

Supplementary Agenda

Audit & Governance Committee



Date & time
Monday, 25 July
2016 at 10.00 am

Place
Ashcombe Suite,
County Hall, Kingston
upon Thames, Surrey
KT1 2DN

Contact
Angela Guest
Room 122, County Hall
Tel 020 8541 9075

Chief Executive
David McNulty

SUPPLEMENTARY AGENDA

The following papers were not available for dispatch with the main agenda. Please bring these to the meeting with you.

- 7 SURREY PENSION FUND LOCAL GOVERNMENT PENSION SCHEME ACCOUNTS 2015/16 AND EXTERNAL AUDIT'S AUDIT FINDINGS REPORT** (Pages 1 - 74)

Grant Thornton as the Council's external auditors has completed their audit and the Pension Fund financial statements are being presented to this Committee to be approved prior to publication.

- 8 EXTERNAL AUDIT FEE LETTER - REMOVED**

This item has been **removed** from the agenda.

David McNulty
Chief Executive
Published: 15 July 2016

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AUDIT & GOVERNANCE COMMITTEE

25 July 2016

SURREY PENSION FUND LOCAL GOVERNMENT PENSION SCHEME ACCOUNTS 2015/16 AND GRANT THORNTON EXTERNAL AUDIT FINDINGS REPORT

SUMMARY AND PURPOSE:

This report presents the audited financial statements of the Pension Fund for the year ended 31 March 2016, in light of the County Council's obligations as the administering authority under the Local Government Pension Scheme (LGPS) Regulations.

The external auditor (Grant Thornton) expects to issue an unqualified opinion on the accounts.

Grant Thornton, as the Council's external auditor, has completed its audit and the Pension Fund financial statements are presented to this Committee to be approved prior to publication.

Annex A represents the primary statements and accompanying notes to the accounts.

The result of the external audit is reported in the Audit Findings for Surrey Pension Fund Report, which is presented at Annex B.

RECOMMENDATIONS:

The Committee is asked to:

- (i) Approve the 2015/16 Pension Fund financial statements in Annex A.
- (ii) Consider the content of the Audit Findings for Surrey Pension Fund Report in Annex B.
- (iii) Determine any issues that need to be referred to Cabinet in relation to the external auditor's conclusions and recommendations.
- (iv) Consider the content of the draft representation letter as set out in Annex C and authorise the Director of Finance to sign it on the council's behalf.

2015/16 PENSION FUND ACCOUNTS

1. Grant Thornton audits both the County Council and Pension Fund accounts and is required to present separate audit opinions on each.

2. During the audit, Grant Thornton identified some issues, which have led to a number of amendments being made to the 2015/16 draft financial statements and related notes to the accounts.
3. Annex A represents the Pension Fund primary statements.

2015/16 ANNUAL GOVERNANCE REPORT

4. The external auditor is required to report on the Pension Fund financial statements. The Audit Findings for Surrey Pension Fund Report is presented at Annex B and sets out a summary of the work carried out, the conclusions reached and recommendations made.
5. The Committee will note that the auditor is anticipating issuing an unqualified opinion on the financial statements

MANAGEMENT REPRESENTATION LETTER

6. It is considered good practice for those charged with governance to provide the external auditor with a letter of representation in respect of matters that are material to the financial statements, but appropriate audit evidence cannot reasonably be expected to exist.

IMPLICATIONS:

- A) Financial
There are no direct financial implications.
- B) Equalities
There are no direct equality implications.
- C) Risk management and value for money
Pension Fund risks are proactively monitored by officers and the Surrey Pension Fund Committee.

REPORT AUTHOR:

Phil Triggs, Strategic Finance Manager (Pension Fund & Treasury)

CONTACT DETAILS:

Phil Triggs 020 8541 9894 – phil.triggs@surreycc.gov.uk

Sources/Background papers:

Closure of Accounts Working Papers 2015/16

Statement of Accounts of the Surrey Pension Fund 205/16

SURREY PENSION FUND

ACCOUNTS 2015/2016

The accounts on the following pages give a stewardship report on the financial transactions of the Surrey Pension Fund during 2015/2016 and of the disposition of its assets at 31 March 2016.

Surrey County Council is responsible for administering a pension fund for staff employed by the county council, the 11 borough and district councils in Surrey and over a hundred other local bodies. The fund includes local authority employees within Surrey, except teachers, police and firefighters for whom separate pension arrangements apply.

The fund exists to provide pensions and other benefits for employees, their widows, widowers or dependants in accordance with Local Government Pension Scheme Regulations.

The number of employees in the fund and the number of pensioners as at 31 March 2015 and 31 March 2016 are:

31 Mar 2015		31 Mar 2016
32,851	Employees in the fund	34,072
22,481	Pensioners	23,197
33,833	Deferred pensioners	34,158
89,165	Total	91,427

Note 1: Description of the fund

The Surrey Pension Fund ('the fund') is part of the Local Government Pension Scheme (LGPS) and is administered by Surrey County Council. The Surrey Pension Fund is the reporting entity

The following description of the fund is a summary only. For more detail, reference should be made to the Surrey Pension Fund Annual Report 2015/16 and the underlying statutory powers underpinning the scheme, namely the Superannuation Act 1972 and the Local Government Pension Scheme (LGPS) Regulations.

a) General

The fund is governed by the Public Services Pensions Act 2013. The fund is administered in accordance with the following secondary legislation:

- The LGPS Regulations 2013 (as amended)
- The LGPS (Transitional Provisions, Savings and Amendment) Regulations 2014 (as amended)

It is a contributory defined benefit pension scheme administered by Surrey County Council to provide pensions and other benefits for pensionable employees of Surrey County Council, the borough and district councils in Surrey and a range of other scheduled and admitted bodies within the county area. Teachers, police officers and firefighters are not included as they come within other national pension schemes.

During 2015/16 the investment decision making and governance of the fund was undertaken by the Pension Fund Board, a committee of the Administering Authority, with representation on behalf of employers and members.

b) Membership

Membership of the LGPS is voluntary and employees are free to choose whether to join the scheme, remain in the scheme or make their own personal arrangements outside the scheme.

Organisations participating in the Surrey Pension Fund include:

- Scheduled bodies, which are local authorities and similar bodies whose staff are automatically entitled to be members of the fund.
- Admitted bodies, which are other organisations that participate in the fund under an admissions agreement between the fund and the relevant organisation. Admitted bodies include voluntary, charitable and similar bodies or private contractors undertaking a local authority function following outsourcing of services to the private sector.

c) Funding

Benefits are funded by contributions and investment earnings. Contributions are made by active members of the fund in accordance with the LGPS (Benefits, Membership and Contributions) Regulations 2007 and ranged from 5.5% to 12.5% of pensionable pay for the financial year ending 31 March 2016. Employee contributions are matched by employers' contributions which are set based on triennial actuarial funding valuations. The last such valuation was at 31 March 2013 and new rates applied from April 2014. Currently employer contribution rates range from 12.0% to 30.0% of pensionable pay.

d) Benefits

Prior to 1 April 2014, pension benefits under the LGPS were based on final pensionable pay and length of pensionable service.

	Service pre 1 April 2008	Service 1 April 2008 until 31 March 2014
Basis of pension	1/80 th of final salary	1/60th of final salary
Lump sum	Automatic lump sum 3 x salary Trade £1 of annual pension for £12 lump sum	No automatic lump sum Trade £1 of annual pension for £12 lump sum

There are a range of other benefits provided under the scheme including early retirement disability pensions and death benefits. For more details please refer to the Surrey Pension Fund website (<http://www.surreypensionfund.org>).

e) New LGPS Scheme 2014

The current UK national government requested Lord Hutton to chair a commission on the reform of public sector pensions. Following the publication of this report in 2011, a new scheme design for the LGPS was agreed. The new scheme commenced on April 1 2014.

The changes will not affect those who currently receive pension payments. All pension benefits built up to 31 March 2014 will be treated according to the existing scheme rules.

	Service 1 April 2008 until 31 March 2014	LGPS 2014 scheme
Basis of pension	Final salary	Career average revalued earnings
Accrual rate	1/60 th of salary	1/49 th of salary
Revaluation rate	No revaluation: based on final salary	Inflation rate: consumer prices index (CPI)
Pensionable pay	Pay excluding non-contractual overtime and non-pensionable additional hours	Pay including non-contractual overtime and additional hours for part time staff
Employee contribution	See below table	See below table
Normal pension age	65	Equal to the individual member's State Pension Age
Lump sum trade off	Trade £1 of annual pension for £12 lump sum	Trade £1 of annual pension for £12 lump sum
Death in service lump sum	3x pensionable payroll	3x pensionable payroll
Death in service survivor benefits	1/160th accrual based on Tier 1 ill health pension enhancement	1/160th accrual based on Tier 1 ill health pension enhancement
Ill Health Provision	Tier 1 - Immediate payment with service enhanced to Normal Pension Age Tier 2 - Immediate payment with 25% service enhancement to Normal Pension Age Tier 3 - Temporary payment of pension for up to 3 years	Tier 1 - Immediate payment with service enhanced to Normal Pension Age Tier 2 - Immediate payment with 25% service enhancement to Normal Pension Age Tier 3 - Temporary payment of pension for up to 3 years
Indexation of pension in payment	Inflation rate: CPI (RPI for pre-2011 increases)	Inflation rate: CPI

Pre 2014 employee contribution rates	
Pensionable payroll banding	Contribution rate
Up to £13,700	5.5%
£13,701 to £16,100	5.8%
£16,101 to £20,800	5.9%
£20,801 to £34,700	6.5%
£34,701 to £46,500	6.8%
£46,501 to £87,100	7.2%
More than £87,100	7.5%
Estimated overall LGPS average	6.5%

LGPS 2014 employee contribution rates for 2015/16	
Pensionable payroll banding	Contribution rate
Up to £13,600	5.5%
£13,601 to £21,200	5.8%
£21,201 to £34,400	6.5%
£34,401 to £43,500	6.8%
£43,501 to £60,700	8.5%
£60,701 to £86,000	9.9%
£86,001 to £101,200	10.5%
£101,201 to £151,800	11.4%
More than £151,800	12.5%
Estimated overall LGPS average	6.5%

For additional information about the LGPS 2014 please refer to the Surrey Pension Fund website (<http://www.surreypensionfund.org>) or the LGPS 2014 scheme website (<http://www.lgps2014.org>).

Note 2: Basis of preparation

The Statement of Accounts summarises the fund's transactions for the 2015/16 financial year and its position at the year end at 31 March 2016. The accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The accounts summarise the transactions of the fund and report on the net assets available to pay pension benefits. The accounts do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present value of promised retirement benefits valued according to the International Accounting Standard (IAS) 19 is disclosed at note 25 of these accounts.

These accounts have been prepared on a going concern basis. The liabilities of the pension fund are ultimately backed by the employing organisations within the fund including government bodies with tax raising powers.

Note 3: Summary of significant accounting policies

Pension fund management expenses are accounted for in accordance with CIPFA guidance on accounting for Local Government Scheme Management Costs.

Fund account – revenue recognition

a) Contribution income

Normal contributions, both from the members and from the employer, are accounted for on an accruals basis in the payroll period to which they relate.

Employers' augmentation contributions and pension strain contributions are accounted for in the period in which the liability arises. Any amount due in year but unpaid will be classed as a current financial asset. Contributions due for forthcoming periods are not represented within the financial statements.

b) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the fund during the financial year and are calculated in accordance with the Local Government Pension Scheme Regulations.

Transfers in/leavers are accounted for when received or paid, which is normally when the member liability is accepted or discharged. Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase scheme benefits are accounted for on a receipts basis and are included within transfers in.

c) Investment income

i) Interest income

Interest income is recognised in the fund account as it accrues using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount premium,

transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

- ii) Dividend income
Dividend income is recognised on the date the shares are quoted as ex-dividend. Any amount not received by the end of the reporting period is disclosed in the net asset statement as a current financial asset.
 - iii) Distributions from pooled funds
Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net asset statement as a current financial asset.
 - iv) Movement in the net market value of investments
Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during in the year.
- d) Private equity
Distributions and drawdowns from private equity partnerships are accounted for according to guidance from the private equity manager as to the nature of the distribution or drawdown. Income and purchases and sales are recognised at the date the capital call or distribution falls due.

Fund account – expense items

- e) Benefits payable
Pensions and lump-sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the net asset statement as current liabilities.
- f) Taxation
The fund is a registered public service scheme under section 1 (1) of the Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments may be subject to withholding tax in the country of origin. Irrecoverable tax is accounted for as a fund expense as it arises. Tax on income due but unpaid at the 31 March 2016 is reported as a current liability.
- g) Administration expenses
Pension administrative expenses reflect the costs incurred in the payment of pensions and other benefits, the maintenance of member records and provision of scheme and entitlement information. Costs incurred in relation to specific employers are recharged to those individual organisations and therefore excluded from the accounts.

All administration expenses are accounted for on an accruals basis. The relevant staffing costs of the pension administration team are recharged to the fund.

Management, accommodation and other overheads are apportioned to the fund in accordance with council policy.

h) Investment and governance expenses

All investment management expenses are accounted for on an accruals basis. Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under management and therefore increase or reduce as the value of these investments change.

Governance costs reflect those expenses which fall outside the parameters of administrative or investment expenses. All oversight and governance expenses are accounted for on an accruals basis with associated staffing and overhead costs apportioned in accordance with council policy.

Net assets statement

i) Financial assets

All financial assets are included in the net asset statement on a fair value basis as at the reporting date, with the exception of loans and receivables which are held at amortised cost. A financial asset is recognised in the net assets statement on the date the fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of the assets are recognised by the fund.

The values of investments as shown in the net assets statement have been determined as follows:

i) Market quoted investments

The value of an investment for which there is a readily available market price is determined by the bid market price ruling on the final day of the accounting period.

ii) Fixed interest securities

Fixed interest securities are recorded at net market value based on their current yields.

iii) Unquoted investments

The fair value of investments for which market quotations are not readily available is as follows:

- Valuations of delisted securities are based on the last sale price prior to delisting, or where subject to liquidation, the amount the fund expects to receive on wind-up, less estimated realisation cost.
- Securities subject to takeover offer are valued at the consideration offered, less estimated realisation costs.
- Directly held investments by limited partnerships, shares in unlisted companies, trusts and bonds. Other unquoted securities typically include pooled investments in property, infrastructure, debt securities and private equity. The valuation of

these pools or directly held securities is undertaken by the investment manager or responsible entity and advised as a unit or security price. The valuation standards followed in these valuations adhere to industry guidelines or to standards set by the constituent documents of the pool or management agreement.

- iv) Investments in private equity funds and unquoted listed partnerships are valued based on the fund's share of the net assets in the private equity fund or limited partnership using the latest financial statements published by the respective fund managers in accordance with the guidelines set out by the International Private Equity and Venture Capital Guidelines, which follow the valuation principles of IFRS.
 - v) Limited partnerships
Fair value is based on the net asset value ascertained from periodic valuations provided by those controlling the partnership.
 - vi) Pooled investment vehicles
Pooled investment vehicles are valued at closing bid price if both bid and offer prices are published; or if singularly priced, at the closing single price.
- j) Foreign currency transactions
Dividends, interest and purchases and sales of investments in foreign currencies have been accounted for at the spot rate on the date of transaction. End-of-year spot market exchange rates are used to value cash balances held in foreign currency bank accounts, market values of overseas investments and purchases and sales outstanding at the end of the reporting period.
- k) Derivatives
The fund uses derivative financial instruments to manage its exposure to specific risks arising from its investment activities. The fund does not hold derivatives for speculation purposes.
- Derivative contract assets are fair valued at bid prices and liabilities are fair valued at offer prices. Changes in fair value of derivative contracts are included in the change in market value.
- The value of futures contracts is determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin.
- The future value of forward currency contracts is based on the market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year end with an equal and opposite contract.
- l) Cash and cash equivalents
Cash comprises cash in hand and demand deposits. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal changes in value.

m) Financial liabilities

The fund recognises financial liabilities at fair value as at the reporting date. A financial liability is recognised in the net asset statement on the date the fund becomes party to the liability. From this date any gains or losses arising from changes in the fair value of the liability are recognised by the fund.

n) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the scheme actuary in accordance with the requirement of IAS 19 and relevant actuarial standards.

As permitted under IAS 26, the fund has opted to disclose the actuarial present value of promised retirement benefits by way of a note to the net asset statement.

o) Additional voluntary contributions

Surrey Pension Fund provides an additional voluntary contributions (AVC) scheme for its members, the assets of which are invested separately from those in the pension fund. The fund has appointed Prudential as the AVC provider. A small number of members remain with the previous provider Equitable Life. AVCs are paid to the AVC provider by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amounts held in their account and the movements in the year.

AVCs are not included in the accounts in accordance with section 4(2)(b) of the Local Government Pension Scheme (Management & Investment of Funds) Regulations 2009 (SI 2009/3093).

Note 4: Critical judgements in applying accounting policies

Unquoted private equity investments

It is important to recognise the highly subjective nature of determining the fair value of private equity investments. They are inherently based on forward looking estimates and judgements involving many factors. Unquoted private equities are valued by the investment managers using the International Private Equity and Venture Capital Guidelines, which follow the valuation principles of IFRS. The value of unquoted private equities at 31 March 2016 was £129 million (£113 million at 31 March 2015).

Pension Fund Liability

The pension fund liability is calculated every three years by the appointed actuary, with annual updates in the intervening years. The methodology used is in line with accepted guidelines and in accordance with IAS 19. Assumptions underpinning the valuations are agreed with the actuary and are summarised in note 25. This estimate is subject to significant variances based on changes to the underlying assumptions.

Note 5: Assumptions made about the future and other major sources of estimation uncertainty

The Statement of Accounts contains estimated figures that are based on assumptions made by the council about the future or that are otherwise uncertain. Estimates are made by taking into account historical experience, current trends and other relevant factors. However, because balances cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

The items in the net assets statement or subsequent notes as at 31 March 2016 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	Estimation of the net liability to pay pension depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets. A firm of consulting actuaries is engaged to provide the fund with expert advice about the assumptions to be applied.	The net pension liability of the fund would change. An increase in the discount rate would result in a corresponding decrease in the pension liability. An increase in earnings would increase the value of liabilities, as would an increase in life expectancy.
Private equity	Private equity investments, both limited partnership and fund of funds, are disclosed at fair value, provided by the administrators of the funds. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the financial statement are £129 million. There is a risk that this investment may be over or under stated in the accounts.
Fund of fund investments	Where investments are made into a fund of fund structure there is an additional level of separation from the fund. There may be a lack of clarity over the classification of the sub funds and investment transactions	The total private equity fund of fund investments are £81 million. There is a risk that asset or investment transaction misclassification may occur.

Note 6: Events after the balance sheet date

The Statement of Accounts will be authorised for issue by the Chief Financial Officer in July 2016. The Statement of Accounts is adjusted to reflect events after the balance sheet date, both favourable and unfavourable, that occur between the end of the reporting date and the date when the Statement of Accounts is authorised for issue that provide evidence of conditions that existed at the end of the reporting period unless deemed insignificant to the true and fair value of the Funds assets and liabilities. No such adjustments have been deemed necessary.

Note 7: Contributions receivable

By category

2014/2015		2015/2016
£000		£000
93,269	Employers	94,565
43,580	Employers deficit	55,283
36,599	Members	37,053
173,448		186,901

2014/2015		2015/2016
£000		£000
83,223	Administering authority	84,530
75,565	Scheduled bodies	82,358
14,660	Admitted bodies	20,013
173,448		186,901

The latest actuarial valuation carried out as at 31 March 2013, set contribution rates for fund employers with effect from April 2014. The financial year 2014/2015 was the first year of the revised employer contribution rates.

Note 8: Transfers in from other pension funds

2014/2015		2015/2016
£000		£000
0	Group transfers from other schemes	0
7,656	Individual transfers in from other schemes	5,518
7,656		5,518

Note 9: Benefits payable

By category

2014/15		2015/16
£000		£000
106,175	Pensions	110,904
17,734	Commutation and lump sum retirement benefits	17,276
2,170	Lump sum death benefits	3,094
34	Interest on late payment of benefits	56
126,113		131,330

By employer*

2014/2015		2015/2016
£000		£000
60,937	Administering Authority	61,079
55,571	Scheduled Bodies	59,766
9,571	Admitted Bodies	10,429
126,079		131,274

*(Note that the above does not include interest on late payment of benefits of £56k)

Note 10: Payments to and on account of leavers

2014/2015		2015/2016
£000		£000
0	Group transfers to other schemes	480
5,896	Individual transfers to other schemes	5,907
227	Refunds of contributions	298
72	Payments for members joining state schemes	77
6,195		6,762

Note 11: Current assets

2014/2015		2015/2016
£000		£000
2,816	Contributions - employees	3,262
10,196	Contributions - employer	12,025
5,937	Sundry debtors	7,803
<u>18,949</u>		<u>23,090</u>

Analysis of current assets

2014/2015		2015/2016
£000		£000
3,112	Central government bodies	5,366
13,713	Other local authorities	15,478
2,123	Other entities and individuals	2,246
<u>18,948</u>		<u>23,090</u>

Note 12: Long term debtors

2014/2015		2015/2016
£000		£000
12,705	Central government bodies	10,890
<u>12,705</u>		<u>10,890</u>

On 1 April 2005 the Magistrates Court Service (an employer in the Surrey Pension Fund) became part of the Civil Service. Terms were agreed for the transfer of liabilities from the Local Government Pension Scheme (LGPS) to the Principal Civil Service Pension Scheme (PCSPS). The fund's actuary determined the value of the pensioner and deferred liabilities remaining with the fund and calculated the retained assets to match these liabilities. The actuary determined that the assets were insufficient to match the liabilities and that a balancing payment would be required.

On 11 March 2013 the total value of the shortfall was agreed as £18.150m, to be made in ten equal, annual instalments commencing on 15 April 2013. The full amount was recognised as contributions during 2012/13. A corresponding debtor was created. The first instalment of £1.815m was received on 26 March 2013 meaning that the remaining nine instalments were due in excess of one year from the 31 March 2013, the whole of the remaining balance was therefore included as a long term debtor in the accounts. The outstanding balance as at 31 March 2016 is £12.705m but £1.815m was due in 2015/16, leaving a long term debtor of £10.890m.

Note 13: Current liabilities

2014/2015		2015/2016
£000		£000
5,541	Sundry creditors	6,595
20	Benefits payable	60
<u>5,561</u>		<u>6,655</u>

Analysis of current liabilities

2014/2015		2015/2016
£000		£000
1,408	Central government bodies	1,483
1,664	Other local authorities	3,053
2,489	Other entities and individuals	2,119
<u>5,561</u>		<u>6,655</u>

Note 14: Investment and governance expenses

2014/2015		2015/2016
£000		£000
14,908	Investment management fees	13,952
226	Investment custody fees	206
723	Oversight and governance costs	672
<u>15,857</u>		<u>14,830</u>

The investment management fees above includes £1.9million (2014/15:£3.9million) in respect of performance-related fees paid/payable to the fund's investment managers. It also includes £1.1million in respect of transaction costs (2014/15: £1.6million).

Note 15: Taxes on Income

2014/2015		2015/2016
£000		£000
603	Withholding tax - equities	821
420	Withholding tax - property	103
1,023		924

Note 16: Investment income

2014/2015		2015/2016
£000		£000
	Fixed interest	
5,905	UK	5,394
5,873	Overseas	6,956
54	Index linked	91
	Equities	
18,781	UK	21,269
10,605	Overseas	12,322
7,936	Property unit trusts	7,943
2,601	Diversified growth	3,245
3,793	Private equity	3,412
523	Interest on cash deposits	180
373	Other	534
56,444		61,346

Diversified growth is an investment in a separate pooled fund, which can invest in a variety of traditional and alternative asset classes to target a return comparable with other growth assets but with reduced volatility.

Note 17a: Reconciliation of movements in investments and derivatives

	Market value at 31 Mar 2015	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Market movements	Market value at 31 Mar 2016
	£000	£000	£000	£000	£000
Fixed interest securities	350,859	157,937	-143,145	-23,070	342,581
Index linked securities	161,260	0	-2,093	9,303	168,470
Equities	1,908,092	257,490	-262,124	-52,434	1,851,024
Property unit trusts	199,410	35,963	-26,003	16,320	225,690
Diversified growth	360,061	30,344	0	-13,719	376,686
Private equity	112,642	24,797	-26,434	18,348	129,353
Derivatives					
- Futures	-288	470	-2	-154	26
- Forex contracts	-8,419	39,557	-12,829	-24,596	-6,287
	3,083,617	546,558	-472,630	-70,002	3,087,543
Cash	77,218			1,347	64,294
Other short term investments	0				37,000
Other investment balances	6,592				7,501
Borrowing	0				0
	3,167,427			-68,655	3,196,338

	Market value at 31 Mar 2014	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Market movements	Market value at 31 Mar 2015
	£000	£000	£000	£000	£000
Fixed interest securities	352,134	50,397	-78,009	26,337	350,859
Index linked securities	94,675	143,817	-102,781	25,549	161,260
Equities	1,747,131	643,615	-679,281	196,627	1,908,092
Property unit trusts	165,824	33,218	-17,909	18,277	199,410
Diversified growth	270,937	60,253	0	28,871	360,061
Private equity	101,814	32,424	-40,239	18,643	112,642
Derivatives					
- Futures	-35	1,447	-159	-1,541	-288
- Forex contracts	7,862	11,823	-14,551	-13,553	-8,419
	2,740,342	976,994	-932,929	299,210	3,083,617
Cash	39,212				77,218
Other investment balances	1,958				6,592
Borrowing	-4,500				0
	2,777,012			299,210	3,167,427

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

Derivative receipts and payments represent the realised gains and losses on forward foreign exchange contracts. The Fund's objective is to decrease risk in the portfolio by entering into futures positions to match assets that are already held in the portfolio.

Note 17b: Analysis of investments

	31 Mar 2015	31 Mar 2016
Fixed interest securities	£000s	£000s
UK public sector & quoted	148,648	82,845
UK pooled funds	51,905	0
Overseas public sector & quoted	76,104	66,961
Overseas pooled fund	74,202	192,775
	350,859	342,581
Index linked securities	161,260	168,470
Equities		
UK quoted	540,276	495,555
UK pooled funds	276,454	281,110
Overseas quoted	554,463	564,742
Overseas pooled funds	536,899	509,617
	1,908,092	1,851,024
Property unit trusts		
UK property funds	194,992	224,098
Overseas property funds	4,418	1,592
	199,410	225,690
Diversified growth		
UK diversified growth funds	0	0
Overseas diversified growth funds	360,061	376,686
	360,061	376,686
Private equity		
UK limited partnerships	24,905	27,970
Overseas limited partnerships	13,852	20,452
UK fund of funds	0	0
Overseas fund of funds	73,885	80,931
	112,642	129,353
Derivatives		
Futures	-288	26
FX forward contracts	-8,419	-6,261
	-8,707	-6,235
Cash deposits	77,218	64,294
Other short term investments	0	37,000
Other investment balances		
Outstanding sales	2,239	1,459
Outstanding purchases	-2,408	-1,105
Tax due on accrued income	-33	-43
Accrued income - dividends and interest	6,794	7,190
	6,592	7,501
Total investments	3,167,427	3,196,338

Note 17c: Analysis of derivatives**Futures**

Futures contracts are exchange traded contracts to buy or sell a standard quantity of a specific asset at a pre-determined future date. At 31 March 2016 the fund had three futures contracts in place with an unrealised gain of £26k. As at 31 March 2015 the Fund had two contracts in place with a net unrealised loss of £288k.

**31 March
2016**

Contract	Expiration date	Expiration date within	Type of underlying investment	Economic exposure £'000	Asset £'000	Liability £'000
Futures	21/06/2015	3 Months	US Treasury Bonds	801	11	0
Futures	21/06/2015	3 Months	US Treasury Bonds	-3,721	8	0
Futures	28/06/2015	3 Months	UK Government Bonds	-7,637	7	0
				-7,637	26	0

**31 March
2015**

Contract	Expiration date	Expiration date within	Type of underlying investment	Economic exposure £'000	Asset £'000	Liability £'000
Futures	19/06/2015	3 Months	US Treasury Bonds	3,312	0	-64
Futures	26/06/2015	3 Months	UK Government Bonds	11,471	0	-224
				14,783	0	-288

Forward currency contracts

Forward foreign exchange contracts are over the counter contracts whereby two parties agree to exchange two currencies on a specified future date at an agreed rate of exchange. At 31 March 2016 the Fund had forward currency contracts in place with a net unrealised loss of £6,287 (net unrealised loss of £8,419k at 31 March 2015).

2015/16

No of contracts	Contract settlement date within	Currency		Notional amount (local currency)		Asset £'000	Liability £'000
		Bought	Sold	Bought (000)	Sold (000)		
1	One Month	BRL	USD	4,002	-1,122	17	-13
1	One Month	GBP	AUD	4	-8	0	0
1	One Month	GBP	EUR	20	-25	0	0
2	Two Months	GBP	EUR	6,118	-7,884	0	-140
4	Three Months	GBP	EUR	87,400	-112,765	0	-2,145
1	One Month	GBP	JPY	87	-14,147	0	0
3	Three Months	GBP	JPY	62,227	-10,246,348	0	-1,291
1	Two Months	GBP	SEK	2,482	-30,350	0	-126
4	Two Months	GBP	USD	16,283	-23,539	0	-93
6	Three Months	GBP	USD	278,256	-403,456	0	-2,403
1	One Month	GBP	ZAR	0	-9	0	0
1	One Month	USD	BRL	966	-4,002	7	-120
1	Four Months	USD	BRL	1,094	-4,002	4	-7
1	One Month	USD	GBP	457	-318	0	0
1	Two Months	USD	GBP	842	-580	6	0
1	Two Months	USD	JPY	2,290	-254,405	10	7
						44	-6,331

2014/15

No of contracts	Contract settlement date within	Currency		Notional amount (local currency)		Asset £'000	Liability £'000
		Bought	Sold	Bought (000)	Sold (000)		
1	One Month	AUD	HKD	63	-380	0	-1
1	One Month	CHF	GBP	69	-48	0	0
1	One Month	EUR	GBP	98	-71	0	0
2	Two Months	EUR	GBP	5,183	-3,831	0	-78
1	One Month	GBP	DKK	176	-1,817	0	0
1	One Month	GBP	EUR	142	-196	0	0
1	Two Months	GBP	EUR	11,511	-15,348	399	0
5	Three Months	GBP	EUR	101,285	-136,236	2,603	0
4	Three Months	GBP	JPY	60,634	-11,040,774	0	-1,458
1	One Month	GBP	MXN	24	-535	0	0
1	Two Months	GBP	MXN	1,095	-24,670	7	0
1	One Month	GBP	NOK	78	-931	0	0
1	One Month	GBP	SEK	133	-1,708	0	0
5	Two Months	GBP	USD	16,218	-24,789	0	-486
7	Three Months	GBP	USD	262,793	-403,768	0	-9,308
1	One Month	GBP	ZAR	13	-228	0	0
1	One Month	HKD	SGD	463	-82	0	0
1	One Month	JPY	USD	1,117,909	-9,437	0	-76
1	One Month	USD	BRL	1,265	-4,002	14	0
1	One Month	USD	GBP	777	-525	0	-2
1	One Month	USD	JPY	9,412	-1,117,909	59	0
1	Three Months	USD	JPY	10,576	-1,283,435	0	-92
						3,082	-11,501

Stock Lending

During the financial year 2015/16 the fund operated a stock lending programme in partnership with the fund custodian. As at 31 March 16 the value of quoted securities on loan was £119.4million in exchange for collateral held by the fund custodian at fair value of £128.2million

Note 17d: Investments analysed by fund manager

Market value 31 March 2015		Manager	Market value 31 March 2016	
£000	%		£000	%
918,551	30.6	Legal & General Investment Management	831,747	26.0%
308,575	10.3	Majedie Asset Management	289,511	9.1%
0	0.0	Mirabaud Asset Management	0	0.0%
242,069	8.0	UBS Asset Management	227,289	7.1%
424,497	14.1	Marathon Asset Management	440,714	13.8%
242,915	8.1	Newton Investment Management	249,031	7.8%
232,799	7.8	Western Asset Management	283,675	8.9%
69,454	2.3	Franklin Templeton Investments	65,268	2.0%
227,691	7.6	Standard Life Investments	246,846	7.7%
132,370	4.4	Baillie Gifford Life Limited	129,839	4.1%
179,326	6.0	CBRE Global Multi-Manager	205,181	6.4%
23,354	0.8	Darwin Property Investment Management	25,687	0.8%
3,001,601			2,994,788	

The table above excludes the private equity portfolio, internal cash and residual cash held by the custodian.

The following investments represent more than 5% of the net investment assets of the fund

Market value 31 March 2015 £000	% of total fund	Security	Market value 31 March 2016 £000	% of total fund
393,877	12.4	Legal & General World Developed Equity Index	380,744	11.9
276,450	8.7	Legal & General UK Equity Index	255,392	8.0
163,459	5.2	Standard Life Global Absolute Return Strategies	173,119	5.4

Note 18a: Classification of financial instruments

The following table analyses the fair value of financial assets and liabilities by category and net asset statement heading. No financial assets were reclassified during the accounting period.

As at 31 March 2015**As at 31 March 2016**

Designated as fair value though profit and loss £000	Loans and receivables £000	Financial liabilities at amortised costs £000		Designated as fair value though profit and loss £000	Loans and receivables £000	Financial liabilities at amortised costs £000
Financial assets						
350,859	0	0	Fixed interest securities	342,581	0	0
161,260	0	0	Index linked securities	168,470	0	0
1,908,092	0	0	Equities	1,851,024	0	0
199,410	0	0	Property unit trusts	225,690	0	0
360,061	0	0	Diversified growth	376,686	0	0
112,642	0	0	Private equity	129,353	0	0
3,082	0	0	Derivatives	70	0	0
0	77,218	0	Cash	0	64,294	0
			Other short term investments		37,000	
9,033	0	0	Other investment balances	8,649	0	0
0	31,654	0	Debtors	0	33,980	0
3,104,439	108,872	0	Total financial assets	3,102,523	135,274	0
Financial liabilities						
-11,789	0	0	Derivatives	-6,331	0	0
-2,441	0	0	Other investment balances	-1,148	0	0
0	0	-5,561	Creditors	0	0	-6,655
0	0	0	Borrowings	0	0	0
-14,230	0	-5,561	Total financial liabilities	-7,479	0	-6,655
3,090,209	108,872	-5,561		3,095,044	135,274	-6,655

Note 18b: Valuation of financial instruments carried at fair value

The valuation of financial instruments has been classified into three levels, according to the quality and reliability of information used to determine fair values.

Level 1

Financial instruments at level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities, quoted fixed securities, quoted index-linked securities and unit trusts.

Listed investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

Level 2

Financial instruments at level 2 are those where quoted market prices are not available, for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3

Financial instruments at level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data.

The fund's private equity investments are valued using techniques that require significant judgement in determining appropriate assumptions. The value of the investments in private equity are based on valuations provided by the managers of the private equity funds in which the Surrey Pension Fund is invested.

These valuations are prepared in accordance with the International Private Equity and Venture Capital Guidelines, which follow the valuation principles of IFRS.

31 March 2016	Quoted market price Level 1 £000	Using observable inputs Level 2 £000	With significant unobservable inputs Level 3 £000	Total £000
Financial assets				
Financial assets through profit & loss	2,848,936	93,353	160,234	3,102,523
Total financial assets	2,848,936	93,353	160,234	3,102,523
Financial liabilities				
Financial liabilities through profit & loss	7,479	0	0	7,479
Total financial liabilities	7,479	0	0	7,479
Net financial assets	2,841,457	93,353	160,234	3,095,044

31 March 2015	Quoted market price Level 1 £000	Using observable inputs Level 2 £000	With significant unobservable inputs Level 3 £000	Total £000
Financial assets				
Financial assets through profit & loss	2,877,727	93,600	133,112	3,104,439
Total financial assets	2,877,727	93,600	133,112	3,104,439
Financial liabilities				
Financial liabilities through profit & loss	14,230	0	0	14,230
Total financial liabilities	14,230	0	0	14,230
Net financial assets	2,863,497	93,600	133,112	3,090,209

Note 18c: Book cost

The book cost of all investments at 31 March 2016 is £2,585million (£2,489million at 31 March 2015).

Note 19: Outstanding commitments

At 31 March 2016 the Fund held part paid investments on which the liability for future calls amounted to £91million (£98million as at 31 March 2015).

Note 20: Nature and extent of risks arising from financial instruments

Risk and risk management

The fund's primary long-term risk is that the fund's assets will fall short of its liabilities (ie promised benefits to members). Therefore the aim of investment risk management is to minimise the risk of an overall reduction in the value of the fund and to maximise the opportunity for gain across the whole portfolio. The fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) and credit risk to an acceptable level. In addition, the fund manages its liquidity risk to ensure there is sufficient liquidity to meet the fund's forecast cash flows. The council manages these investment risks as part of its overall pension fund risk management programme.

Responsibility for the fund's risk management strategy rests with the Pension Fund. Risk management policies are established to identify and analyse the risks faced by the council's pensions operations. Policies are reviewed regularly to reflect changes in activity and in market conditions.

a) **Market risk**

Market risk is the risk of loss from fluctuations in equity prices, interest and foreign exchange rates and credit spreads. The fund is exposed to market risk from its investment activities, particularly through its equity holdings. The level of risk exposure depends on market conditions, expectations of future price, yield and the asset mix.

To mitigate market risk, the pension fund is invested in a diverse pool of assets to ensure a reasonable balance between different asset categories, having taken external professional advice as necessary. The management of the assets is split between a number of investment fund managers with different benchmark performance targets and investment strategies. Managers are expected to maintain a diverse portfolio and each manager has investment guidelines in place that specify the manager's investment powers and restrictions. Managers are required to report on any temporary breaches of their investment powers and are required to take corrective action as soon as is practicable.

Other price risk

Other price risk represents the risk that the value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate risk or foreign exchange risk), whether those changes are caused by factors specific to the individual instrument or its issuer or factors affecting all such instruments in the market.

The fund is exposed to share and derivative price risk. This arises from investments held by the fund for which the future price is uncertain. All securities investments present a risk of loss of capital. The maximum risk resulting from a financial instrument is determined by the fair value of the instrument.

By diversifying investments across asset classes and managers, the fund aims to reduce the exposure to price risk. Statutory limits prescribed by Regulations are also in place to avoid concentration of risk in specific areas.

Other price risk – Sensitivity Analysis

The WM Company has provided the fund with an analysis of historical asset class returns to determine potential movements in the market price risk of investments during 2015/16 reporting period. The potential volatilities are consistent with a one standard deviation movement in the change in value of the assets over the latest three years.

Asset type	Value at 31 March 2016 £000	Change	Value on increase £000	Value on decrease £000
UK equities	776,665	10.01%	854,409	698,921
Overseas equities	1,074,359	9.32%	1,174,489	974,229
Fixed interest bonds	342,581	5.61%	361,800	323,362
Index linked	168,470	9.48%	184,441	152,499
Cash	64,294	0.01%	64,300	64,288
Other short term investments	37,000	0.01%	37,004	36,996
Property	225,690	1.74%	229,617	221,763
Alternatives	129,353	6.45%	137,696	121,010
Diversified growth fund	376,686	3.90%	391,377	361,995
Other assets	1,240	0.01%	1,241	1,239
Total Investment Assets	3,196,338	6.60%⁽¹⁾	3,407,296	2,985,380

Asset type	Value at 31 March 2015 £000	Change	Value on increase £000	Value on decrease £000
UK equities	816,730	9.76%	896,443	737,017
Overseas equities	1,091,362	9.09%	1,190,567	992,157
Fixed interest bonds	350,859	5.52%	370,226	331,492
Index linked	161,260	9.33%	176,306	146,214
Cash	77,218	0.01%	77,226	77,210
Property	199,410	2.43%	204,256	194,564
Alternatives	112,642	5.60%	118,950	106,334
Diversified growth fund	360,061	3.27%	371,835	348,287
Other assets	-2,115	0.00%	-2,115	-2,115
Total Investment Assets	3,167,427	6.12%⁽¹⁾	3,361,274	2,973,580

(1) The percentage change for total investment assets includes the impact of correlation across asset classes. Therefore the impact upon total assets will not tally to the sum of each asset class' individual value on increase/decrease.

Interest rate risk

The fund invests in financial assets for the primary purpose of obtaining a return on investments. These investments are subject to interest rate risks, which represent the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The fund is predominantly exposed to interest rate risk through its holdings in bonds. Western Asset Management, the Fund's appointed active bond manager, manages this risk. The fund also invests in pooled bond funds managed by Legal & General and Franklin Templeton.

The fund's direct exposure to interest rate movements as at 31 March 2016 and 31 March 2015 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value.

As at 31 March 2015 £000		As at 31 March 2015 £000	
77,218	Cash & cash equivalents	64,294	
0	Other short term investments	37,000	
350,859	Fixed interest securities	342,581	
428,077	Total	443,875	

Interest rate risk sensitivity analysis

The council recognises that interest rates can vary and can affect both income to the fund and the value of the net assets available to pay benefits. Long term average interest rates are not particularly volatile from one year to the next so a potential move in interest rates of 100 basis points is deemed reasonable.

The analysis below assumes all other variables remain constant and shows the effect in the year on the net assets of a +/- 100 basis point change in interest rates.

Asset type	Carrying amount as at 31 March 2016	Change in net assets	
	£000	+100 bps £000	- 100 bps £000
Cash & cash equivalents	64,294	64	-64
Other short term investments	37,000	37	-37
Fixed interest securities	342,581	343	-343
Total	443,875	444	-444

Asset type	Carrying amount as at 31 March 2015	Change in net assets	
	£000	+100 bps £000	- 100 bps £000
Cash & cash equivalents	77,218	772	-772
Fixed interest securities	350,859	3,509	-3,509
Total	428,077	4,281	-4,281

Currency risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The fund is exposed to currency risk on financial instruments that are denominated in any currency other than sterling. The fund holds monetary and non-monetary assets denominated in currencies other than sterling.

The fund therefore has a policy to passively hedge up to 50% of the equity exposure to US Dollar, Yen and the Euro. Legal and General Investment Management manages this currency hedge. Individual fund managers may also use derivatives if permitted by their investment management agreements. Furthermore, fund managers will take account of currency risk in their investment decisions.

Currency risk – sensitivity analysis

The WM Company has provided the fund with an analysis of historical exchange rate movements to determine potential changes in the fair value of assets during the 2015/16 reporting period due to exchange rate movements.

The analysis assumes all other variables remain constant.

Asset type	Value at 31 March 2015 £000	% Change	Value on increase £000	Value on decrease £000
Equities	983,313	6.24%	1,044,672	921,954
Fixed interest	211,966	6.24%	225,193	198,739
Property and Private Equity	102,975	6.24%	109,401	96,549
Diversified Growth	376,686	6.24%	400,191	353,181
Cash and Other Assets	10,433	6.24%	11,084	9,782
Total	1,685,373	6.24%	1,790,541	1,580,205

For comparison last year figures are included below.

Asset type	Value at 31 March 2015 £000	% Change	Value on increase £000	Value on decrease £000
Equities	1,074,070	5.94%	1,137,820	1,010,320
Fixed interest	117,553	5.94%	124,530	110,576
Property and Private Equity	94,249	5.94%	99,843	88,655
Diversified Growth	360,061	5.94%	381,432	338,690
Cash and Other Assets	-3,644	5.94%	-3,860	-3,428
Total	1,642,289	5.94%	1,739,765	1,544,813

b) Credit risk

Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the fund to incur a financial loss. The market values of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the fund's financial assets and liabilities.

In essence the fund's entire investment portfolio is exposed to some form of credit risk, with the exception of the derivative positions, where the risk equates to the net market value of a positive derivative position. However, the selection of high quality counterparties, brokers and financial institutions minimises the credit risk that may occur through the failure to settle a transaction in a timely manner.

Contractual credit risk is represented by the net payment or receipt that remains outstanding, and the cost of replacing the derivative position in the event of a counterparty default. The residual risk is minimal due to the various insurance policies held by exchanges to cover defaulting counterparties.

The fund's cash balance is lent to borrowers in accordance with the county council's treasury management strategy. There are rigorous procedures in place to manage the security of all cash deposits, including criteria for the quality of counterparties and limits on the amount that can be placed with any one of those counterparties. The council operates a lowest common denominator approach to counterparty management which means that available counterparties must meet the minimum credit rating criteria with all three ratings agencies.

The fund has agreed a total of £37m in short fixed term deposits as part of the treasury management strategy; these include £37 million of fixed term deposits with other Local Authorities.

Balance at 31 March 2015 £000	Fixed Term Deposits	Balance at 31 March 2016 £000
	Sheffield City Council	10,000
	The Wirral Metropolitan Borough Council	7,000
	Woking Borough Council	5,000
	Southend on Sea Borough Council	5,000
	Wiltshire Council	10,000
0	Other short term investments	37,000

The fund holds a separate bank account with HSBC, which holds AA long term credit ratings (or equivalent) with all three credit rating agencies (Fitch, Moody's, Standard and Poor's).

The fund has a call account with Natwest Bank and Lloyds Bank, an account with a money market fund, managed by Goldman Sachs Asset management and a term deposit placed with Nationwide Building society. In line with the treasury strategy, the maximum deposit level allowed with each counterparty is £15 million.

Balance at 31 March 2015 £000		Balance at 31 March 2016 £000
	Term Deposits	
0	Nationwide	10,000
	Call account	
7,400	Natwest	12
0	Lloyds	5,031
	Money market fund	
15,000	Goldman Sachs	6,700
	Current account	
-193	HSBC	3,835
22,207	Internally Managed Cash	25,578
55,011	Externally Managed Cash	38,716
77,218	Total Cash	64,294

The fund's cash holding under its treasury management arrangements as at 31 March 2016 was £25.6million (£22.2million at 31 March 2015).

c) Liquidity risk

Liquidity risk represents the risk that the fund will not be able to meet its financial obligations as they fall due. The council therefore takes steps to ensure that the pension fund has adequate cash to meet its commitments. The fund needs to manage its cash flows to ensure pensioner payroll costs are met and sufficient cash is available to meet investment commitments.

The treasury management activities of the fund are managed by Surrey County Council on a daily basis. A cash flow forecast is updated daily to help understand and manage the timings of the fund's cash flows.

The fund has immediate access to the internally managed cash holdings and money market fund.

The fund is able to borrow cash to meet short-term cash requirements, no such instances occurred during 2014/15 or 2015/16

The fund currently has a long-term positive cash flow, which reflects the fact that contributions into the fund exceed benefits being paid out. Cash flow surpluses are invested with fund managers, given that the fund has an aim of being as fully invested as possible after allowing for the need to hold working balances. Regular rebalancing exercises take place, which involves assessing the level of internal cash available to be invested with managers.

d) Derivative risk

Some portfolios in which the fund invests may utilise financial derivative instruments to reduce risks or costs or to generate additional returns to meet the portfolio's

objectives. Use of such derivatives does not guarantee a positive result for the portfolio.

Derivatives may invoke a small initial investment but carry the potential for a much greater liability. This is known as leverage. A small market movement could therefore have a proportionately larger impact either for or against the fund. Other specific risks include the inability of the portfolio manager to close out a derivative position due to illiquidity in the derivative market.

The employment of derivatives within the fund is limited to specific portfolios where their usage is primarily to manage volatility associated with other holdings. A significant movement to the detriment of the portfolio is intended to be balanced by positive movements in other areas of the portfolio. Fund managers will be expected to ensure a balanced, diverse pool of assets with internal exposure restrictions to limit the impact of potential market movements.

Note 21: Related party transactions

i) Employer pension contributions paid by Surrey County Council in 2015/16 amounted to £65,019k (£64,074k in 2014/15).

2014/2015 £000		2015/2016 £000
42,996	Employers' current service contributions	43,370
18,834	Lump sum payments to recover the deficit in respect of past service	21,087
2,244	Payments into the fund to recover the additional cost of early retirement liabilities	562
<u>64,074</u>		<u>65,019</u>

ii) Surrey Pension Fund paid Surrey County Council £1,382k for services provided in 2015/16 (£1,662k in 2014/15).

2014/2015 £000		2015/2016 £000
252	Treasury management, accounting and managerial services	261
1,410	Pension administration services	1,121
<u>1,662</u>		<u>1,382</u>

iii) Net amounts owed by Surrey County Council to the fund as at 31 March 2016 were £8,583k (£6,594k at 31 March 2015).

Note 22: Key management personnel

The below employees of Surrey County Council hold key positions in the financial management of the Surrey Pension Fund. Their financial relationship with the fund is disclosed as a proportion of salary costs, including employer pension contributions and national insurance contributions that can be attributed to the fund. The post for Senior Specialist Advisor had only recently been created and filled by the end of 2014/15 and was excluded from the note for 2014/15 accounts. The role has sufficient influence within the management of the pension fund to warrant inclusion for 2015/16 and restated for 2014/15.

2014/15 £ (restated)	Position	2015/16 £	
22,313	Chief Finance Officer	22,484	1
67,659	Pension Fund & Treasury Manager	73,164	2
10,372	Senior Specialist Advisor	44,132	2
52,653	Senior Accountant (Alex)	53,662	3
152,998		193,442	

1. 15% of time allocated to pension fund
2. 70% of time allocated to pension fund
3. 100% of time allocated to pension fund

Note 23: Custody

Custody arrangements for all securities and cash balances are provided by the fund's global custodian, The Northern Trust Company, excluding private equity investments and internally held cash. For the Fund's private equity investments, the custodial arrangements are managed by the individual private equity partnership with each custodian in charge of all private equity partnership assets, not just those of the Surrey Pension Fund.

Custodian arrangements for the managers responsible for private equity are as follows:

Private Equity Manager	Custody Provider
BlackRock	PNC Bank
Goldman Sachs	State Street Global Advisors
HG Capital	Bank of New York
Livingbridge (Formerly ISIS)	Lloyds Banking Group
Standard Life	State Street Global Advisors, Deutsche Bank & JP Morgan
Capital Dynamics	Bank of America

Note 24 : Actuarial statement for 2015/16 - funding arrangements

This statement has been prepared in accordance with Regulation 57(1)(d) of the Local Government Pension Scheme Regulations 2013. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

Description of funding policy

The funding policy is set out in the Surrey Pension Fund's (the Fund) Funding Strategy Statement (FSS). In summary, the key funding principles are as follows:

- to achieve and then maintain a funding target that requires assets equal to 100% on an ongoing basis of the present value of benefits based on completed service including provision for the effects of future salary growth and inflation up to retirement;
- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment
- 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.

The FSS sets out how the administering authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable. For employers whose covenant was considered by the administering authority to be sufficiently strong, contributions have been stabilised below the theoretical rate required to return their portion of the Fund to full funding over 20 years if the valuation assumptions are borne out.

Asset-liability modelling has been carried out which demonstrate that if these contribution rates are paid and future contribution changes are constrained as set out in the FSS, there is still a better than 65% chance that the Fund will return to full funding over 20 years.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 36 of the Local Government Pension Scheme (Administration) Regulations 2008 was as at 31 March 2013. This valuation revealed that the Fund's assets, which at 31 March 2013 were valued at £2,559 million, were sufficient to meet 72.3% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2013 valuation was £980 million.

Individual employers' contributions for the period 1 April 2014 to 31 March 2017 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the valuation report dated 31 March 2014

Method

The liabilities were assessed using an accrued benefits method which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth to retirement or expected earlier date of leaving pensionable membership.

Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value.

The key financial assumptions adopted for the 2013 valuation were as follows:

Financial assumptions	31 March 2013	
	% p.a. Nominal	% p.a. Real
Discount rate	4.6%	2.1%
Pay increases	3.8%	1.3%
Price inflation/Pension increases	2.5%	-

The key demographic assumption was the allowance made for longevity. As a member of Club Vita, the baseline longevity assumptions adopted at this valuation were a bespoke set of VitaCurves that were specifically tailored to fit the membership profile of the Fund. Longevity improvements were in line with standard PXA92 year of birth mortality tables, with medium cohort projections and a 1% p.a. underpin effective from 2007. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current pensioners	22.5 years	24.6 years
Future pensioners	24.5 years	26.9 years

Copies of the 2013 valuation report and Funding Strategy Statement are available on request from Surrey County Council, the Administering Authority to the Fund.

Experience over the year since April 2013

Experience has been worse than expected since the last formal valuation (excluding the effect of any membership movements). Real bond yields have fallen dramatically placing a higher value on liabilities. The effect of this has been only partially offset by the effect of strong asset returns. Funding levels are therefore likely to have worsened and deficits increased over the period.

The next actuarial valuation will be carried out as at 31 March 2016. The Funding Strategy Statement will also be reviewed at that time.

Fellow of the Institute and Faculty of Actuaries

For and on behalf of Hymans Robertson LLP

28 April 2016

Note 25: Actuarial present value of future retirement benefits

CIPFA's Code of Practice on Local Authority Accounting 2015/16 requires administering authorities of LGPS funds that prepare pension fund accounts to disclose what IAS26 refers to as the actuarial present value of promised retirement benefits.

The actuarial present value of promised retirement benefits is to be calculated similarly to the defined benefit obligation under IAS19. There are three options for its disclosure in pension fund account:

- Showing the figure in the net asset statement, in which case it requires the statement to disclose the resulting surplus or deficit;
- as a note to the accounts; or
- by reference to this information in an accompanying report.

If an actuarial valuation has not been prepared at the date of the financial statements, IAS26 requires the most recent valuation to be used as a base and the date of the valuation disclosed. The valuation should be carried out using assumptions in line with IAS19 and not the Pension Fund's funding assumptions.

I have been instructed by the Administering Authority to provide the necessary information for the Surrey Pension Fund, which is the remainder of this note.

Balance sheet

Year ended	31 March 2015	31 March 2016
	£m	£m
Present value of promised retirement benefits	4,984	4,684

Liabilities have been projected using a roll forward approximation from the latest formal funding valuation as at 31 March 2013. I estimate this liability at 31 March 2016 comprises £2,356m in respect of employee members, £873m in respect of deferred pensioners and £1,455m in respect of pensioners. The approximation involved in the roll forward model means that the split of scheme liabilities between the three classes of member may not be reliable. However, I am satisfied the aggregate liability is a reasonable estimate of the actuarial present value of benefit promises. I have not made any allowance for unfunded benefits.

The above figures include both vested and non-vested benefits, although the latter is assumed to have a negligible value.

It should be noted the above figures are appropriate for the Administering Authority only for preparation of the accounts of the Pension Fund. They should not be used for any other purpose (i.e. comparing against liability measures on a funding basis or a cessation basis).

Assumptions

The assumptions used are those adopted for the Administering Authority's IAS19 report as required by the Code of Practice. These are given below. I estimate that the impact of the change of assumptions to 31 March 2016 is to decrease the actuarial present value by £462m.

Financial assumptions

My recommended financial assumptions are summarised below:

Year ended	31 March 2015	31 March 2016
Inflation/pension increase rate	2.4%	2.2%
Salary increase rate	3.8%	3.7%
Discount rate	3.2%	3.5%

Longevity assumptions

As discussed in the accompanying report, the life expectancy assumption is based on the Fund's VitaCurves with improvements in line with the CMI 2010 model, assuming the current rate of improvements has reached a peak and will converge to long term rate of 1.25% p.a. Based on these assumptions, the average future life expectancies at age 65 are summarised below:

	Males	Females
Current pensioners	22.5 years	24.6 years
Future pensioners*	24.5 years	26.9 years

*Future pensioners are assumed to be currently aged 45.

Commutation assumption

An allowance is included for future retirements to elect to take 25% of the maximum additional tax-free cash up to HMRC limits for pre-April 2008 service and 63% of the maximum tax-free cash for post-April 2008 service.

Professional notes

This paper accompanies my covering report titled 'Actuarial Valuation as at 31 March 2015 for IAS19 purposes' dated 15 April 2015. The covering report identifies the appropriate reliances and limitations for the use of the figures in this paper, together with further details regarding the professional requirements and assumptions.

Barry McKay FFA
28 April 2016
For and on behalf of Hymans Robertson LLP

Note 26: Additional Voluntary Contributions

Market Value 2014/15 £000	Position	Market Value 2015/16 £000
9,613	Prudential	10,207
<u>9,613</u>		<u>10,207</u>

Additional Voluntary Contributions, net of returned payments, of £2.2million were paid directly to Prudential during the year (£2.1million during 2014/15).

Note 27: Statement of investment principles

Full details of the fund's investment policy are documented in the Statement of Investment Principles. This is published in the pension fund's full annual report and on the Surrey Pension Fund website.

Note 28: Annual report

The Surrey Pension Fund Annual Report 2015/2016 provides further details on the management, investment performance and governance of the Fund.

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The Audit Findings for Surrey Pension Fund

DRAFT

This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report.

Year ended 31 March 2016

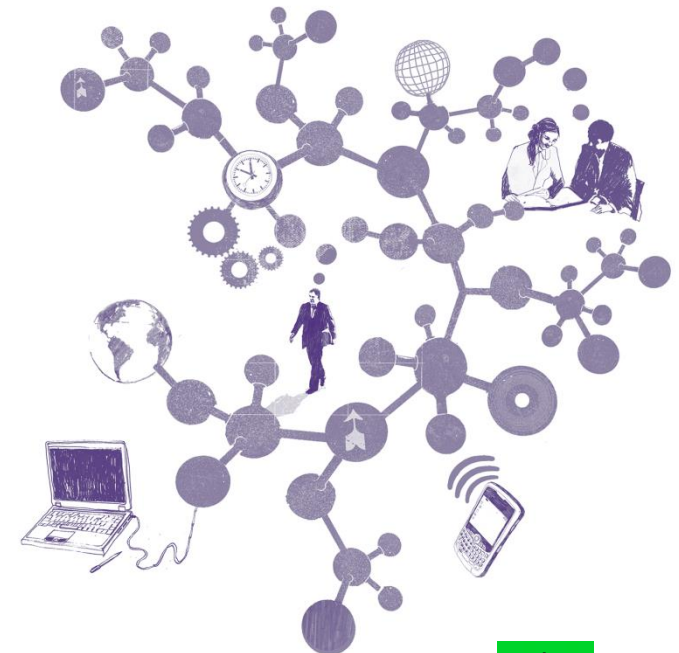
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Dear Members of the Audit and Governance Committee

Audit Findings for Surrey Pension Fund for the year ending 31 March 2016

This Audit Findings report highlights the significant findings arising from the audit for the benefit of those charged with governance (in the case of Surrey Pension Fund, the Audit and Governance Committee), as required by International Standard on Auditing (UK & Ireland) 260, the Local Audit and Accountability Act 2014 and the National Audit Office Code of Audit Practice. Its contents have been discussed with management.

As auditors we are responsible for performing the audit, in accordance with International Standards on Auditing (UK & Ireland), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

We would like to take this opportunity to record our appreciation for the kind assistance provided by the finance team and other staff during our audit.

Yours sincerely

Emily Hill
 Engagement Lead

Chartered Accountants

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Section 1: Executive summary

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- 01. Executive summary
- 02. Audit findings
- 03. Fees, non audit services and independence
- 04. Communication of audit matters

Purpose of this report

This report highlights the key issues affecting the results of Surrey Pension Fund ('the Fund') and the preparation of the Fund's financial statements for the year ended 31 March 2016. It is also used to report our audit findings to management and those charged with governance in accordance with the requirements of International Standard on Auditing (UK & Ireland) 260, and the Local Audit and Accountability Act 2014 ('the Act').

Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Fund's financial statements give a true and fair view of the financial position of the fund and its income and expenditure for the year and whether they have been properly prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting.

We are also required consider other information published together with the audited financial statements, whether it is consistent with the financial statements and in line with required guidance. This includes the Narrative Report and the Pension Fund Annual Report.

Introduction

In the conduct of our audit we have not had to alter or change our audit approach, which we communicated to you in our Audit Plan dated April 2016.

As at 8 July, our audit is substantially complete although we are finalising our procedures in the following areas:

- controls testing of new members
- review of the final version of the financial statements
- obtaining and reviewing the signed management letter of representation and
- updating our post balance sheet events review, to the date of signing the opinion

We received draft financial statements and accompanying working papers at the commencement of our work, in accordance with the agreed timetable.

We anticipate providing a unqualified audit opinion in respect of the financial statements (see Appendix B). We have not included our anticipated opinion on the Pension Fund Annual Report as this has yet to be prepared by management.

Key audit and financial reporting issues

Financial statements opinion

We have identified one adjustment affecting the Fund's reported financial position (details are recorded in section two of this report). The draft financial statements for the year ended 31 March 2016 recorded net assets available for benefits during the year of £3,223,628k; the audited financial statements show net assets available for benefits during the year of £3,223,663k. This change is driven by inclusion of accrued interest for short-term investments deposits that had been omitted in the draft financial statements and correction to the cash balance (both amendments are highly trivial to the financial statements). We have also recommended a small number of adjustments to improve the presentation of the financial statements.

The key messages arising from our audit of the Fund's financial statements are:

- Draft financial statements were provided for the agreed deadline of 10 June. There were a small number of omissions and inconsistencies in the accounts disclosures but these were far fewer in number than the previous year.
- Working papers were not provided at the start of fieldwork as agreed with the pensions team in April 2016. However, these were provided quickly when individually requested.
- Responses to queries were generally within the agreed timeframe and an improvement on the prior year.

We anticipate providing an unqualified opinion in respect of the Fund's financial statements.

Further details are set out in section two of this report.

Controls

Roles and responsibilities

The Fund's management is responsible for the identification, assessment, management and monitoring of risk, and for developing, operating and monitoring the system of internal control.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we report these to the Fund.

Findings

We draw your attention to an observation regarding controls in place for reconciling cash balances on the general ledger.

Further details are provided within section two of this report.

The way forward

Matters arising from the financial statements audit have been discussed with the Director of Finance.

We have made a number of recommendations, which are set out in the action plan at Appendix A. Recommendations have been discussed and agreed with the Director of Finance and the pensions and finance teams.

Acknowledgement

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

Grant Thornton UK LLP
July 2016

Section 2: Audit findings

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Communication of audit matters

This section summarises the findings of the audit, we report on the final level of materiality used and the work undertaken against the risks we identified in our initial audit plan. We also conclude on the accounting policies, estimates and judgements used and highlight any weaknesses found as part of the audit in internal controls. As required by auditing standards we detail both adjusted and unadjusted misstatements to the accounts and their impact on the financial statements.

Materiality

In performing our audit, we apply the concept of materiality, following the requirements of International Standard on Auditing (UK & Ireland) (ISA) 320: Materiality in planning and performing an audit. The standard states that 'misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements'.

As we reported in our audit plan, we determined overall materiality to be £31,935k (being 1% of net assets from the prior year audited accounts). We have considered whether this level remained appropriate during the course of the audit and have updated the calculation to reflect net asset figures per the 2015/16 draft financial statements, leading to materiality of £32,236k.

We also set an amount below which misstatements would be clearly trivial and would not need to be accumulated or reported to those charged with governance because we would not expect that the accumulated effect of such amounts would have a material impact on the financial statements. We have defined the amount below which misstatements would be clearly trivial to be £1,612k. Our assessment of the value of clearly trivial matters has been adjusted to reflect our revised materiality calculation.

As we reported in our audit plan, we identified the following items where we decided that separate materiality levels were appropriate. These remain the same as reported in our audit plan.

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Balance/transaction/disclosure	Explanation	Materiality level
Related party transactions	Due to public interest in these disclosures and the statutory requirement for them to be made.	Any errors identified by testing will be assessed individually, with due regard given to the nature of the error and its potential impact on users of the financial statements. We are unable to quantify a materiality level as the concept of related party transactions takes in to account what is material to both the Fund and the related party.
Cash and cash equivalents	The balance of cash and cash equivalents is usually material, and as the majority of your transactions affect the balance it is therefore considered to be material by nature also.	Any errors identified by testing in excess of £500k will be considered as to whether they would affect the users understanding of the financial statements.

Audit findings against significant risks

"Significant risks often relate to significant non-routine transactions and judgmental matters. Non-routine transactions are transactions that are unusual, either due to size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty" (ISA(UK&I)315).

In this section we detail our response to the significant risks of material misstatement which we identified in the Audit Plan. As we noted in our plan, there are two presumed significant risks which are applicable to all audits under auditing standards.

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
1.	<p>The revenue cycle includes fraudulent transactions</p> <p>Under ISA(UK&I)240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.</p>	<p>We rebutted this presumption during the interim phase of the audit and communicated this to you in our Audit Plan. We have not had reason to amend this judgement during the remainder of the audit.</p>	<p>Our audit work has not identified any material issues in respect of revenue recognition.</p>
2.	<p>Management over-ride of controls</p> <p>Under ISA(UK&I)240 it is presumed that the risk of management over-ride of controls is present in all entities.</p>	<p>Provide summary of work performed, e.g.</p> <ul style="list-style-type: none"> • review of entity controls • testing of journal entries • review of accounting estimates, judgements and decisions made by management • review of unusual significant transactions 	<p>Our audit work has not identified any evidence of management over-ride of controls. In particular the findings of our review of journal controls and testing of journal entries has not identified any significant issues.</p> <p>We set out later in this section of the report our work and findings on key accounting estimates and judgements.</p>

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Audit findings against significant risks (continued)

We have also identified the following significant risks of material misstatement from our understanding of the entity. We set out below the work we have completed to address these risks.

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
3.	<p>Level 3 Investments – Valuation is incorrect</p> <p>Under ISA(UK&I)315 significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.</p>	<ul style="list-style-type: none"> • We gained an understanding of the transaction including a review of supporting documentation. • We consider and documented management's controls over the valuation of these investments. • We carried out walkthrough tests of the controls identified in the cycle. • Tested a sample of private equity investments by obtaining and reviewing the audited accounts at latest date for individual investments and agreeing these to the fund manager reports at that date. Reconciliation of those values to the values at 31 March with reference to known movements in the intervening period. • Reviewed the qualifications of fund managers as experts to value the level 3 investments at year end and gained an understanding of how the valuation of these investments has been reached. • Reviewed the nature and basis of estimated values and considered what assurance management has over the year end valuations provided for these types of investments. • Reviewed the competence, expertise and objectivity of any management experts used. 	<p>Our audit work has not identified any material issues in respect of the risk identified.</p>

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Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan. Recommendations, together with management responses are attached at appendix A.

Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
Investment Income	Investment activity not valid. (Occurrence) Investment income not accurate. (Accuracy)	We have undertaken the following work in relation to this risk: <ul style="list-style-type: none"> Review of the reconciliation of information provided by the fund managers, the custodian and the Fund's own records and seek explanations for variances. Sample testing of investment income to fund manager reports ensure it is appropriate. Completion of a predictive analytical review for different types of investment income. 	Our audit work has not identified any material issues in respect of the risk identified.
Investment purchases and sales	Investment activity not valid. (Occurrence) Investment valuation not correct. (Valuation gross)	We have undertaken the following work in relation to this risk: <ul style="list-style-type: none"> Sample testing of material purchases and sales, agreeing these to supporting documentation. Review of the reconciliation of information provided by the fund managers, the custodian and the Fund's own records and seek explanations for variances. 	Our audit work has not identified any material issues in respect of the risk identified.
Investment values – Level 2 investments	Valuation is incorrect. (Valuation net)	We have undertaken the following work in relation to this risk: <ul style="list-style-type: none"> Review of the reconciliation of information provided by the fund managers, the custodian and the Fund's own records and seek explanations for variances. 	Our audit work has not identified any material issues in respect of the risk identified.

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Audit findings against other risks (continued)

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Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
<p>Contributions</p>	<p>Recorded contributions not correct (Occurrence)</p>	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> • Sample testing contributions from scheduled and admitted bodies to supporting documentation. • Controls testing over occurrence, completeness and accuracy of contributions. • Testing a sample of contributions to source data to gain assurance over their accuracy and occurrence, including contributions from Surrey County Council (co-ordinated with the Council's audit team). • Rationalise contributions received with reference to changes in member body payrolls and numbers of contributing pensioners to ensure that any unexpected trends are satisfactorily explained. • Monthly trend analysis of contributions received to determine whether contributions are largely consistent and investigate any anomalous results. 	<p>Our audit work has not identified any material issues in respect of the risk identified.</p>
<p>Benefits payable</p>	<p>Benefits improperly computed/claims liability understated (Completeness, accuracy and occurrence)</p>	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> • Controls testing over completeness, accuracy and occurrence of benefit payments. • Sample testing of individual pensions in payment by reference to member files. • Walkthrough tests of controls over benefit payments. • Rationalisation of pensions paid with reference to changes in pensioner numbers and increases applied in the year to ensure that any unusual trends are satisfactorily explained. • Monthly trend analysis of benefits paid to determine whether benefits are largely consistent and investigate any anomalous results. 	<p>Our audit work has not identified any material issues in respect of the risk identified.</p>





Audit findings against other risks (continued)

Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
<p>Member Data</p>	<p>Member data not correct. (Rights and Obligations)</p>	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> • Sample testing of changes to member data for new members, leavers and new pensioners that occurred during the year to source documentation. • Walkthrough tests of identified controls over member data. • Controls testing over annual/monthly reconciliations and verifications with individual members. • Sample testing of changes to member data for new members, leavers and new pensioners that occurred during the year to source documentation. 	<p>Subject to completion of our procedures as outlined on page 5, our audit work has not identified any material issues in respect of the risk identified.</p> <p>We will update the Audit and Governance Committee with the outcome of our work.</p> <p>As part of our controls testing of new starters, we identified that of the 11 cases tested, 52 new members did not receive the new starter letter as per the expected process. In these cases we were able to undertake additional testing and we did not identify further instances of this having taken place. This has no impact on the contribution figures in the Fund Account, nor the membership statistics included in the accounts. We have discussed the issue with the Pension Services Manager and acknowledge that this omission has been recognised and mitigating actions are planned during 2016. We have made a recommendation regarding continued implementation of this process as part of the action plan attached to Appendix A.</p>




Accounting policies, estimates and judgements

In this section we report on our consideration of accounting policies, in particular revenue recognition policies, and key estimates and judgements made and included with the Fund's financial statements.

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Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	The Fund's policy for recognition of contributions income and investment income is set out in note 3 to the financial statements.	The revenue recognition policy is consistent with the CIPFA Code of Practice on Local Authority Accounting and the findings from our audit of the financial statements.	 (Green)
Judgements and estimates	Key estimates and judgements disclosed in the notes to the financial statements include: <ul style="list-style-type: none"> - Valuation of unquoted private equity investments - Valuation of the Pension Fund liability 	We reviewed the key estimates and judgements made by management in the material notes to the financial statements. We concluded that in all instances they are consistent with guidance per the Code.	 (Green)
Going concern	Officers have a reasonable expectation that the services provided by the Fund will continue for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.	We have reviewed officer's assessment and are satisfied with management's assessment that the going concern basis is appropriate for the 2015/16 financial statements.	 (Green)
Other accounting policies	We have reviewed the Fund's policies against the requirements of the CIPFA Code and accounting standards.	We have reviewed the Fund's policies against the requirements of the CIPFA Code of Practice. The Fund's accounting policies are appropriate and consistent with previous years.	 (Green)

Assessment

-  (Red) Marginal accounting policy which could potentially attract attention from regulators (Red)
-  (Amber) Accounting policy appropriate but scope for improved disclosure (Amber)
-  (Green) Accounting policy appropriate and disclosures sufficient (Green)

Other communication requirements


We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

	Issue	Commentary
1.	Matters in relation to fraud	<ul style="list-style-type: none"> We have previously discussed the risk of fraud with the Audit and Governance Committee and not been made aware of any issues. We have not been made aware of any other incidents in the period and no other issues have been identified during the course of our audit procedures.
2.	Matters in relation to related parties	<ul style="list-style-type: none"> From the work we carried out, we have not identified any related party transactions which have not been disclosed.
3.	Matters in relation to laws and regulations	<ul style="list-style-type: none"> You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
4.	Written representations	<ul style="list-style-type: none"> A standard letter of representation has been requested from the Fund.
5.	Confirmation requests from third parties	<ul style="list-style-type: none"> We requested from management permission to send confirmation requests to the Fund's bank, fund managers, custodian and actuary. This permission was granted and the requests were sent. All of these requests were returned with positive confirmation.
6.	Disclosures	<ul style="list-style-type: none"> Our review found no material omissions in the financial statements.
7.	Matters on which we report by exception	<ul style="list-style-type: none"> We are required to report by exception where the Pension Fund Annual Report is inconsistent with the financial statements. Due to statutory deadlines the Pension Fund Annual Report is not required to be published until the 1 December 2016 and therefore this has not yet been produced. We are therefore unable to give a certificate of completion on the administering authority audit until this work has been completed.




Internal controls

The purpose of an audit is to express an opinion on the financial statements.

Our audit included consideration of internal controls relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. We considered and walked through the internal controls for Investment Income, Contributions, Benefits Payable and Member Data. The matters that we identified during the course of our audit are set out in the table below. These and other recommendations, together with management responses, are included in the action plan attached at Appendix A. We have reviewed the impact of this deficiency and note that we have not had to alter our audit approach as a result of this finding.

	Assessment	Issue and risk	Recommendation
1.	 (Green) Deficiency - risk of inconsequential misstatement	Cash balances Our testing identified accumulated unreconciled differences in the cash balance. Whilst these differences are trivial, the reconciliation of cash is an important control and the differences have increased on those identified in the previous year. Management have previously not corrected these differences as they have deemed them to be numerically insignificant, but they have adjusted for these differences in the current year financial statements.	Given the potential sensitivity of cash balances, unreconciled differences on cash balances should be fully adjusted on at least an annual basis.

Assessment

-  (Red) Material weakness – risk of material misstatement (Red)
-  (Amber) Significant deficiency – risk of significant misstatement (Amber)
-  (Green) Deficiency – risk of inconsequential misstatement (Green)

Adjusted misstatements

No adjustments to the draft accounts have been identified during the audit process. We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Unadjusted misstatements

We have not identified any unadjusted misstatements as a result of our audit procedures.

Misclassifications and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Adjustment type	Value £'000	Account balance	Impact on the financial statements
1 Disclosure	Market movements: 176,328	Note 17a - Reconciliation of movements in investments and derivatives	The draft financial statements showed an understatement of the prior year change in market value figures in the note when compared with the Fund Account. The draft figure was £176,328k, as compared with the value in the Fund Account of £299,210k. In addition, the purchases and sales figures in this part of the disclosure were also understated - the reason for all three differences is that the disclosure had not been updated from the comparator figures in the 2014/15 financial statements. Management have corrected for these differences, which have a disclosure impact only.
2 Disclosure	Cash: 37,000	Net asset statement	Of the cash balance, £37,000k relating to short-term investments to a number of local authorities have been reclassified as such as they do not constitute the definition of a short-term deposit. This change has no net impact on the financial statements.

Section 3: Fees, non-audit services and independence

- 01. Executive summary
- 02. Audit findings
- 03. Fees, non audit services and independence**
- 04. Communication of audit matters

We confirm below our final fees charged for the audit and confirm there were no fees for the provision of non audit services.

Fees

	Per Audit Plan £	Actual fees £
Pension fund scale fee	27,105	27,105
Total audit fees (excluding VAT)	27,105	27,105

Fees for other services

Service	Fees £
Audit related services	Nil
Non-audit services	Nil

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

Section 4: Communication of audit matters

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Communication of audit matters

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Communication to those charged with governance

International Standards on Auditing ISA (UK&I) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table opposite.

The Audit Plan outlined our audit strategy and plan to deliver the audit, while this Audit Findings report presents the key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

Respective responsibilities

The Audit Findings Report has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by Public Sector Audit Appointments Limited (<http://www.psa.co.uk/appointing-auditors/terms-of-appointment/>)

We have been appointed as the Fund's independent external auditors by the Audit Commission, the body responsible for appointing external auditors to local public bodies in England at the time of our appointment. As external auditors, we have a broad remit covering finance and governance matters.

Our annual work programme is set in accordance with the Code of Audit Practice issued by the NAO (<https://www.nao.org.uk/code-audit-practice/about-code/>). Our work considers the Fund's key risks when reaching our conclusions under the Code of Audit Practice.

It is the responsibility of the Fund to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Fund is fulfilling these responsibilities.

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	✓	
Overview of the planned scope and timing of the audit. Form, timing and expected general content of communications	✓	
Views about the qualitative aspects of the entity's accounting and financial reporting practices, significant matters and issues arising during the audit and written representations that have been sought		✓
Confirmation of independence and objectivity	✓	✓
A statement that we have complied with relevant ethical requirements regarding independence, relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged Details of safeguards applied to threats to independence	✓	✓
Material weaknesses in internal control identified during the audit		✓
Identification or suspicion of fraud involving management and/or others which results in material misstatement of the financial statements		✓
Non compliance with laws and regulations		✓
Expected modifications to auditor's report		✓
Uncorrected misstatements		✓
Significant matters arising in connection with related parties		✓
Significant matters in relation to going concern		✓

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Appendices

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Appendix A: Action plan

Priority

High - Significant effect on control system

Medium - Effect on control system

Low - Best practice

Rec No.	Recommendation	Priority	Management response	Implementation date & responsibility
1.	New starter letters should be sent to all new members of the pension scheme and a full review of those instances where this did not take place during 2015/16 should be undertaken.	Medium	A process review has been undertaken and an automated bulk process for generating new joiner letters has been initiated - process maps have been recorded as part of the Audit. The missing cases for 2015/16 have been identified as part of the process review and will be contacted as part of the bulk processing.	Pension Services Manager, September 2016
2.	Given the potential sensitivity of cash balances, unreconciled differences on cash balances should be fully adjusted on at least an annual basis.	High	Fund manager and custodian cash balances are currently monitored on a quarterly basis. Management will ensure that any variances will be fully adjusted as part of a quarterly reconciliation.	Senior Accountant, December 2016

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Appendix B: Audit opinion

We anticipate we will provide the Fund with an unqualified audit report.

DRAFT INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SURREY COUNTY COUNCIL

We have audited the pension fund financial statements of Surrey County Council (the "Authority") for the year ended 31 March 2016 under the Local Audit and Accountability Act 2014 (the "Act"). The pension fund financial statements comprise the Fund Account, the Net Asset Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

This report is made solely to the members of the Authority, as a body, in accordance with Part 5 of the Act and as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Director of Finance and auditor

As explained more fully in the Statement of Responsibilities, the Director of Finance is responsible for the preparation of the Authority's Statement of Accounts, which includes the pension fund financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16, which give a true and fair view. Our responsibility is to audit and express an opinion on the pension fund financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the pension fund financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the pension fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall presentation of the pension fund financial statements. In addition, we read all the financial and non-financial information in the Authority's Statement of Accounts to identify material inconsistencies with the audited pension fund financial statements and to identify any information that is apparently materially incorrect

based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on the pension fund financial statements

In our opinion the pension fund financial statements:

- present a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2016 and of the amount and disposition at that date of the fund's assets and liabilities; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 and applicable law.

Opinion on other matters

In our opinion, the other information published together with the audited pension fund financial statements in the Authority's Statement of Accounts is consistent with the audited pension fund financial statements.

Emily Hill
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

Grant Thornton House
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DRAFT July 2016



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Grant Thornton UK LLP
Grant Thornton House
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12 July 2016

Dear Sirs

Surrey Pension Fund

Financial Statements for the year ended 31 March 2016

This representation letter is provided in connection with your audit of the financial statements of Surrey Pension Fund ('the Fund') for the year ended 31 March 2016 for the purpose of expressing an opinion as to whether the financial statements show a true and fair view of the financial transactions of the Fund during the year ended 31 March 2016, and of the amount and disposition at that date of its assets and liabilities, in accordance with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 ('the Code').

We confirm that to the best of our knowledge and belief having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

Financial Statements

- 1 We have fulfilled our responsibilities for the preparation of the financial statements in accordance with proper practices as set out in the Code; which give a true and fair view in accordance therewith, and for keeping records in respect of contributions received in respect of active members.
- 2 We have complied with the requirements of all statutory directions affecting the Fund and these matters have been appropriately reflected and disclosed in the financial statements.
- 3 The Council has complied with all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.
- 4 We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud.
- 5 Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.
- 6 We acknowledge our responsibilities for making the accounting estimates included in the financial statements. Where it was necessary to choose between estimation techniques that comply with the Code, we selected the estimation technique considered to be the most appropriate to the Fund's particular circumstances for the purpose of giving a true and fair view. Those estimates reflect our judgement based on our knowledge and experience about past and current events and are also based on our assumptions about conditions we expect to exist and courses of action we expect to take.



- 7 We are satisfied that the material judgements used in the preparation of the financial statements are soundly based, in accordance with the Code and adequately disclosed in the financial statements. There are no other material judgements that need to be disclosed.
- 8 Except as disclosed in the financial statements:
- a there are no unrecorded liabilities, actual or contingent
 - b none of the assets of the Fund have been assigned, pledged or mortgaged
 - c there are no material prior year charges or credits, nor exceptional or non-recurring items requiring separate disclosure.
- 9 Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of the Code.
- 10 Actual or possible litigation and claims have been accounted for and disclosed in accordance with the requirements of the Code.
- 11 All events subsequent to the date of the financial statements and for which the Code requires adjustment or disclosure have been adjusted or disclosed.
- 12 We have considered the misclassification and disclosures changes schedules included in your Audit Findings Report. The financial statements have been amended for these misclassifications and disclosure changes and are free of material misstatements, including omissions.
- 13 We believe that the Fund's financial statements should be prepared on a going concern basis on the grounds that current and future sources of funding or support will be more than adequate for the Fund's needs. We believe that no further disclosures relating to the Fund's ability to continue as a going concern need to be made in the financial statements.
- 14 We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

Information Provided

- 15 We have provided you with:
- a access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - b additional information that you have requested from us for the purpose of your audit; and
 - c unrestricted access to persons from whom you determined it necessary to obtain audit evidence.
- 16 We have communicated to you all deficiencies in internal control of which management is aware.
- 17 We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- 18 All transactions have been recorded in the accounting records and are reflected in the financial statements.
- 19 We have disclosed to you all our knowledge of fraud or suspected fraud affecting the Fund involving:

- a management;
- b employees who have significant roles in internal control; or
- c others where the fraud could have a material effect on the financial statements.

20 We have disclosed to you all our knowledge of any allegations of fraud, or suspected fraud, affecting the Fund's financial statements communicated by employees, former employees, analysts, regulators or others.

21 We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

22 We have disclosed to you the identity of all the Fund's related parties and all the related party relationships and transactions of which we are aware.

23 We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.

Approval

The approval of this letter of representation was minuted by the Council's Audit and Governance Committee at its meeting on 25 July 2016.

Yours faithfully

Name.....

Position.....

Date.....

Name.....

Position.....

Date.....

Signed on behalf of Surrey County Council as administering body of the Surrey Pension Fund

