opinion of the Fund actuary, the current funding policy is consistent with the current investment strategy of the Fund. The asset outperformance assumption contained in the discount rate (see Appendix E3) is within a range that would be considered acceptable for funding purposes; it is also considered to be consistent with the requirement to take a "prudent longer-term view" of the funding of liabilities as required by the UK Government (see Appendix A1).

However, in the short term – such as the three yearly assessments at formal valuations – there is the scope for considerable volatility and there is a material chance that in the short-term and even medium term, asset returns will fall short of this target. The stability measures described in Section 3 will damp down, but not remove, the effect on employers' contributions.
The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

4.4 How does this differ for a large stable employer?

The Actuary has developed four key measures which capture the essence of the Fund's strategies, both funding and investment:

Prudence - the Fund should have a reasonable expectation of being fully funded in the long term;
Affordability – how much can employers afford;

Stewardship – the assumptions used should be sustainable in the long term, without having to resort to overly optimistic assumptions about the future to maintain an apparently healthy funding position; and

Stability – employers should not see significant moves in their contribution rates from one year to the next, to help provide a more stable budgeting environment.

The key problem is that the key objectives often conflict. For example, minimising the long term cost of the scheme (i.e. keeping employer rates affordable) is best achieved by investing in higher returning assets e.g. equities. However, equities are also very volatile (i.e. go up and down fairly frequently in fairly large moves), which conflicts with the objective to have stable contribution rates.

Therefore, a balance needs to be maintained between risk and reward, which has been considered by the use of Asset Liability Modelling: this is a set of calculation techniques applied by the Fund's actuary to model the range of potential future solvency levels and contribution rates.

The Actuary was able to model the impact of these four key areas, for the purpose of setting a stabilisation approach (see 3.3 Note (b)). The modelling demonstrated that retaining the present investment strategy, coupled with constraining employer contribution rate changes as described in 3.3 Note (b), struck an appropriate balance between the above objectives. In particular the stabilisation approach currently adopted meets the need for stability of contributions without jeopardising the Administering Authority's aims of prudent stewardship of the Fund.

Whilst the current stabilisation mechanism is to remain in place until 2020, it should be noted that this will need to be reviewed following the 2019 valuation.

4.5 Does the Fund monitor its overall funding position?

The Administering Authority monitors the relative funding position, i.e. changes in the relationship between asset values and the liabilities value, quarterly. It reports this to the regular Pensions Committee meetings, and also to employers through newsletters and Employers Forums.

5 Statutory reporting and comparison to other LGPS Funds

5.1 Purpose

Under Section 13(4)(c) of the Public Service Pensions Act 2013 ("Section 13"), the Government Actuary's Department must, following each triennial actuarial valuation, report to the Department of Communities & Local Government (DCLG) on each of the LGPS Funds in England & Wales. This report will cover whether, for each Fund, the rate of employer contributions are set at an appropriate level to ensure both the solvency and the long term cost efficiency of the Fund.

This additional DCLG oversight may have an impact on the strategy for setting contribution rates at future valuations.

5.2 Solvency

For the purposes of Section 13, the rate of employer contributions shall be deemed to have been set at an appropriate level to ensure solvency if:

(a) the rate of employer contributions is set to target a funding level for the Fund of 100%, over an appropriate time period and using appropriate actuarial assumptions (where appropriateness is considered in both absolute and relative terms in comparison with other funds); and either
(b) employers collectively have the financial capacity to increase employer contributions, and/or the Fund is able to realise contingent assets should future circumstances require, in order to continue to target a funding level of 100%; or
(c) there is an appropriate plan in place should there be, or if there is expected in future to be, a material reduction in the capacity of fund employers to increase contributions as might be needed.

5.3 Long Term Cost Efficiency

The rate of employer contributions shall be deemed to have been set at an appropriate level to ensure long term cost efficiency if:

i. the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual,
ii. with an appropriate adjustment to that rate for any surplus or deficit in the Fund.

In assessing whether the above condition is met, DCLG may have regard to various absolute and relative considerations. A relative consideration is primarily concerned with comparing LGPS pension funds with other LGPS pension funds. An absolute consideration is primarily concerned with comparing Funds with a given objective benchmark. Relative considerations include:

1. the implied deficit recovery period; and
2. the investment return required to achieve full funding after 20 years.

Absolute considerations include:

1. the extent to which the contributions payable are sufficient to cover the cost of current benefit accrual and the interest cost on any deficit;
2. how the required investment return under “relative considerations” above compares to the estimated future return being targeted by the Fund’s current investment strategy;
3. the extent to which contributions actually paid have been in line with the expected contributions based on the extant rates and adjustment certificate; and
4. the extent to which any new deficit recovery plan can be directly reconciled with, and can be demonstrated to be a continuation of, any previous deficit recovery plan, after allowing for actual Fund experience.

DCLG may assess and compare these metrics on a suitable standardised market-related basis, for example where the local funds’ actuarial bases do not make comparisons straightforward.

Appendix A – Regulatory framework

A1 Why does the Fund need an FSS?

The Department for Communities and Local Government (DCLG) has stated that the purpose of the FSS is:

*"to establish a **clear and transparent fund-specific strategy** which will identify how employers' pension liabilities are best met going forward;*
*to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and*
*to take a **prudent longer-term view** of funding those liabilities."*

These objectives are desirable individually, but may be mutually conflicting.

The requirement to maintain and publish a FSS is contained in LGPS Regulations which are updated from time to time. In publishing the FSS the Administering Authority has to have regard to any guidance published by Chartered Institute of Public Finance and Accountancy (CIPFA) (most recently in 2016) and to its Statement of Investment Principles / Investment Strategy Statement.

This is the framework within which the Fund's actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Administering Authority when other funding decisions are required, such as when employers join or leave the Fund. The FSS applies to all employers participating in the Fund.

A2 Does the Administering Authority consult anyone on the FSS?

Yes. This is required by LGPS Regulations. It is covered in more detail by the most recent CIPFA guidance, which states that the FSS must first be subject to "consultation with such persons as the authority considers appropriate", and should include "a meaningful dialogue at officer and elected member level with council tax raising authorities and with corresponding representatives of other participating employers".

In practice, for the Fund, the consultation process for this FSS was as follows:

a) A draft version of the FSS was issued to all participating employers on 13 January 2017 for comment;
b) Comments were requested within 30 days;
c) The draft FSS will be taken to the Pension Board on 27 February at which questions regarding the FSS can be raised and answered;
d) Following the end of the consultation period the FSS will be updated where required and will be taken to the Pension Panel on the 15th of March 2017 for agreement.
e) The FSS will then published by 31 March 2017.
f) The FSS is made available through the following routes:
    - Published on the website: www.lbbdpensionfund.org;
    - A copy sent by e-mail to each participating employer in the Fund;
    - A full copy [included in/linked from] the annual report and accounts of the Fund;
    - Copies sent to investment managers and advisers;

A4 How often is the FSS reviewed?

The FSS is reviewed in detail at least every three years as part of the triennial valuation. This version is expected to remain unaltered until it is consulted upon as part of the formal process for the next valuation in 2019.

It is possible that (usually slight) amendments may be needed within the three-year period. These would be needed to reflect any regulatory changes, or alterations to the way the Fund operates (e.g. to accommodate a new class of employer). Any such amendments would be consulted upon as appropriate:

- trivial amendments would be simply notified at the next round of employer communications,
- amendments affecting only one class of employer would be consulted with those employers,
- other more significant amendments would be subject to full consultation.

In any event, changes to the FSS would need agreement by the Pensions Committee and would be included in the relevant Committee Meeting minutes.

A5 How does the FSS fit into other Fund documents?

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues, for example there are several separate statements published by the Fund including the Investment Strategy Statement, Governance and Communications Strategy and an Annual Report and Accounts with up to date information on the Fund. These documents can be found on the web at www.lbbdpensionfund.org.

Appendix B – Responsibilities of key parties

The efficient and effective operation of the Fund needs various parties to each play their part.

B1 The Administering Authority should:-

1. operate the Fund as per the LGPS Regulations;
2. effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a Fund employer;
3. collect employer and employee contributions, and investment income and other amounts due to the Fund;
4. ensure that cash is available to meet benefit payments as and when they fall due;
5. pay from the Fund the relevant benefits and entitlements that are due;
6. invest surplus monies (i.e. contributions and other income which are not immediately needed to pay benefits) in accordance with the Fund's Statement of Investment Principles/Investment Strategy Statement (SIP/ISS) and LGPS Regulations;
7. communicate appropriately with employers so that they fully understand their obligations to the Fund;
8. respond appropriately to safeguard the Fund against the consequences of employer default;
9. manage the valuation process in consultation with the Fund's actuary;
10. provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
11. prepare and maintain a FSS and a SIP/ISS, after consultation;
12. notify the Fund's actuary of material changes which could affect funding (this is covered in a separate agreement with the actuary); and
13. monitor all aspects of the fund's performance and funding and amend the FSS and SIP/ISS as necessary and appropriate.

B2 The Individual Employer should:-

1. deduct contributions from employees' pay correctly;
2. pay all contributions, including their own as determined by the actuary, promptly by the due date;
3. have a policy and exercise discretions within the regulatory framework;
4. make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain; and
5. notify the Administering Authority promptly of all changes to its circumstances, prospects or membership, which could affect future funding.

B3 The Fund Actuary should:-

1. prepare valuations, including the setting of employers' contribution rates. This will involve agreeing assumptions with the Administering Authority, having regard to the FSS and LGPS Regulations, and targeting each employer's solvency appropriately;
2. provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
3. provide advice relating to new employers in the Fund, including the level and type of bonds or other forms of security (and the monitoring of these);

4. prepare advice and calculations in connection with bulk transfers and individual benefit-related matters;
5. assist the Administering Authority in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;
6. advise on the termination of employers' participation in the Fund; and
7. fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

B4 Other parties: -

1. investment advisers (either internal or external) should ensure the Fund's SIP/ISS remains appropriate, and consistent with this FSS;
2. investment managers, custodians and bankers should all play their part in the effective investment (and dis-investment) of Fund assets, in line with the SIP/ISS;
3. auditors should comply with their auditing standards, ensure Fund compliance with all requirements, monitor and advise on fraud detection, and sign off annual reports and financial statements as required;
4. governance advisers may be appointed to advise the Administering Authority on efficient processes and working methods in managing the Fund;
5. legal advisers (either internal or external) should ensure the Fund's operation and management remains fully compliant with all regulations and broader local government requirements, including the Administering Authority's own procedures;
6. the Department for Communities and Local Government (assisted by the Government Actuary's Department) and the Scheme Advisory Board, should work with LGPS Funds to meet Section 13 requirements.

Appendix C – Key risks and controls

C1 Types of risk

The Administering Authority has an active risk management programme in place. The measures that it has in place to control key risks are summarised below under the following headings:

- financial;
- demographic;
- regulatory; and
- governance.

C2 Financial risks

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning the valuation of liabilities over the long-term.	Only anticipate long-term returns on a relatively prudent basis to reduce risk of under-performing. Assets invested based on specialist advice, in a suitably diversified manner across asset classes, geographies, managers, etc. Analyse progress at three yearly valuations for all employers. Inter-valuation roll-forward of liabilities between valuations at whole Fund level.
Inappropriate long-term investment strategy.	Overall investment strategy options considered as an integral part of the funding strategy. Used asset liability modelling to measure 4 key outcomes. Chosen option considered to provide the best balance.
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	Stabilisation modelling at whole Fund level allows for the probability of this within a longer-term context. Inter-valuation monitoring, as above. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.
Pay and price inflation significantly more than anticipated.	The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases. Inter-valuation monitoring, as above, gives early warning. Some investment in bonds also helps to mitigate this risk. Employers pay for their own salary awards and should be mindful of the geared effect on pension liabilities of any bias in pensionable

Risk	Summary of Control Mechanisms
	pay rises towards longer-serving employees.
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	An explicit stabilisation mechanism has been agreed as part of the funding strategy. Other measures are also in place to limit sudden increases in contributions.
Orphaned employers give rise to added costs for the Fund	The Fund seeks a cessation debt (or security/guarantor) to minimise the risk of this happening in the future. If it occurs, the Actuary calculates the added cost spread pro-rata among all employers – (see 3.9).

C3 Demographic risks

Risk	Summary of Control Mechanisms
Pensioners living longer, thus increasing cost to Fund.	Set mortality assumptions with some allowance for future increases in life expectancy. The Fund Actuary has direct access to the experience of over 50 LGPS funds which allows early identification of changes in life expectancy that might in turn affect the assumptions underpinning the valuation.
Maturing Fund – i.e. proportion of actively contributing employees declines relative to retired employees.	Continue to monitor at each valuation, consider seeking monetary amounts rather than % of pay and consider alternative investment strategies.
Deteriorating patterns of early retirements	Employers are charged the extra cost of non ill-health retirements following each individual decision. Employer ill health retirement experience is monitored, and insurance is an option.
Reductions in payroll causing insufficient deficit recovery payments	In many cases this may not be sufficient cause for concern, and will in effect be caught at the next formal valuation. However, there are protections where there is concern, as follows: Employers in the stabilisation mechanism may be brought out of that mechanism to permit appropriate contribution increases (see Note (b) to 3.3). For other employers, review of contributions is permitted in general between valuations (see Note (f) to 3.3) and may require a move in deficit contributions from a percentage of payroll to fixed monetary amounts.

C4 Regulatory risks

Risk	Summary of Control Mechanisms
Changes to national pension requirements and/or HMRC rules e.g. changes arising from public sector pensions reform.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. The results of the most recent reforms were built into the 2013 valuation. Any changes to member contribution rates or benefit levels will be carefully communicated with members to minimise possible opt-outs or adverse actions.
Time, cost and/or reputational risks associated with any DCLG intervention triggered by the Section 13 analysis (see Section 5).	Take advice from Fund Actuary on position of Fund as at prior valuation, and consideration of proposed valuation approach relative to anticipated Section 13 analysis.
Changes by Government to particular employer participation in LGPS Funds, leading to impacts on funding and/or investment strategies.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. Take advice from Fund Actuary on impact of changes on the Fund and amend strategy as appropriate.

C5 Governance risks

Risk	Summary of Control Mechanisms
Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements) or not advised of an employer closing to new entrants.	The Administering Authority has a close relationship with employing bodies and communicates required standards e.g. for submission of data. The Actuary may revise the rates and Adjustments certificate to increase an employer's contributions between triennial valuations Deficit contributions may be expressed as monetary amounts.
Actuarial or investment advice is not sought, or is not heeded, or proves to be insufficient in some way	The Administering Authority maintains close contact with its specialist advisers. Advice is delivered via formal meetings involving Elected Members, and recorded appropriately. Actuarial advice is subject to professional requirements such as peer review.
Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.
An employer ceasing to exist with insufficient funding or adequacy of a	The Administering Authority believes that it would normally be too late to address the

Risk	Summary of Control Mechanisms
bond.	position if it was left to the time of departure. The risk is mitigated by: Seeking a funding guarantee from another scheme employer, or external body, where-ever possible (see Notes (h) and (j) to 3.3). Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice. Vetting prospective employers before admission. Where permitted under the regulations requiring a bond to protect the Fund from various risks. Requiring new Community Admission Bodies to have a guarantor. Reviewing bond or guarantor arrangements at regular intervals (see Note (f) to 3.3). Reviewing contributions well ahead of cessation if thought appropriate (see Note (a) to 3.3).

Appendix D – The calculation of Employer contributions

In Section 2 there was a broad description of the way in which contribution rates are calculated. This Appendix considers these calculations in much more detail.

All three steps above are considered when setting contributions (more details are given in Section 3 and Appendix D:

1. The **funding target** is based on a set of assumptions about the future, e.g. investment returns, inflation, pensioners' life expectancies. However, if an employer is approaching the end of its participation in the Fund then its funding target may be set on a more prudent basis, so that its liabilities are less likely to be spread among other employers after its cessation of participation;

2. The **time horizon** required is, in broad terms, the period over which any deficit is to be recovered. A shorter period will lead to higher contributions, and vice versa (all other things being equal). Employers may be given a lower time horizon if they have a less permanent anticipated membership, or do not have tax-raising powers to increase contributions if investment returns under-perform;

3. The required **probability of achieving** the funding target over that time horizon will be dependent on the Fund's view of the strength of employer covenant and its funding profile. Where an employer is weaker, or potentially ceasing from the Fund, then the required probability will be set higher, which in turn will increase the required contributions (and vice versa).

The calculations involve actuarial assumptions about future experience, and these are described in detail in Appendix E.

D1 What is the difference between calculations across the whole Fund and calculations for an individual employer?

Employer contributions are normally made up of two elements:

a) the estimated cost of ongoing benefits being accrued, referred to as the "Primary contribution rate" (see D2 below); plus
b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "Secondary contribution rate" (see D3 below).

The contribution rate for each employer is measured as above, appropriate for each employer's funding position and membership. The whole Fund position, including that used in reporting to DCLG (see section 5), is calculated in effect as the sum of all the individual employer rates. DCLG currently only regulates at whole Fund level, without monitoring individual employer positions.

D2 How is the Primary contribution rate calculated?

The Primary element of the employer contribution rate is calculated with the aim that these contributions will meet benefit payments in respect of members' **future** service in the Fund. This is based upon the cost (in excess of members' contributions) of the benefits which employee members earn from their service each year.

The Primary rate is calculated separately for all the employers, although employers within a pool will pay the contribution rate applicable to the pool. The Primary rate is calculated such that it is projected to:

1. meet the required funding target for all future years' accrual of benefits*, excluding any accrued assets,
2. within the determined time horizon (see note 3.3 Note (c) for further details),
3. with a sufficiently high probability, as set by the Fund's strategy for the category of employer (see 3.3 Note (e) for further details).

* The projection is for the current active membership where the employer no longer admits new entrants, or additionally allows for new entrants where this is appropriate.

The projections are carried out using an economic modeller developed by the Fund's actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund's investment strategy), inflation, and bond yields. The measured contributions are calculated such that the proportion of outcomes meeting the employer's funding target (by the end of the time horizon) is equal to the required probability.

The approach includes expenses of administration to the extent that the Fund bears them, and includes allowances for benefits payable on death in service and on ill health retirement.

D3 How is the Secondary contribution rate calculated?

The combined Primary and Secondary rates aim to achieve the employer's funding target, within the appropriate time horizon, with the relevant degree of probability.

For the funding target, the Fund actuary agrees the assumptions to be used with the Administering Authority – see Appendix E. These assumptions are used to calculate the present value of all benefit payments expected in the future, relating to that employer's current and former employees, based on pensionable service to the valuation date only (i.e. ignoring further benefits to be built up in the future).

The Fund operates the same target funding level for all employers of 100% of its accrued liabilities valued on the ongoing basis, unless otherwise determined (see Section 3).

The Secondary rate is calculated as the balance over and above the Primary rate, such that the total is projected to:

1. meet the required funding target relating to combined past and future service benefit accrual, including accrued asset share (see D5 below)
2. within the determined time horizon (see 3.3 Note (c) for further details)
3. with a sufficiently high probability, as set by the Fund's strategy for the category of employer (see 3.3 Note (e) for further details).

The projections are carried out using an economic modeller developed by the Fund Actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund's investment strategy), inflation, and bond yields. The measured contributions are calculated such that the proportion of outcomes with at least 100% solvency (by the end of the time horizon) is equal to the required probability.

D4 What affects a given employer's valuation results?

The results of these calculations for a given individual employer will be affected by:

1. past contributions relative to the cost of accruals of benefits;
2. different liability profiles of employers (e.g. mix of members by age, gender, service vs. salary);
3. the effect of any differences in the funding target, i.e. the valuation basis used to value the employer's liabilities;
4. any different time horizons;
5. the difference between actual and assumed rises in pensionable pay;
6. the difference between actual and assumed increases to pensions in payment and deferred pensions;
7. the difference between actual and assumed retirements on grounds of ill-health from active status;
8. the difference between actual and assumed amounts of pension ceasing on death;
9. the additional costs of any non-ill-health retirements relative to any extra payments made; and/or
10. differences in the required probability of achieving the funding target.

D5 How is each employer's asset share calculated?

The Administering Authority does not account for each employer's assets separately. Instead, the Fund's actuary is required to apportion the assets of the whole Fund between the employers, at each triennial valuation.

This apportionment uses the income and expenditure figures provided for certain cash flows for each employer. This process adjusts for transfers of liabilities between employers participating in the Fund, but does make several simplifying assumptions. The split is calculated using an actuarial technique known as "analysis of surplus".

Actual investment returns achieved on the Fund between each valuation are applied proportionately across all employers, to the extent that employers in effect share the same investment strategy. Transfers of liabilities between employers within the Fund occur automatically within this process, with a sum broadly equivalent to the reserve required on the ongoing basis being exchanged between the two employers.

The Fund actuary does not allow for certain relatively minor events, including but not limited to:

1. the actual timing of employer contributions within any financial year;
2. the effect of the premature payment of any deferred pensions on grounds of incapacity.

These effects are swept up within a miscellaneous item in the analysis of surplus, which is split between employers in proportion to their liabilities.

The methodology adopted means that there will inevitably be some difference between the asset shares calculated for individual employers and those that would have resulted had they participated in their own ring-fenced section of the Fund.

The asset apportionment is capable of verification but not to audit standard. The Administering Authority recognises the limitations in the process, but it considers that the Fund actuary's approach addresses the risks of employer cross-subsidisation to an acceptable degree.

Appendix E – Actuarial assumptions

E1 What are the actuarial assumptions?

These are expectations of future experience used to place a value on future benefit payments ("the liabilities"). Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits. Changes in assumptions will affect the measured funding target. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.
The combination of all assumptions is described as the "basis". A more optimistic basis might involve higher assumed investment returns (discount rate), or lower assumed salary growth, pension increases or life expectancy; a more optimistic basis will give lower funding targets and lower employer costs. A more prudent basis will give higher funding targets and higher employer costs.

E2 What basis is used by the Fund?

The Fund's standard funding basis is described as the "ongoing basis", which applies to most employers in most circumstances. This is described in more detail below. It anticipates employers remaining in the Fund in the long term.

However, in certain circumstances, typically where the employer is not expected to remain in the Fund long term, a more prudent basis applies: see Note (a) to 3.3.

E3 What assumptions are made in the ongoing basis?

a) Investment return / discount rate

The key financial assumption is the anticipated return on the Fund's investments. This "discount rate" assumption makes allowance for an anticipated out-performance of Fund returns relative to long term yields on UK Government bonds ("gilts"). There is, however, no guarantee that Fund returns will out-perform gilts. The risk is greater when measured over short periods such as the three years between formal actuarial valuations, when the actual returns and assumed returns can deviate sharply.

Given the very long-term nature of the liabilities, a long term view of prospective asset returns is taken. The long term in this context would be 20 to 30 years or more.

For the purpose of the triennial funding valuation at 31 March 2016 and setting contribution rates effective from 1 April 2017, the Fund actuary has assumed that future investment returns earned by the Fund over the long term will be 1.9% per annum greater than gilt yields at the time of the valuation (this is higher than that used at the 2013 valuation, which therefore gives a lower funding target, all other things being equal). In the opinion of the Fund actuary, based on the current investment strategy of the Fund, this asset out-performance assumption is within a range that would be considered acceptable for the purposes of the funding valuation.

b) Salary growth

Pay for public sector employees is currently subject to restriction by the UK Government until 2020. Although this "pay freeze" does not officially apply to local government and associated employers, it has been suggested that they are likely to show similar restraint in respect of pay awards. Based on long term historical analysis of the membership in LGPS funds, and continued austerity measures, the salary increase assumption at the 2016 valuation has been set to be a blended rate combined of:

1. 1% p.a. until 31 March 2020, followed by
2. retail prices index (RPI) p.a. thereafter.

This gives a single "blended" assumption of RPI less 0.55%. This is a change from the previous valuation, which assumed a flat assumption of RPI plus 0.5% per annum. The change has led to a reduction in the funding target (all other things being equal).

c) Pension increases

Since 2011 the consumer prices index (CPI), rather than RPI, has been the basis for increases to public sector pensions in deferment and in payment. Note that the basis of such increases is set by the Government, and is not under the control of the Fund or any employers.

As at the previous valuation, we derive our assumption for RPI from market data as the difference between the yield on long-dated fixed interest and index-linked government bonds. This is then reduced to arrive at the CPI assumption, to allow for the "formula effect" of the difference between RPI and CPI. At this valuation, we have used a reduction of 1.0% per annum. This is a larger reduction than at 2013 (which was 0.8% p.a.), which will serve to reduce the funding target (all other things being equal). (Note that the reduction is applied in a geometric, not arithmetic, basis).

d) Life expectancy

The demographic assumptions are intended to be best estimates of future experience in the Fund based on past experience of LGPS funds which participate in Club Vita, the longevity analytics service used by the Fund, and endorsed by the actuary.

The longevity assumptions that have been adopted at this valuation are a bespoke set of "VitaCurves", produced by the Club Vita's detailed analysis, which are specifically tailored to fit the membership profile of the Fund. These curves are based on the data provided by the Fund for the purposes of this valuation.

It is acknowledged that future life expectancy and the allowance for future improvements in life expectancy, is uncertain. There is a consensus amongst actuaries, demographers and medical experts that life expectancy is likely to improve in the future. Allowance has been made in the ongoing valuation basis for future improvements in line with the 2013 version of the Continuous Mortality Investigation model published by the Actuarial Profession and a 1.25% per annum minimum underpin to future reductions in mortality rates. This is a similar allowance for future improvements than was made in 2013.
The combined effect of the above changes from the 2013 valuation approach, is to reduce life expectancy by around 0.5 years on average, which reduces the funding target all other things

being equal. The approach taken is considered reasonable in light of the long-term nature of the Fund and the assumed level of security underpinning members' benefits.

e) General

The same financial assumptions are adopted for most employers, in deriving the funding target underpinning the Primary and Secondary rates: as described in (3.3), these calculated figures are translated in different ways into employer contributions, depending on the employer's circumstances.

The demographic assumptions, in particular the life expectancy assumption, in effect vary by type of member and so reflect the different membership profiles of employers.

Appendix F – Glossary

Actuarial assumptions/ basis	The combined set of assumptions made by the actuary, regarding the future, to calculate the value of **the funding target**. The main assumptions will relate to the **discount rate**, salary growth, pension increases and longevity. More prudent assumptions will give a higher target value, whereas more optimistic assumptions will give a lower value.
Administering Authority	The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".
Admission Bodies	Employers where there is an Admission Agreement setting out the employer's obligations. These can be Community Admission Bodies or Transferee Admission Bodies. For more details (see 2.3).
Covenant	The assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term.
Designating Employer	Employers such as town and parish councils that can participate in the LGPS via resolution. These employers can designate which of their employees are eligible to join the Fund.
Discount rate	The annual rate at which future assumed cashflows (in and out of the Fund) are discounted to the present day. This is necessary to provide a **funding target** which is consistent with the present-day value of the assets. A lower discount rate gives a higher target value, and vice versa. It is used in the calculation of the **Primary and Secondary rates**.
Employer	An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **funding target** values for each employer are individually tracked, together with its **Primary rate** at each **valuation**.
Funding target	The actuarially calculated present value of all pension entitlements of all **members** of the Fund, built up to date. This is compared with the present market value of Fund assets to derive the **deficit**. It is calculated on a chosen set of **actuarial assumptions**.
Gilt	A UK Government bond, ie a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but their main use in funding is as an objective measure of solvency.
Guarantee /	A formal promise by a third party (the guarantor) that it will meet any

guarantor pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's **covenant** to be as strong as its guarantor's.

Letting employer An employer which outsources or transfers a part of its services and workforce to another employer (usually a contractor). The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer. A letting employer will usually be a local authority, but can sometimes be another type of employer such as an Academy.

LGPS The Local Government Pension Scheme, a public-sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 101 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.

Maturity A general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.

Members The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).

Primary contribution rate The employer contribution rate required to pay for ongoing accrual of active members' benefits (including an allowance for administrative expenses). See Appendix D for further details.

Profile The profile of an employer's membership or liability reflects various measurements of that employer's **members**, ie current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.

Rates and Adjustments Certificate A formal document required by the LGPS Regulations, which must be updated at least every three years after the formal **valuation**. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three-year period until the next valuation is completed.

Scheduled Bodies Types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These

include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).

Secondary contribution rate The difference between the employer's actual and **Primary contribution rates**. In broad terms, this relates to the shortfall of its asset share to its **funding target**. See Appendix D for further details.

Stabilisation Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund. Different methods may involve: probability-based modelling of future market movements; longer deficit recovery periods; higher discount rates; or some combination of these.

Valuation An actuarial investigation to calculate the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too. This is normally carried out in full every three years (last done as at 31 March 2016), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.

Employer/Pool Name	Primary rate 2017/18	Secondary rate 2017/18	Primary rate 2018/19	Secondary rate 2018/19	Primary rate 2019/20	Secondary rate 2019/20
LBBD	17.8%	6.7%	17.8%	6.70%	17.8%	6.70%
University of East London*	18.0%	8.60%	18.0%	8.60%	18.0%	8.60%
Barking College	19.0%	6.30%	19.0%	6.30%	19.0%	6.30%
Barking and Dagenham CAB	28.8%	14.2%	28.8%	14.2%	28.8%	14.2%
Broadway Theatre	29.2%	1.90%	29.2%	1.90%	29.2%	1.90%
Elevate	25.6%	-4.3%	25.6%	-4.3%	25.6%	-4.30%
Laing O'Rourke	23.5%	4.60%	23.5%	4.60%	23.5%	4.60%
Thames View Infant Academy	18.1%	0.00%	18.1%	0.00%	18.1%	0.00%
Riverside Free School	17.3%	0.00%	17.3%	0.00%	17.3%	0.00%
Dorothy Barley Academy	18.7%	0.00%	18.7%	0.00%	18.7%	0.00%
Goresbrook School	15.6%	0.00%	15.6%	0.00%	15.6%	0.00%
Thames View Junior Academy	18.5%	1.50%	18.5%	1.50%	18.5%	1.50%
Sydney Russell Academy	18.8%	1.70%	18.8%	1.70%	18.8%	1.70%
Riverside Primary	17.6%	0.00%	17.6%	0.00%	17.6%	0.00%
Riverside SEN School	17.7%	0.00%	17.7%	0.00%	17.7%	0.00%
Partnership Learning	18.1%	3.80%	18.1%	3.80%	18.1%	3.80%
Elutec	18.8%	1.20%	18.8%	1.20%	18.8%	1.20%
Warren School Academy Pool	20.4%	4.00%	20.4%	4.00%	20.4%	4.00%

- Rates agreed subject to collateral being agreed with the UEL as a security for the outstanding deficit.

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London Borough of Barking and Dagenham Pension Fund

INVESTMENT STRATEGY STATEMENT

January 2017

1. Introduction

This is the Investment Strategy Statement (ISS) produced by London Borough of Barking and Dagenham as administering authority of the London Borough of Barking and Dagenham Pension Fund ("the Fund"), to comply with the regulatory requirements specified in The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 and the Statutory Guidance on Preparing and Maintaining an Investment Strategy Statement issued by the Department for Communities and Local Government (DCLG) in September 2016.

The Regulations (regulation 7) set out that the ISS must include:

a) *a requirement to invest fund money in a wide variety of investments;*
b) *the authority's assessment of the suitability of particular investments and types of investments;*
c) *the authority's approach to risk, including the ways in which risks are to be assessed and managed;*
d) *the authority's approach to pooling investments, including the use of collective investment vehicles and shared services;*
e) *the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and*
f) *the authority's policy on the exercise of the rights (including voting rights) attaching to investments.*

This ISS seeks to address the Requirements of Regulation 7 and the Statutory Guidance of September 2016.

The ISS replaces the Statement of Investment Principles and, although it is a similar document, there are several additional disclosures that need to be covered including:

- The removal of the investment restrictions contained in schedule 1of the LGPS (Management and Investment of Funds) Regulations 2009;
- Fund's approach to pooling investments and shared services;
- How social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and
- The Fund's assessment of the suitability of all major asset classes.

The Statement is subject to review from time to time and will certainly be reviewed within six months of any material change in investment policy or other matters as required by law. As a minimum the ISS must be reviewed every three years. The ISS has been produced following a complete review of the Fund's investment strategy and incorporates the requirements of the Funding Strategy Statement. In preparing this Statement the administrating authority has taken and considered advice from the Fund's Investment Advisor, Aon Hewitt, and from the Fund's Independent Investment Advisor, John Raisin Financial Services Limited.

A copy of the ISS can be found at: www.lbbdpensionfund.org
For further information please contact David Dickinson: david.dickinson@lbbd.gov.uk.

2. Overall Responsibilities

A full explanation of the Fund's governance arrangements can be found in the Council's Constitution Part C – Responsibility for Functions – Our Scheme of Delegation - Section M – The Pension Panel published on the Council's website: http://www.lbbd.gov.uk/CouncilandDemocracy/Documents/Constitution/const-c-section-m.pdf

3. Investment Responsibilities

The Administering Authority the Council has delegated responsibility for the administration of the Fund to the Section 151 officer, advised by the Pension Panel and after taking expert advice from the Fund's Investment Advisor (Aon Hewitt) and the Fund's Independent Advisor, John Raisin Financial Services Limited.

As at 31 December 2016 the Pension Panel comprised:

Pension Panel Voting Members

Chair:	Councillor Dominic Twomey
Deputy:	Councillor Faraaz Shaukat
	Councillor Sade Bright
	Councillor Edna Fergus
	Councillor James Ogungbose
	Councillor John White
	Councillor Jeff Wade

Non-Voting Members

Union Representative:	Gavin Palmer (GMB)
Member Representative:	Bernie Hanreck
Employer Representative:	Dusty Amroliwala (UEL)

In preparing the ISS the Panel has consulted with the administrating authority and other principal employers within the Fund and has taken and considered proper written advice from the Aon Hewitt and John Raisin Financial Services Limited.

In Appendix A, the Panel has set out details of the extent to which the Fund complies with the six principles set out in the Chartered Institute of Public Finance and Accountancy's (CIPFA) publication, 'Investment Decision Making and Disclosure in the Local Government Pension Scheme 2012 – a guide to the application of the 2008 Myners Principles to the management of LGPS funds'.

Although under the LGPS Investment Regulations 2016 an Administering Authority is no longer required to report the extent of their compliance against the Myners Principles, the London Borough of Barking and Dagenham has decided to continue to report this, as an appendix to the ISS, as it considers this to be both good governance practice and an element of good investment practice.

4. Fund Objective

The primary objective of the Fund is to provide pension and lump sum benefits for members on their retirement and/or benefits on death, before or after retirement, for their dependents, on a defined benefits basis.

The Panel aims to fund the Fund in such a manner that, in normal market conditions, all accrued benefits are fully covered by the value of the Fund's assets and that an appropriate level of employer contributions is set to meet the cost of future benefits accruing. For employee members, benefits will be based on service completed but will take account of future salary increases.

This funding position will be reviewed at each triennial actuarial valuation of the Fund, or more frequently as required. The most recent triennial valuation took place in 2016, with the contribution rates effective from 1 April 2017.

5. Investment Strategy

The Panel has translated its objectives into a suitable strategic asset allocation benchmark for the Fund (Appendix B). Within the strategic benchmark the investment structure adopted by the Panel comprises a mix of segregated and pooled manager mandates, including actively managed and passive mandates. The Fund benchmark is consistent with the Panel's views on the appropriate balance between generating a satisfactory long-term return on investments whilst taking account of market volatility and risk and the nature of the Fund's liabilities. All day to day investment decisions have been delegated to the Fund's authorised investment managers.

The Panel monitors investment strategy relative to the agreed asset allocation benchmark. The investment strategy will be reviewed at least every three years following actuarial valuations of the Fund.

6. Pooling Investments (Regulation 7(2)(d) - The approach to pooling investments, including the use of collective investment vehicles and shared services).

The Fund has formally agreed to join the London Collective Investment Vehicle (LCIV) as part of the Government's pooling agenda. The LCIV is fully authorised by the FCA as an Alternative Investment Fund Manager ("AIFM") with permission to operate a UK based Authorised Contractual Scheme fund (the "ACS Fund"). The ACS Fund, which is tax transparent in the context of international tax treaties, will be structured as an umbrella fund with a range of sub-funds providing access, over time, to the full range of asset classes that the boroughs require to implement their investment strategies.

For all future investments, where there is a suitable asset class provided, the Fund will seek to utilise the LCIV. Unless prohibited by Regulation or Statutory Guidance where the asset class is not available via the LCIV and it is not appropriate to access it via a passive allocation, the Fund will seek clarification from DCLG as to whether the Fund can tender for a suitable manager.

Current LCIV allocations

As at 31 December 2016 the Fund had nearly a third of its assets invested through the LCIV, including:

- Two Diversified Growth Managers: Newton, Pyrford
- One active equity manager: Baillie Gifford.

Passive Investments via Life Funds

Approximately a fifth of the Fund's investments are via passively managed Life Funds. LIFE Funds are exempt from being included within the pooling arrangements. This allocation will be reviewed annually.

Current Partnerships

The Fund is invested in three separate partnerships including one in an alternatives investment with M&G / Prudential and two with the Fund's infrastructure manager Hermes GPE. The size of the M&G / Prudential investment is a maximum of 1% of the Fund's assets under management.

The infrastructure investment is accessed via two partnerships, with a limit of 10%. The allocation was agreed by the pension panel on 19 June 2012 and subsequently increased to 10.0% at the 23 March 2015 Panel, with an investment period limited to 17 years. From 1 April 2017, the split allocation will be combined into one LLP.

The Fund has a 10% allocation to LLPs and these investments will remain outside of the LCIV.

Diversified Alternatives

The Fund has a 7% investment in Diversified Alternatives, including Hedge Funds and Private Equity via Aberdeen Asset Management. These illiquid assets will not be moved to the LCIV until there is an adequate alternative provided by LCIV.

Credit, Property and Equity Income Strategy

The Fund has approximately 30% of its assets invested in credit, property, and an equity income strategy. There is the potential for these allocations to be moved to the LCIV and these holdings will be reviewed as and when suitable alternatives are provided by the LCIV. The review will consider the strategy, the assets held, the risks and the suitability of the strategy within the overall Fund prior to any investment agreement being made and proper advice will be sought from the Fund's advisors. Where an alternative is suitable then transition arrangement will be arranged.

If the alternative strategy is not suitable then the current manager will remain. If there is a requirement for the Fund to move from the manager to the LCIV then an

alternative solution will be to seek to access a suitable passive strategy through a LIFE Fund.

7. Funding Strategy Statement

There are close links between the ISS and the Funding Strategy Statement, which sets out the Fund's approach to funding its pension liabilities and the resulting impact on employer contribution rates. The Funding Strategy Statement is available on the Fund's website: www.lbbdpensionfund.org

8. Types of investment to be held

The Fund may invest in quoted and unquoted securities of UK and overseas markets, including equities, fixed interest and index linked bonds, cash, property and commodities, infrastructure and diversified alternatives, either directly or through pooled funds.

The Fund may also make use of contracts for differences and other derivatives either directly or in pooled funds investing in these products, for the purpose of efficient portfolio management or to hedge specific risks. The Panel considers all of these classes of investment to be suitable in the circumstances of the Fund.

The strategic asset allocation of the Fund includes a mix of asset types across a range of geographies in order to provide diversification of returns.

9. Statutory Investment Limits

Statutory maximum limits, as previously outlined in schedule 1 of the LGPS (Management and Investment of Funds) Regulations 2009 are no longer applicable. Instead this Fund will make asset allocation decisions based on a prudential approach to securing a diversified investment strategy.

The maximum percentage of the Fund's total value that the Fund will invest in each asset class is provided below and is subject to an annual review:

Equities	55%	Bonds	25%
Absolute Return	30%	Property	20%
Infrastructure	20%	Diversified Alternatives	20%
Cash	5%		

10. Balance between different kinds of investments

The Panel has appointed a number of investment managers all of whom are authorised under the Financial Services and Markets Act 2000 to undertake investment business.

The Panel, after seeking proper investment advice, has agreed specific benchmarks with each manager so that, in aggregate, they are consistent with the overall asset allocation for the Fund. The Fund's investment managers will hold a mix of investments which reflects their views relative to their respective benchmarks. Within

each major market and asset class, the managers will maintain diversified portfolios through direct investment or pooled vehicles.

In March 2017 an Asset Liability Review (ALR) was completed by Aon, with a training session held on 13 March 2017. Following the ALR a review of the strategy will be completed and the ISS updated to reflect any agreed changes.

11. Risk

The Fund is exposed to a number of risks which pose a threat to the Fund meeting its objectives. The principal risks affecting the Fund are:

Funding risks:

- Financial mismatch

  1. The risk that Fund assets fail to grow in line with the developing cost of meeting Fund liabilities.

  2. The risk that unexpected inflation increases the pension and benefit payments and the Fund assets do not grow fast enough to meet the increased cost.

- Changing demographics –The risk that longevity improves and other demographic factors change increasing the cost of Fund benefits.

- Systemic risk - The possibility of an interlinked and simultaneous failure of several asset classes and/or investment managers, possibly compounded by financial 'contagion', resulting in an increase in the cost of meeting Fund liabilities.

The Panel measures and manages financial mismatch in two ways. As indicated above, it has set a strategic asset allocation benchmark for the Fund. It assesses risk relative to that benchmark by monitoring the Fund's asset allocation and investment returns relative to the benchmark. It also assesses risk relative to liabilities by monitoring the delivery of benchmark returns relative to liabilities.

The Panel keeps under review mortality and other demographic assumptions which could influence the cost of the benefits. These assumptions are considered formally at the triennial valuation.

The Panel seeks to mitigate systemic risk through a diversified portfolio but it is not possible to make specific provision for all possible eventualities that may arise under this heading.

Asset risks

- Concentration - The risk that significant allocation to any single asset category and its underperformance relative to expectation would result in difficulties in achieving funding objectives.

- Illiquidity - The risk that the Fund cannot meet its immediate liabilities because it has insufficient liquid assets.

- Manager underperformance - The failure by the fund managers to achieve the rate of investment return assumed in setting their mandates

The Panel manages asset risks as follows:

It provides a practical constraint on Fund investments deviating greatly from the intended approach by setting itself diversification guidelines and by investing in a range of investment mandates each of which has a defined objective, performance benchmark and manager process which, taken in aggregate, constrains risk within the Panel's expected parameters. By investing across a range of assets, including quoted equities and bonds; the Panel has recognised the need for some access to liquidity in the short term. In appointing several investment managers, the Panel has considered the risk of underperformance by any single investment manager.

Other provider risk

- Transition risk - The risk of incurring unexpected costs in relation to the transition of assets among managers. When carrying out significant transitions, the Panel takes professional advice and considers the appointment of specialist transition managers.
- Custody risk - The risk of losing economic rights to Fund assets, when held in custody or when being traded.
- Credit default - The possibility of default of a counterparty in meeting its obligations.

The Panel monitors and manages risks in these areas through a process of regular scrutiny of its providers and audit of the operations they conduct for the Fund.

The Fund also maintains an extensive risk register, where risks the Fund is exposed to are considered, with appropriate action taken to mitigate the risk where possible.

12. Expected return on investments

Over the long term, the overall level of investment returns is expected to exceed the rate of return assumed by the actuary in funding the Fund.

13. Realisation of investments

The majority of the Fund's investments are quoted on major stock markets and may be realised relatively quickly if required. A proportion of the Fund's investments, including Property, Infrastructure and Diversified Alternatives, with 7%, 10% and 7% respective benchmark allocations, would take longer to be realised.

The overall liquidity of the Fund's assets is considered in the light of potential demands for cash.

14. Social, Environmental and Ethical Considerations (Regulation 7(2)(e) - How social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments)

The Fund is committed to being a long-term steward of the assets in which it invests and expects this approach to protect and enhance the value of the Fund in the long term. In making investment decisions, the Fund seeks and receives proper advice from internal and external advisers with the requisite knowledge and skills.

The Panel recognises that social, environmental and ethical considerations (SEE) are among the factors which investment managers will take into account, where relevant, when selecting investments for purchase, retention or sale. In addition, the Panel undertakes training on a regular basis and this will include training and information sessions on matters of social, environmental and corporate governance.

The Fund requires its investment managers to integrate all material financial factors, including corporate governance, environmental, social, and ethical considerations, into the decision-making process for all fund investments. It expects its managers to follow good practice and use their influence as major institutional investors and long-term stewards of capital to promote good practice in the investee companies and markets to which the Fund is exposed.

The Fund expects its external investment managers (and specifically the London CIV through which the Fund will increasingly invest) to undertake appropriate monitoring of current investments regarding their policies and practices on all issues which could present a material financial risk to the long-term performance of the fund such as corporate governance and environmental factors. The Fund expects its fund managers to integrate material ESG factors within its investment analysis and decision making.

Effective monitoring and identification of these issues can enable engagement with boards and management of investee companies to seek resolution of potential problems at an early stage. Where collaboration is likely to be the most effective mechanism for encouraging issues to be addressed, the Fund expects its investment managers to participate in joint action with other institutional investors as permitted by relevant legal and regulatory codes.

The Fund will invest on the basis of financial risk and return having considered a full range of factors contributing to the financial risk including social, environment and

governance factors to the extent these directly or indirectly impact on financial risk and return.

The Fund, in preparing and reviewing its ISS will consult with interested stakeholders including, but not limited to Fund employers, investment managers, Local Pension Board, advisers to the Fund and other parties that it deems appropriate to consult with.

Current Restrictions:

At the 12 March 2014 Panel Meeting, Members agreed a policy to restrict direct investment in tobacco but allow indirect investments in tobacco through pooled funds for both passive and active managers.

This restriction will be reviewed as part of each Investment Strategy Review.

15. Exercise of Voting Rights (Regulation 7(2)(f) - The exercise of rights (including voting rights) attaching to investments)

The Fund recognises the importance of its role as stewards of capital and the need to ensure the highest standards of governance and promoting corporate responsibility in the underlying companies in which its investments reside. The Fund recognises that ultimately this protects the financial interests of the Fund and its ultimate beneficiaries. The Fund has a commitment to actively exercising the ownership rights attached to its investments reflecting the Fund's conviction that responsible asset owners should maintain oversight of the companies in which it ultimately invests recognising that the companies' activities impact upon not only their customers and clients, but more widely upon their employees and other stakeholders and wider society.

The Panel has delegated the exercise of voting rights to the investment manager(s) on the basis that voting power will be exercised by them with the objective of preserving and enhancing long term shareholder value. Accordingly, the manager(s) has produced written guidelines of its process and practice in this regard. The manager(s) is encouraged to vote in line with its guidelines in respect of all resolutions at annual and extraordinary general meetings of companies.

Investments through the London CIV are covered by the voting policy of the CIV which has been agreed by the Pensions Sectoral Joint Committee. Voting is delegated to the external managers and monitored on a quarterly basis. The CIV will arrange for managers to vote in accordance with voting alerts issued by the Local Authority Pension Fund Forum (LAPFF) as far as practically possible to do so and will hold managers to account where they have not voted in accordance with the LAPFF directions.

The Fund will incorporate a report of voting activity as part of its Pension Fund Annual report which is published on the Council and Pension Fund website:

a) The Fund has issued a Statement of Compliance with the Stewardship Code which can be found on the Council / Pension Fund website and has also

agreed to become a signatory to the Code in accordance with the Statutory Guidance issued in September 2016.

b) The Fund has reviewed the London CIV Statement of Compliance with the Stewardship Code and has agreed to adopt this Statement.

In addition, the Fund expects its investment managers to work collaboratively with others if this will lead to greater influence and deliver improved outcomes for shareholders and more broadly.

The Fund, through its participation in the London CIV, will work closely with other LGPS Funds in London to enhance the level of engagement both with external managers and the underlying companies in which invests. In addition the Fund:

a) is a member of the LAPFF and in this way joins with other LGPS Funds to magnify its voice and maximise the influence of investors as asset owners
b) gives support to shareholder resolutions where these reflect concerns which are shared and represent the Fund interest
c) joins wider lobbying activities where appropriate opportunities arise.

16. Stock Lending

The policy on stock lending reflects the nature of the mandates awarded to investment managers by the Panel, which include both pooled and segregated mandates.

The Panel has considered its approach to stock lending, taking advice from its investment advisers. After consideration of that advice, the Panel has given authority to its custodian to lend stocks (principally equities) within its mandates subject to agreed collateral being provided and an overall restriction that the proportion of Fund assets that are available to be lent at any time is limited to 25% of Fund assets.

Stock lending does not prevent any investments from being sold. Safeguards are in place to reduce the risk of financial loss to the Fund in the event of default. These safeguards include receiving liquid collateral in excess of the value of the loan, indemnity agreement with the lending agent and regular reviews of credit-worthiness of potential borrowers. The Panel reviews its policy on stock lending (including the amount and type of collateral used) on a regular basis.

17. Safekeeping of Assets

A global custodian is employed to ensure the safekeeping of investments.

18. Performance measurement

An independent provider is employed to calculate performance for the Funds. Each quarter, the Panel considers the performance of the combined assets and each manager's portfolio against their respective benchmark. The Panel review performance on an annual basis.

19. Stewardship Code

The UK Stewardship Code (SC) aims to enhance the quality of engagement between institutional investors and companies to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities. The Code sets out good practice on engagement with investee companies to which the FRC believes institutional investors should aspire and operates on a 'comply or explain' basis. The FCA requires UK authorised asset managers to report on whether or not they apply the Code. . In accordance with the Statutory Guidance of September 2016 the Fund has determined that it should become a Signatory to the Code. The Fund's compliance with the UK SC is included as Appendix C.

20. Additional Voluntary Contributions (AVCs)

The Panel gives members the opportunity to invest in a range of vehicles at the members' discretion. Currently AVC is managed by Prudential Plc.

Signed For and on Behalf of the Pension Panel of the London Borough of Barking and Dagenham Pension Fund

________________________________ ________________________________

Claire Symonds Chief Operating Officer

Appendix A: Myners Principles

The Pension Panel considers that its practices are compliant with the CIPFA principles for Investment Decision Making in LGPS. The 6 principles are:

1) Effective decision making
2) Clear objectives
3) Risk and liabilities
4) Performance assessment
5) Responsible ownership
6) Transparency and reporting

The Panel's self-assessment of adherence to the principles is shown below

Principles	Response on Adherence
Principle 1 Effective Decision Making: Administering authorities should ensure: • That decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to make them effectively and monitor their implementation; and • That those persons or organisations have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.	**Compliant** Decisions are taken by the Pension Panel, which is responsible for the management of the Fund. The Panel has support from Council officers with sufficient experience to assist them. The Panel also seeks advice from professional actuarial and investment advisers to ensure it can be familiar with the issues concerned when making decisions. The Panel is able to make robust challenges to advice and is aware of where potential conflicts of interest may reside within the Panel and in relation to service providers.

Principle 2 Clear objectives: • An overall investment objective should be set out for the fund that takes account of the scheme's liabilities, the potential impact on local tax payers, the strength of the covenant for non-local authority employers, and the attitude to risk of both the administering authority and scheme employers, and these should be clearly communicated to advisers and investment managers.	**Compliant** The Panel has established objectives for the Fund which takes account of the nature of Fund liabilities and the contribution strategy. This involved discussions with the Actuary to enable the Panel to set the overall risk budget for the Fund. This is reflected in the investment mandates awarded to the asset managers. There is dialogue with admitted bodies within the Fund in relation to the contributions they pay, their capacity to pay these contributions and the level of guarantees they can provide.
Principle 3 Risk and liabilities: • In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities. • These include the implications for local tax payers, the strength of the covenant for participating employers, the risk of their default and longevity risk.	**Compliant** The investment strategy is considered in the light of the nature of the Fund liabilities, the timescale over which benefits will be paid, and financial and demographic factors affecting the liabilities, such as inflation and improving longevity. The Panel and Council officers have discussed the contribution strategy with the Actuary taking account of the strength of covenant of the Council and its long term horizon. Discussions have also taken place with admitted bodies in relation to the affordability of contributions and the strengths of their covenants.
Principle 4 Performance assessment: • Arrangements should be in place for the formal measurement of performance of the investments, investment managers and advisers. • Administering authorities should also periodically make a formal assessment of their own effectiveness as a decision-making body and report on this to	**Compliant** The performance of the Fund and its individual managers are monitored on a regular basis. The quality of advisers is assessed on a qualitative basis but is not formally measured. Advisers are subject to periodic re-tender. *The Fund's contracts with its advisers are regularly market tested.* *The Pension Panel will carry out a formal process to measure its own effectiveness and will report this to the Pensions Panel on a*

scheme members.	*regular basis.* *Training and attendance of members of the Pensions Panel are monitored and reported on annually.*
Principle 5 Responsible Ownership: Administering authorities should • recognise, and ensure that their partners in the investment chain adopt, the FRC's UK Stewardship Code • include a statement of their policy on responsible ownership in the Investment Strategy Statement. • Report periodically to scheme members on the discharge of such responsibilities.	***Compliant*** The Pensions Panel encourages its investment managers to adopt the Financial Reporting Council (FRC's) UK Stewardship Code but not all managers may necessarily comply fully with the Code's principles This Investment Strategy Statement includes a statement on the Fund's policy on responsible ownership. The Fund has determined to become a Signatory to the FRC Code in accordance with the Statutory Guidance issued by the DCLG in September 2016 .
Principle 6 Transparency and Reporting: Administering authorities should • act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives. • Should provide regular communication to scheme members in the form they consider most appropriate.	**Compliant** The Pension Panel maintains minutes of meetings which are available on the Council website. The Council holds a formal annual meeting for members and also meets periodically with sponsoring employer bodies. A member representative attends Panel meetings. The Investment Strategy Statement is published on the Council website and is available to members on request. Other information on the Scheme is available to members on the Council website.

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Appendix B: Strategic Asset Allocation

The strategic asset allocation of the Fund, together with control ranges and the benchmark index for each asset class is as follows:

Asset Class	***Strategic Allocation As at 31 March 2016 %***	***Strategy Control Range %***	***Benchmark Index***
Global Equities	*46*	*42.0–51.0*	*MSCI AC World Index*
TOTAL EQUITIES	***46***	***42.0–51.0***	*MSCI AC World Index*
UK Bonds	*5*	*4.0-6.0*	*Merrill Lynch Sterling Broad Market*
Global Credit	***8***	***6.0-10.0***	*Target Return 6%*
Non-investment grade bonds		*Up to 75%*	
Emerging markets debt		*Up to 30%*	
Non-rated debt (rated internally)		*Up to 10%*	
Securitised Debt		*Up to 25%*	
TOTAL BONDS	***13***	***11.0–15.0***	
Absolute Return	***17***	***15.0–19.0***	*Pyrford: RPI +5% p.a. Newton: 1 mth LIBOR +4% p.a*
Property	***7***	***6.0–9.0***	*IPD UK Property Fund Indices All Balanced Property Funds*
Diversified Alternatives	***7***	***6.0-10.0***	*3mth LIBOR plus 4%*
Infrastructure	***10***	***4.0–11.0***	*Target yield 5.9% per annum*
Senior Loans*	***0***	***0.0-1.0***	*Target Return 5-6%*
Cash	***0***	***0.0–3.0***	
TOTAL ASSETS	***100***	***-***	

** Senior Loans Strategic Allocation reduced to 0% as holding is under 0.5%.*

Appendix C: Statement of Compliance with UK Stewardship Code

<table>
<tr><td>Principle 1
Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.</td><td>Stewardship is seen as part of the responsibilities of share ownership, and is therefore an integral part of the Fund's investment strategy.

The Pension Panel actively monitor the fund managers through quarterly performance analysis, annual and periodic meetings with the individual fund managers and through direct monitoring by the officers, which includes monitoring and reporting on:

• Fund manager performance;
• Investment Process compliance and changes;
• Changes in personnel (joiners and leavers);
• Significant portfolio developments;
• Breaches of the IMA / Restrictions;
• Business wins and losses; and
• Corporate and other issues.

Voting is delegated to Fund Managers through the Investment Management Agreement (IMA).

Baillie Gifford, UBS and Kempen take direct responsibility for stewardship issues, voting and engagement, in the funds which they manage on our behalf. These managers publish Statements of Compliance with the Stewardship code.

Details are available on their websites at

www.bailliegifford.com/pages/UKInstitutional/CorporateGovernance/CorporateGovernaceSRI.aspx

http://www.ubs.com/global/en/about_ubs/corporate_covernance.htm

http://www.kempen.nl/over_kempen.aspx?id=27770</td></tr>
<tr><td>Principle 2
Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.</td><td>We also encourage the asset managers employed by the Funds to have effective policies addressing potential conflicts of interest.

In respect of conflicts of interest within the Fund, Pension Panel members are required to make declarations of interest prior to Panel meetings.

The Funds' overriding obligation is to act in the best financial interests of the members.</td></tr>
<tr><td>Principle 3
Institutional investors should monitor their investee companies.</td><td>Day-to-day responsibility for managing the Fund's investments is delegated to the relevant fund managers, who are expected to monitor companies, intervene where necessary, and report back regularly on activity undertaken.
Reports from fund managers on voting and engagement activity will be reported to the Panel on a quarterly basis from June 2013.
Concerns are raised directly with the fund managers and issues raised are reported back to the Panel at the subsequent Panel meeting.
Fund manager Internal Control reports are monitored, with breaches reported back to the Panel.
Where the Fund is directly invested, such as infrastructure, members of the Panel and officers are able to attend their AGM.</td></tr>
</table>

Principle 4 *Institutional investors should establish clear guidelines on when and how they will escalate their stewardship activities.*	*As highlighted above, responsibility for day-to-day interaction with companies is delegated, including the escalation of engagement when necessary.* *We expect the approach to engagement on our behalf to be value orientated and focussed on long term profitability. We expect Kempen, Baillie Gifford and UBS to disclose their guidelines for such activities in their own statements of adherence to the Code. Their guidelines for such activities are expected to be disclosed in their own statement of adherence to the Stewardship Code.* *Consistent with our fiduciary duty to beneficiaries, we also participate in shareholder litigation. We pursue compensation for any losses sustained because of inappropriate actions by company directors in order to encourage improved conduct in the future.*
Principle 5 *Institutional investors should be willing to act collectively with other investors where appropriate*	*The Fund seeks to work collaboratively with other institutional shareholders in order to maximize the influence that it can have on individual companies.* *The Fund is a member of the Local Authority Pension Fund Forum (LAPFF) which seeks to promote the highest standards of corporate governance and corporate responsibility amongst investee companies.* *Where possible, the Fund seeks to exercise its voting rights attaching to its non-UK equity holdings by delegation through Power of Attorneys.*
Principle 6 *Institutional investors should have a clear policy on voting and disclosure of voting activity.*	*The emphasis of our voting policy is to promote best practice. We seek to vote on all shares held.* *Our preference is for managers to vote on the Funds behalf and for responsible stewardship to be integral to the investment decision making process.* *We are comfortable with delegation of voting to Baillie Gifford and Kempen for the funds they manage.UBS vote on our behalf because the investment is in a passive pooled fund. The managers' voting policies can be found at the websites mentioned above.*
Principle 7 *Institutional investors should report periodically on their stewardship and voting activities.*	*We will seek to report annually on stewardship activity through a specific section in the Funds' annual report and accounts and on our website.* *We also report annually on stewardship issues to the Pension Panel.*

Appendix 3: Investment Strategy Statement (ISS) Regulatory Requirements

JOHN RAISIN FINANCIAL SERVICES LIMITED

The Local Government Pension Scheme Investment Regulations 2016 - a paper by the Independent Advisor February 2017

Background

On 1 November 2016, ***The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016*** (the LGPS Investment Regulations 2016) came into force. This paper examines and explains the background to the Regulations, their contents and implications.

In November 2015, the Government had issued a Consultation proposing reform of the LGPS Investment Regulations. This Consultation proposed a number of significant changes including:

- Revoking and replacing the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as Amended)

- Removing Schedule 1 to the 2009 Regulations which placed % based restrictions on the nature of investments LGPS Funds could make and replacing this with a *"prudential person"* approach similar to that which applies to private sector Defined Benefit Pension Schemes. Under the proposed revised approach, it would be a matter for each LGPS Fund to determine the mix and balance of its investments taking risk into account

- Further deregulation particularly in relation to the appointment and review of external Investment Managers

- The replacement of the existing requirement for each LGPS Fund to define its investment strategy in a Statement of Investment Principles (SIP) with a requirement to prepare and approve an Investment Strategy Statement (ISS)

- A requirement for each LGPS Fund to define its approach to Investment Pooling (part of draft Regulation 7)

- A proposed power for the Secretary of State (draft Regulation 8) to issue directions to an LGPS Fund in relation to investment matters where the Secretary of State had determined that the Fund had failed to have regard to the requirements of regulation and guidance

The Consultation also included a specific question seeking views on the use of derivatives. The extent to which/circumstances in which LGPS Funds could utilise derivatives had been unclear under the 2009 Investment Regulations.

Government response to the Consultation

In September 2016, the Government responded to the Consultation by issuing three documents. These were the 2016 Investment Regulations, Statutory Guidance to accompany the new Regulations and the formal response to the Consultation.

- ***The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016*** which were laid before Parliament on 23 September 2016 and came into effect on 1 November 2016 were very closely based on the Draft Regulations issued in November 2015. These include the introduction of a *"prudential person"* approach to LGPS investment and also a clearly positive emphasis on both Environmental, Social and Governance (ESG), and Stewardship considerations. The Regulations confirm the Government's intention to proceed with Investment Pooling and the introduction of a power of intervention (Directions) by the Secretary of State in specified circumstances

- The Statutory Guidance entitled ***Local Government Pension Scheme Guidance on Preparing and Maintaining an Investment Strategy Statement*** provides guidance for LGPS Funds in preparing their Investment Strategy Statement in accordance with Regulation 7 of the 2016 Investment Regulations. Guidance is given in respect of each of the six component parts of Regulation 7. This Statutory Guidance also provides context and clarification in respect of the issuing of Directions by the Secretary of State to an individual LGPS Fund under Regulation 8 of the 2016 Investment Regulations. Based on the Guidance such a Direction would only be issued if a Fund was in clear breach of the Regulations or Statutory Guidance and after careful consultation including with the relevant Fund.

- The ***Government response to the Consultation*** of November 2015.

The LGPS Investment Regulations 2016

There are 12 individual Regulations in the LGPS Investment Regulations 2016. Significant changes as compared to the LGPS Investment Regulations 2009 (As Amended) relate to:

Definition of Investment

Regulation 3 of the 2016 Regulations provides a revised definition of *"investment."* Overall the definition of *"investment"* in the 2016 Regulations is less complex than that in the 2009 Regulations. The new Regulations remove the previous uncertainty around the use of derivative instruments. Unlike the 2009 Regulations the 2016 Regulations specifically list *"derivatives"* as a permissible investment.

Investment Strategy Statement (which includes Asset Allocation decisions, Investment Pooling, ESG and Stewardship considerations)

Regulation 7 of the 2016 Regulations introduces the requirement for each LGPS Fund to formulate an **Investment Strategy Statement (ISS).** This document

replaces the Statement of Investment Principles (SIP) required under the 2009 Regulations.

As proposed in the November 2015 Consultation the limits in respect of % allocations to particular investments contained in Schedule 1 of the 2009 Investment Regulations are not carried forward to the 2016 Regulations. LGPS Funds now have the freedom to implement a *"prudential person"* approach to their Investment Strategy approach. They must however comply with Regulation 7 of the 2016 Investment Regulations and Guidance issued by the Secretary of State. Such Guidance was issued in September 2016 and may subsequently be revised.

Regulation 7(2) states: *The authority's investment strategy must include –*

a) a requirement to invest fund money in a wide variety of investments;

b) the authority's assessment of the suitability of particular investments and types of investments;

c) the authority's approach to risk, including the ways in which risks are to be assessed and managed;

d) the authority's approach to pooling investments, including the use of collective investment vehicles and shared services;

e) the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and

f) the authority's policy on the exercise of the rights (including voting rights) attaching to investments.

The Guidance issued by the Secretary of State in September 2016 includes six pages of Guidance in relation to the preparation of the ISS under Regulation 7(2).

The 2016 Investment Regulations and Guidance provide the freedom to LGPS Funds to invest in such assets as they consider appropriate through the removal of Schedule 1 to the 2009 Investment Regulations. The Regulations and Guidance also encourage LGPS Funds to carefully and proactively consider their strategic asset allocations. Whereas the 2009 Regulations merely required the SIP to cover *"the types of investments to be held"* Regulation 7(2)(a) of the 2016 Regulations state that a Fund's ISS must include "*a requirement to invest fund money in a wide variety of investments"*

The Guidance of September 2016 clearly encourages LGPS Fund's to adopt a genuinely diversified investment strategy and to avoid over reliance on any particular asset class and refers to a wide range of potential asset classes. It is however stated that *"this guidance does not purport to prescribe the specific asset classes over which fund monies must be diversified. This remains a decision for the individual administering authorities to make. Administering authorities are expected to be able to demonstrate that those responsible for making investment decisions have taken*

and acted on proper advice and that diversification decisions have been taken in the best long term interest of scheme beneficiaries."

In clear contrast to the 2009 Regulations the 2016 Regulations positively promote an Environmental, Social and Governance (ESG) approach. Regulation 7(2)(e) states a Fund's investment strategy must include *"the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments."* The 2009 Regulations had a very different emphasis stating that the SIP must cover *"the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments."*

The Guidance of September 2016 further positively promotes an ESG emphasis and includes the following statement *"The law is generally clear that schemes should consider any factors that are financially material to the performance of their investments, including social, environmental and corporate governance factors…"* Furthermore the guidance states *"Although schemes should make the pursuit of a financial return their predominant concern, they may also take purely non-financial considerations into account provided in doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision."*

The September 2016 Guidance also positively promotes social impact investing including the statement *"……some part of the financial return may be foregone in order to generate the social impact. These investments will also be compatible with the prudent approach providing administering authorities have good reason to think scheme members share their concern for social impact, and there is no risk of significant financial detriment to the fund."*

In relation to ESG issues the Guidance states *"the Government has made it clear that using pension policies to pursue boycotts, disinvestment and sanctions against foreign nations and UK defence industries are inappropriate, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government."* This proposal which was contained in the Consultation of November 2015 resulted in a large response to the Consultation. 98% of the 23,516 responses received were from members of the public primarily in response to this proposal. The Guidance on *"…boycotts, disinvestment and sanctions…."* is however extremely unlikely to have any impact on the investment strategy of any individual LGPS Fund as the pursuit of a financial return is the primary criteria against which investment decisions must be made. The primacy of the financial return criteria has always been known to and abided by in the case of LGPS Funds and therefore it would seem unnecessary for the Government to have included the paragraph on boycotts, disinvestments and sanctions in the Guidance of September 2016.

In contrast to the 2009 Investment Regulations the 2016 Regulations by virtue of Regulation 7(2)(f) (in the words of the Guidance document) *"requires every administering authority to formulate a policy that reflects their stewardship responsibilities."* The Guidance positively promotes active stewardship stating *"Stewardship aims to promote the long term success of companies…. Stewardship activities include monitoring and engaging with companies…. Engagement by*

administering authorities is purposeful…." The Guidance further states that *"authorities are encouraged to consider the best way to engage with companies to promote their long term success….."*

Notably the Guidance states that individual LGPS Funds *"should"* become signatories to the UK Stewardship Code *"and state how they implement the seven principles and guidance of the Code, which apply on a "comply or explain" basis"*. This Code which was issued by the Financial Reporting Council in July 2010 and revised in September 2012 aims to enhance the quality of engagement between investors and companies. This also represents a significant development as (based on research undertaken by the author of this paper) no more than 16 out of the 89 Administering Authorities in England and Wales had become signatories to the Code prior to the DCLG issuing its Guidance of September 2016. Furthermore the Guidance states LGPS Funds *"Should publish a report of voting activity as part of their pension fund annual report…."*

Regulation 7(2)(d) and the associated Guidance incorporate the requirement for LGPS Funds to delegate, in due course, the implementation of their Investment Strategy to an Investment Pool approved by the Government in accordance with criteria agreed by the Government. The Guidance requires each Fund to submit to the Scheme Advisory Board *"an annual report on the progress of asset transfers"* to their chosen Investment Pool.

In accordance with Regulation 7(6) each LGPS Fund must publish its (new) Investment Strategy Statement by 1 April 2017.

Directions by the Secretary of State

Regulation 8 provides that the Secretary of State may issue a Direction in relation to a LGPS Fund's investment functions if (s)he *"is satisfied that the authority is failing to act in accordance with guidance issued under regulation 7(1)."* The Guidance of September 2016 both provides an explanation for the introduction of Regulation 8 and makes it clear that the power of intervention would only be used where, after due consultation and consideration, it is clear the Investment Regulations/Statutory Guidance have been breached. The Guidance *states "In relaxing the regulatory framework for scheme investments, administering authorities will be expected to make their investment decisions within a prudential framework with less central prescription. It is important therefore that the regulations include a safeguard to ensure that this less prescriptive approach is used appropriately and in the best long term interests of scheme beneficiaries and taxpayers."*

The Guidance then states *"Where there is evidence to suggest that an authority is acting unreasonably, it may be appropriate for the Secretary of State to consider intervention, but only where this is justified and where the relevant parties have been consulted. Regulation 8 includes a number of safeguards, including full consultation with the relevant authority, to ensure that the proposed power is used appropriately, proportionately and only where justified by the evidence."*

The Guidance also states that *"The Secretary of State's power of intervention does not interfere with the duty of elected members under general public law principles to*

make investment decisions in the best long-term interest of scheme beneficiaries and taxpayers."

Based on the wording of Regulation 8 and the Guidance the power of intervention is definitely a reserve power which would not normally be utilised. A clear example of where it might however be applied is where a LGPS Fund refused to actively engage in Investment Pooling.

Investment Managers

The 2009 Investment Regulations contained four regulations relating to Investment Managers. These covered in detail their definition, choice, terms of appointment and review. In contrast Regulation 9 of the 2016 Investment Regulations alone covers the issue of Investment Managers. This represents a clear deregulation and granting of freedoms and flexibilities to individual LGPS Funds. Rather than the detailed prescriptive approach of the 2009 Regulations the new Regulation 9 simply requires that the Fund *"must reasonably believe that the investment manager's ability in and practical experience of financial matters make that investment manager suitably qualified to make investment decisions for it"* and that the *"authority must take proper advice in relation to the appointment and the terms on which the appointment is made."*

Transitional Provisions

Regulation 12(2) of the 2016 Regulations states that the requirements in relation to the maintenance of a Statement of Investment Principles and the restrictions on investment under Schedule 1 to the 2009 Investment Regulations *"continue to have effect"* until the Authority publishes its Investment Strategy Statement in accordance with (new) Regulation 7.

Conclusion

The 2016 LGPS Investment Regulations provide greater flexibilities and freedoms to LGPS Funds in terms of both their Investment Strategy and the appointment of Investment Managers (prior to Investment Pooling). The new Regulations place a clear emphasis on both ESG and Stewardship activity by the LGPS. The new Regulations put in place the regulatory framework for Investment Pooling in the LGPS. Although the new Regulations introduce an explicit power of intervention by the Secretary of State this is in the context of a less restrictive regulatory approach and clear guidelines/criteria which mean that such intervention would be rare and occur only where there was both a clear breach of the Regulations and after due consultation and consideration.

John Raisin - 10 February 2017

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"Strategic and Operational Support for Pension Funds and their Stakeholders"

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