Notice of Meeting

Surrey Pension Fund Board

Date & time	Place	Contact	Chief Executive
Friday, 19 September 2014 at 9.30 am	Ashcombe Suite, County Hall, Kingston upon Thames, Surrey KT1 2DN	Cheryl Hardman Room 122, County Hall Tel 020 8541 9075 cherylh@surreycc.gov.uk	David McNulty

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This meeting will be held in public. If you would like to attend and you have any special requirements, please contact Cheryl Hardman on 020 8541 9075.

Elected Members
Ms Denise Le Gal (Chairman), Mr Nick Skellett CBE (Vice-Chairman), Mr W D Barker OBE, Mr Tim Evans, Mr John Orrick and Mr Stuart Selleck

Co-opted Members:
Mr Tony Elias (District Representative), Judith Glover (Borough/District Councils), Ian Perkin (Office of the Surrey Police and Crime Commissioner) and Philip Walker (Employees)

AGENDA

1 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

2 MINUTES OF THE PREVIOUS MEETING: 15 MAY 2014

(Pages 1 - 40)

To agree the minutes as a true record of the meeting.

3 DECLARATIONS OF INTEREST

To receive any declarations of disclosable pecuniary interests from Members in respect of any item to be considered at the meeting.

Notes:

- In line with the Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012, declarations may relate to the interest of the member, or the member's spouse or civil partner, or a person with whom the member is living as husband or wife, or a person with whom the member is living as if they were civil partners and the member is aware they have the interest.
- Members need only disclose interests not currently listed on the Register of Disclosable Pecuniary Interests.
- Members must notify the Monitoring Officer of any interests disclosed at the meeting so they may be added to the Register.
- Members are reminded that they must not participate in any item where they have a disclosable pecuniary interest.

4 QUESTIONS AND PETITIONS

To receive any questions or petitions.

Notes:

1. The deadline for Member's questions is 12.00pm four working days before the meeting (*15 September 2014)*.
2. The deadline for public questions is seven days before the meeting (*12 September 2014)*.
3. The deadline for petitions was 14 days before the meeting, and no petitions have been received.

5 ACTION TRACKING

(Pages 41 - 46)

An action tracker is attached, detailing actions from previous meetings. The Board is asked to review progress on the items listed.

6 INVESTMENT STRATEGY REVIEW

Report to follow.

7 MANAGER ISSUES AND INVESTMENT PERFORMANCE (Pages 47 - 72)

This report is a summary of all manager issues that need to be brought to the attention of the Pension Fund Board, as well as manager investment performance.

8 SURREY PENSION FUND ACCOUNTS 2013/14 (Pages 73 - 150)

This report presents the audited financial statements of the Pension Fund for the year ended 31 March 2014, with respect of the County Council's obligations as the administering authority under the Local Government Pension Scheme (LGPS) Regulations.

The external auditor (Grant Thornton) has issued an unqualified opinion on the accounts and this is outlined in the Audit Findings for Surrey Pension Fund Report.

9 PENSION FUND RISK REGISTER (Pages 151 - 156)

Surrey County Council, as administering authority for the Surrey Pension Fund, is responsible for the delivery of benefit promises made to members of the Surrey Pension Fund. It achieves this by setting objectives and goals with varying timeframes. Risks lie in failing to meet the intended goals.

Risks that are established as an issue must be identified and evaluated via a risk register. The risks must be prioritised with existing controls or new controls implemented to mitigate the risks. This should be recorded in a risk register, which needs monitoring on a quarterly basis.

10 REVISED STATEMENT OF INVESTMENT PRINCIPLES (Pages 157 - 174)

With adjustments to asset allocation within the Pension Fund, it is necessary to approve a revised Statement of Investment Principles (SIP).

11 KEY PERFORMANCE INDICATORS (Pages 175 - 180)

In line with best practice, Pension Fund Board members will be supplied with Pension Fund key performance indicators (KPIs) on a quarterly basis, covering investment and administration practices.

12 CORPORATE GOVERNANCE SHARE VOTING (Pages 181 - 196)

This report provides a summary of the Fund's share voting process in Q1 2014/15.

13 **LOCAL GOVERNMENT PENSION SCHEME: DRAFT GOVERNANCE REGULATIONS** (Pages 197 - 224)

The report explains the planned changes to the governance of the Local Government Pension Scheme (LGPS) as a result of the Public Service Pensions Act 2013 and draft Regulations recently issued. A key requirement is for a proposed new local Pension Scrutiny Board to monitor compliance with rules and standards.

14 **LGPS REFORM: OPPORTUNITIES FOR COLLABORATION, COST SAVINGS AND EFFICIENCIES** (Pages 225 - 232)

On 21 June 2013, the Department for Communities and Local Government (DCLG) issued a call for evidence on the future structure of the Local Government Pension Scheme. A document was submitted on behalf of the Pension Fund Board, in consultation with the Chairman of the Pension Fund Board. On 1 May 2014, the Government published a further consultation document, which acknowledged the initiatives put in place by many administering authorities with regard to collaboration and the set up of collective investment vehicles.

15 **DATE OF NEXT MEETING**

The next meeting of the Surrey Pension Fund Board will be on 14 November 2014. The Surrey Pension Fund AGM will be on 21 November 2014.

David McNulty
Chief Executive
Published: Date Not Specified

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MINUTES of the meeting of the **SURREY PENSION FUND BOARD** held at 9.30 am on 15 May 2014 at Ashcombe Suite, County Hall, Kingston upon Thames, Surrey KT1 2DN.

These minutes are subject to confirmation by the Committee at its next meeting.

Elected Members:

* Ms Denise Le Gal (Chairman)
* Mr Nick Skellett CBE (Vice-Chairman)
* Mr W D Barker OBE
* Mr Tim Evans
* Mr John Orrick
* Mr Stuart Selleck

Ex officio Members:

Mr David Munro, Chairman of the County Council
Mrs Sally Ann B Marks, Vice Chairman of the County Council
Mr David Hodge, Leader of the Council
Mr Peter Martin, Deputy Leader

Co-opted Members:

* Mr Tony Elias, District Representative
* Judith Glover, Borough/District Councils
* Ian Perkin, Office of the Surrey Police and Crime Commissioner
Philip Walker, Employees

In attendance

Paul Baker, Pensions Manager
Helen Gibson, Pensions Regulator
Cheryl Hardman, Regulatory Committee Manager
John Harrison, Surrey Pension Fund Advisor
Sheila Little, Chief Finance Officer (Section 151 Officer)
Alex Moylan, Senior Accountant
Robert Plumb, Pensions Regulator
Phil Triggs, Strategic Manager – Pension Fund & Treasury
Steve Turner, Partner, Mercer
Matt Woodman, Hymans Robertson
John Wright, Hymans Robertson - Actuary

16/14 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS [Item 1]

Apologies for absence were received from Philip Walker.

The Chairman informed the Committee that Mike Goodman had been promoted to the Cabinet and so had stood down from the Surrey Pension Fund Board. She thanked Mr Goodman for his work on the Board, in particular with the establishment of the Risk Register.

Tim Evans had been appointed to the Board. He is a knowledgeable Member with 35 years experience in pensions.

17/14 MINUTES OF THE PREVIOUS MEETING [14 FEBRUARY 2014] [Item 2]

The Minutes were agreed as an accurate record of the meeting subject to a change to the date on which the Minutes were to be agreed.

18/14 DECLARATIONS OF INTEREST [Item 3]

There were no declarations of interest.

19/14 QUESTIONS AND PETITIONS [Item 4]

There were none.

20/14 ACTION TRACKING [Item 5]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. Many of the actions from previous meetings would be addressed at the current meeting.

Actions/Further Information to be Provided:
None.

Resolved:
That the actions tracker was noted and the committee agreed to remove the completed actions from the tracker.

Next steps:
None.

21/14 MANAGER ISSUES AND INVESTMENT PERFORMANCE [Item 6]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report. He highlighted the recommendation by the Fund's independent advisor that attention be given to the question of rebalancing. The Chairman suggested that the committee return to this issue at the end of the meeting.

2. The committee had previously asked at what rate did Surrey County Council charge for loans (**Action Review ref: A5/14**). This information was included in the committee report. Such rates were assessed by speaking with money market brokers on the morning such transactions were planned to take place.
3. The Chairman suggested that the list of strategies, policies and reporting frameworks approved by the Board underlined how much work had been undertaken in the past year. The Board now had a comprehensive set of strategies and policies. She thanked officers for their hard work.
4. The Strategic Manager – Pension Fund & Treasury highlighted the improved performance of the markets over the past few weeks and stated that the estimated market value of the Fund as of 15 May 2014 was £2,806m.

Tony Elias joined the meeting.

5. With regard to the performance of Fund Managers, the Strategic Manager – Pension Fund & Treasury highlighted the under-performance of Franklin Templeton in Quarter 4 and the significant out-performance of Majedie.

Tim Evans joined the meeting.

6. Members expressed some concern about Newton's performance. The Surrey Pension Fund Advisor confirmed that Newton was still pursuing a thematic based investment philosophy. Changes to the global equity team had been made in 2012, which had resulted in a reduction in the number of stocks held in the portfolio from around 120 to 80 holdings in order for the manager to demonstrate greater conviction in its investment ideas. It was noted that Newton had maintained a relatively cautious approach to investing which had been reflected in their portfolio. Given the strong rise in markets over the last couple of years it was questioned whether Newton had been too slow to change its view, which may have impacted relative performance. He advised keeping an eye on Newton. The Chairman asked the Surrey Pension Fund Advisor to keep a watching brief on Newton and suggested that the Board review whether to invite Newton to a future meeting after a further quarter's performance results are published (**Action Review ref: A9/14**).
7. Officers confirmed that CBRE had been high on the agenda over the past 18 months. The performance target for the mandate had been discussed with them and subsequently revised. The allocation to CBRE has also been increased through additional funding which was specifically aimed to help the manager reduce the portfolio's exposure to the closed-ended European property holdings. The Mercer representative explained that while the UK element of the property portfolio was doing well, the European property funds continued to detract from relative performance. However, this wasn't as much of a problem now as it was.
8. The Surrey Pension Fund Advisor introduced and expanded on the notes of his meetings with Fund Managers.

2

9. A member of the Board queried whether the situation in Ukraine could have any impact on the Pension Fund through gas supply disputes. The Mercer representative confirmed that the Surrey Pension Fund does have a small exposure through Franklin Templeton. The Surrey Pension Fund Advisor added that impacts from the Ukrainian crisis had not been seen widely in financial markets. There was continued concern from some Members of potential future effects.
10. In response to a query about why the Fund would be investing in a bond mandate which had a low duration position of 1.4 years, the Surrey Pension Fund Advisor explained that the logic of Franklin Templeton's approach was to develop a portfolio with broad, diversified sources of return from global income and currency markets. The Chairman highlighted that Franklin Templeton had an unconstrained, somewhat contrarian investment approach, which could potentially lead to underperformance in the short-term, but that the manager had a strong track record over the long-term.

Actions/Further Information to be Provided:
Board to review whether to invite Newton to a future meeting after a further quarter's performance results are published.

Resolved:

a. To approve the report and the decisions as laid out.
b. To postpone the decisions on rebalancing whether to make a USD 20m commitment to the Standard Life Secondary Opportunities Fund 11 (SOF 11) to the end of the meeting.

Next steps:
None.

22/14 PRIVATE EQUITY INVESTMENT PERFORMANCE REVIEW [Item 7]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report and highlighted that estimates suggest that the target level of return sought from the Surrey private equity programme had been exceeded.
2. There was concern that one specific manager was reluctant to share its Internal Rate of Return (IRR). The Surrey Pension Fund Advisor stated that IRRs tend to show Investment Managers in a good light so it was worrying that the manager would not share this information. The Strategic Manager – Pension Fund & Treasury agreed to request the data for the various funds.
3. Following a discussion about the measurement of private equity performance and the value of using the IRR to present performance, the Chairman requested that future reports present a cash flow analysis of how payments are received over time (**Action Review ref: A10/14**).

Actions/Further Information to be Provided:
Future reports on private equity performance to present a cash flow analysis of how payments are received over time.

Resolved:

a. That the Board notes the current position on the Fund's Private Equity investment performance; and
b. That the Fund continues to commit to follow on funds of the existing private equity managers as they become available and subject to each case going to the Pension Fund Board for approval.

Next steps:
None.

23/14 PENSION FUND BUSINESS PLAN 2013/14: OUTTURN REPORT AND FINAL 2014/15 PLAN [Item 8]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report and then the Pension Manager provided an update on preparation for the new LGPS 2014 scheme. He stressed the lengths the officers had gone to, to keep the Pension Fund membership informed. 70-80 presentations had been made to employee members of the fund and seven employer workshops had taken place. Guidance notes had also been issued. The major changes that payroll departments had to undertake were impressed upon the Board. However all deadlines had been met.
2. The results of the Governance Self-Assessment completed by members of the Board were tabled and are attached as Annexes 1 and 2. The Strategic Manager – Pension Fund & Treasury explained that the rating was from 1 (good) to 5 (poor). The average rating was then calculated for each question and presented alongside the range of responses. The Chairman felt that the big issues to be taken from the self-assessment were that the Board does not have enough time to be truly effective and that meetings do not allow sufficient focus on the 'big picture' strategic issues. She opened up a discussion on how this could be addressed. Members felt that there was value in having additional training and informal discussions between formal Board meetings. The Board wished to develop a general consensus on where the market is headed and an understanding of what other Pension Fund Boards were doing. Pre-meetings with the Pension Fund Board Advisor and the Mercer representative were also supported to ensure that members had the right questions when meeting Fund Managers. There was little support for increasing the number of formal Board meetings. The possibility of having a smaller Investment Sub-Committee was discussed to allow changes to the Investment strategy to be driven through. However there was some concern that this would lead to some members of the Board being more informed than others. The Strategic Manager – Pensions Fund & Treasury was asked to bring a report recommending a way forward for the Board (**Action Review ref: A11/14**).

2

3. The Chairman suggested that a training needs analysis be carried out by the Board later in the year, adapting the CIPFA questions used previously by the Pension Fund Panel (**Action Review ref: A12/14**).

Actions/Further Information to be Provided:

i. A report to be brought to the next meeting of the Surrey Pension Fund Board on how to address the results of the Governance Self-Assessment.
ii. A training needs analysis to be conducted later in the year.

Resolved:

a. That progress with regard to the Business Plan objectives in respect of the 2013/14 financial year be noted.
b. That the final version of the 2014/15 Business Plan be approved.

Next steps:
None.

24/14 ACTUARIAL VALUATION 2013: OUTCOME [Item 9]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report and acknowledged the work of the Pensions Administration Team in terms of ensuring high quality data is held in respect of the Fund's membership.
2. The disbanding of the pooling arrangements in respect of parish councils and other admitted bodies as a result of the actuarial valuation was highlighted. The timing of introducing individualised contribution rates for employers according to their own liability profile was challenging because of the budget-setting timetable across employer bodies. This meant the consultation was not possible which had led to some dissatisfaction with the process followed. However, the Fund had no option but to accept the recommendations from the actuary so the outcome of any consultation would have been the same as what happened in practice. Members highlighted the difficulties that parish councils have in explaining the impact on the parish council precept to parishioners.
3. The Strategic Manager – Pension Fund & Treasury introduced the Funding Strategy Statement which had been consulted upon since the previous Surrey Pension Fund Board meeting. He also confirmed that District and Borough Councils had flexibility to reduce their deficit recovery period.

Actions/Further Information to be Provided:
None.

Resolved:

a. That the report be noted and the 2013 Actuarial Valuation and Rates & Adjustments Certificate be adopted.
b. That the final version of the Funding Strategy Statement be approved.

Next steps:
None.

25/14 PENSION FUND RISK REGISTER [Item 10]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report, highlighting the changes since the previous meeting. The risks of bond yields falling and pay & price inflation had been reassessed and were now listed as the top two risks for the Pension Fund. Although longevity had fallen to the third risk it was still a core risk for the Fund. Mitigating actions outlined for the top three risks were not considered sufficient to address the risks and so the net risk score was the same as the total risk score.
2. The mismatching of assets and liabilities had been raised from the 15th risk on the register to the fourth risk. The Chairman stated that she was not convinced that assets and liabilities mismatching was that high a risk for the Fund. The Hymans Actuary suggested that if the Fund took a full asset to liabilities matching approach now the contributions required would be unaffordable. However, the Board needs to check that the Fund is not taking more risks than necessary.
3. Members suggested that the Board needs to focus on the long-term future and getting to full funding. The Mercer representative suggested that the Investment Strategy review later on the agenda would help the Board develop a clear idea of where it wants to get to and the Strategy that should be in place when it gets there.
4. Members queried what assumptions Hymans Robertson uses for the potential reduction in the workforce as a result of the pressures that the public sector is under. The Hymans Actuary responded that there is a risk of the workforce collapsing and this has been addressed through risk management processes. If payroll shrinks, this would have an impact of reduced contributions to the Fund. Mitigating actions are listed for the workforce diminishing in a short period of time.
5. Members suggested that some of the risks appear very similar, eg risks 1, 2, 4 & 10. Officers agreed that the risks could be reviewed to make the register more concise but the Board was also reminded of the objective for the register to be explicit (**Action Review ref: A13/14**). Members requested for Risk 36 to be dropped from the register (**Action Review ref: A14/14**). A further risk to address the implementation of the proposed changes to the LGPS was requested (**Action Review ref: A15/14**).

Actions/Further Information to be Provided:

i. Risks to be reviewed to make the register more concise.
ii. Risk 36 to be dropped from the register.
iii. A risk to address the implementation of the proposed changes to the LGPS to be added.

2

Resolved:
That the Risk Register be noted and amendments made reflecting the discussion at the Board meeting.

Next steps:
None.

The Board meeting was adjourned from 11.15am to 11.30am for a short break.

26/14 REVISED STATEMENT OF INVESTMENT PRINCIPLES [Item 11]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the revised Statement of Investment Principles. He explained that the changes were cosmetic and the opportunity had been taken to revise the section dealing with the CIPFA/Myners principles.
2. In response to a question about whether all of the Fund's Investment Managers were from the UK, the Mercer representative stated that Western Asset Management was headquartered in Pasadena although it had an investment team in London. Franklin Templeton is based in San Francisco but also has an investment team in London.
3. It was suggested and agreed that section 2(ii) of the Statement of Investment Principles should state: "To have a strategic asset allocation that is both well diversified and expected to provide long term investment returns in excess of the anticipated rise in the *value of the* Fund's liabilities" (**Action Review ref: A16/14**).

Actions/Further Information to be Provided:
The Statement of Investment Principles to be amended as agreed in point 3.

Resolved:
That the revised Statement of Investment Principles be approved subject to amendments as discussed at the meeting.

Next steps:
None.

27/14 KEY PERFORMANCE INDICATORS [Item 12]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. An updated KPI Statement was tabled and is attached to the Minutes as Annex 3.
2. The Pensions Manager introduced the report. The Employer Satisfaction Survey results had now been included and the target performance level had been passed.

3. The Strategic Manager – Pension Fund & Treasury also highlighted the Internal Audit report on Pensions Administration which had been found to be effective.
4. In response to a query, the Strategic Manager – Pension Fund & Treasury explained that the performance in Q4 2012/13 had been very good and it was not possible to continue to replicate such a significant return. Rolling forward, the annual return would be impacted by the dropping out of a quarter's significantly high performance.
5. The Strategic Manager – Pension Fund & Treasury agreed to include the estimated deficit of the Fund in future KPI Statements, while making it clear that it is an estimated market value and not an actuarial valuation (**Action Review ref: A17/14**).

Actions/Further Information to be Provided:
To include the estimated deficit of the Fund in future KPI Statements, while making it clear that it is estimated market value and not an actuarial valuation.

Resolved:
That the KPI Statement be noted.

Next steps:
None.

28/14 PENSION FUND ADMINISTRATION SERVICE LEVEL AGREEMENT [Item 13]

Declarations of Interest:
None.

Key Points Raised During the Discussion:
1. The Pensions Manager introduced the report and highlighted that the welcome packs for new scheme members was an electronic pack. Retired members receive a paper payslip when rates change.
2. The Service Level Agreement would be published on the Pension Fund website once it had been agreed (**Action Review ref: A18/14**).
3. Members were assured that Internal Audit look at Pensions Administration annually and pointed out that the last report had been included as an annex to the previous item. The service had been found to be effective.
4. Appeals following a complaint against the Pensions Administration team would be heard by a Panel of senior officers: the Pensions Manager, Head of Legal & Democratic Services, and Chief Finance Officer. In response to a query, the Pensions Manager stated that appeals were better dealt with under delegated powers as they could be quite technical and invariably were concerned with ill-health retirements.

Actions/Further Information to be Provided:
The Service Level Agreement to be published on the Pension Fund website

Resolved:
That the Service Level Agreement be approved.

Next steps:
None.

29/14 CORPORATE GOVERNANCE SHARE VOTING [Item 14]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report.
2. In response to a query about how many votes were taken against the advisor's recommendation, the Strategic Manager – Pension Fund & Treasury informed the Board that this had happened once during Q4. The Local Authority Pension Fund Forum had recommended that Funds vote against the Barclays remuneration policy and the Surrey Pension Fund followed this advice. The advice from Manifest had been to vote for the remuneration policy as not paying a market bonus would lead to staff leaving. The Chairman stated that the remuneration policy had still been pushed through but the vote was marginal.
3. Members queried why some votes were singled out for consideration by the Board. The Chairman reminded the Board that it had asked officers to send them details of the most contentious/newsworthy votes.
4. The Strategic Manager – Pension Fund & Treasury informed the Board that it was a rare occurrence when votes against company boards were carried. However, he pointed out that while votes against company boards may not be carried at the time of the vote, they often help make the case for change. He gave the example of Marks & Spencer appointing a joint Chief Executive and Chairman. The Local Authority Pension Fund Forum had run a well-supported campaign for separate individuals to hold these posts. The vote against management was not carried although it was a record vote in favour of the resolution at the time. A short time later Marks & Spencer did change their policies and decide to conform to the campaigns objectives.

Actions/Further Information to be Provided:
None.

Resolved:

a. That the report on Corporate Governance Share Voting be noted.
b. That the Responsible Investment and Stewardship Policy for 2014/15 be approved.

Next steps:
None.

2

30/14 LGPS REFORM: OPPORTUNITIES FOR COLLABORATION, COST SAVINGS AND EFFICIENCIES [Item 15]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Hymans Actuary tabled a briefing note summarising the Hymans Robertson cost-benefit analysis of fund merger and asset pooling (attached as Annex 4). A further consultation had been announced on 1 May 2014 by DCLG, which acknowledges the initiatives put in place by many administering authorities with regard to collaboration and the set up of collective investment vehicles (CIVs). Hymans had demonstrated that full Fund mergers would delay savings and so the DCLG consultation now rules out mergers and concentrates on asset pooling. The value of local decision-making had also been recognised by the government.
2. The Hymans Robertson representatives highlighted the finding that over the past ten years Local Government Pension Funds in aggregate would have achieved the same outcome if they had invested passively, with significantly lower fees. However, they argued that they were not recommending that the whole of the LGPS goes passive. Where a Fund has good governance it should continue what it has been doing. Where it has poor governance it could move to a passive investment strategy. The representatives then ran through the consultation questions and highlighted the key issues to be considered. They also stated that the consultation invites thoughts on reducing fund deficits although this is not one of the five consultation questions.
3. The Hymans Actuary confirmed that there are currently no CIVs in the market for the LGPS. The London Boroughs are presently setting up a CIV and counties may be able to use them.
4. The Hymans Robertson representatives informed the Board that there are only eight to ten equity managers across the LGPS. If CIVs are established, they are likely to be run by the same investment managers. Benefits of CIVs could include a reduction in fees. The Chairman stated that some investment managers were already voluntarily reducing fees to merged funds. Further benefits of CIVs would include savings on transactional costs as purchases and sales could be netted off.
5. Members were encouraged by the modification of the government’s plans in response to evidence.
6. The Hymans Actuary suggested that there should be a good response rate to the consultation and that the concepts in the consultation would benefit all funds.
7. The Chairman suggested that poorly run schemes could consider asking well run schemes to take them over.
8. In response to a query, the Hymans representatives stated that a move to passive investment strategies by local authority pension funds would have no impact on the market in aggregate.
9. Members felt that there was a timing issue and that, by moving quickly, greater benefits could be achieved.

The Board adjourned for lunch from 12.50pm to 1.30pm.

10. Members suggested that the initial response to the call for evidence be reviewed and arguments repeated in response to this consultation.
11. The Chairman stressed that the consultation response should highlight good governance and absorb the Hymans Robertson arguments.

Actions/Further Information to be Provided:
None.

Resolved:
a. That the report be noted.
b. That officers be authorised to respond to the consultation with views expressed within the forum of the Board meeting.

Next steps:
None.

31/14 NATIONAL CHANGES TO THE LGPS [Item 16]

Declarations of Interest:
None.

Key Points Raised During the Discussion:
1. The Strategic Manager – Pension Fund & Treasury introduced the report and explained the background to the preparation of the paper for South East 7 attached as Annex 1 to the report. He informed the Board that there would be an officer meeting on 28 May 2014 to work on proposals and that he would report back on the outcomes of that meeting (**Action Review ref: A19/14**). This may be through an informal meeting of the Board.
2. The Chairman informed the Board that the Leader of the Council was particularly keen to look at opportunities for collaboration within the South East 7.
3. The Chairman clarified that while the negotiations were confidential, the report was a public document and had been published on the website.
4. The Chairman informed the Board that Westminster City Council had awarded Surrey with its Pensions Administration and this would come into effect on 1 September 2014. The Surrey Pension Fund already has a partnership with East Sussex which includes pensions administration. This is now fully integrated. There are opportunities to learn from partnerships. For example, Surrey gained a procurement portal from East Sussex and there are functions and practice which has been shared with East Sussex.
5. The Surrey Pension Fund Advisor suggested that there would be other local authorities looking for support on various functions, eg where internal investment managers are close to retirement, funds may look to other local authorities for support.

6. In response to a query about whether there was any limit on the size of mergers or collaboration, the Hymans representatives suggested that there was a scale issue. Large funds were good for infrastructure and liquid assets but not if the investments are being actively managed. Large scale funds can also lead to them being remote from employers although it is possible to keep a local touch while benefiting from limiting replication of written communications. The application of scale requires consideration.

Actions/Further Information to be Provided:
Strategic Manager – Pension Fund & Treasury to report back on the outcomes of the officer meeting on 28 May 2014 before the next meeting of the Surrey Pension Fund Board.

Resolved:
That the report be noted.

Next steps:
None.

The meeting adjourned for a break from 1.50pm to 2.05pm.

32/14 INVESTMENT STRATEGY REVIEW [Item 17]

Declarations of Interest:
None.

Key Points Raised During the Discussion:
1. The Strategic Manager – Pension Fund & Treasury introduced the report which had been discussed informally with Board members. There was a lengthy debate, with key points including:
2. The Chairman queried why some investment advisors (including Mercer) were recommending that LGPS funds establish a liability-driven investment strategy when funds were still a relatively long way from being fully funded. The Mercer representative explained the need to start implementing changes now to prepare for a change to the investment strategy once the fund was fully funded. If the Board waits until it gets to 100% funding, it will very likely miss the opportunity to move to a new strategy when the time is right as the building blocks won't be in place.
3. The Mercer representative highlighted the proposed strategy on page 271 of the agenda packs.
4. The Chairman suggested that she didn't disagree with the strategy but with the timing. She queried the definition used for growth assets which she felt were not currently 91.2% of investments. The Mercer representative highlighted the breakdown of growth assets on page 265 of the agenda packs. There was some debate amongst Members, officers and advisors about the definition applied, in particular in relation to Corporate Bonds. The Mercer representative explained that he considered the main role of this asset class for the Fund was as a return-seeking asset. It was acknowledged that some downside protection was provided relative to adverse movements in the value of the liabilities but that this would not be significant given

2

the low level of interest sensitivity and lack of any direct linkage to inflation.

5. The Chairman suggested that the Surrey Pension Fund was not currently taking excessive risks, given the level of funding. The Mercer representative suggested that as the funding level improves it is possible to take risk off the table and that a clear plan should be in place to achieve this.
6. The Hymans Actuary suggested that there was a question over whether a large deficit matters and whether the Fund should therefore be seeking to reduce risk. The Mercer representative agreed that Surrey needs to decide if it is happy with the current level of deficit risk. The liabilities are likely to continue to increase, even with good performance by investments.
7. The Pensions Regulator stated that it was not clear if the Regulator would have any remit over investment strategies.
8. The Hymans actuary suggested that if it is intended to de-risk in the future, governance should be put in place early on. Procedures should state what the actuary is expected to do and what the Fund's advisors are expected to so.
9. Members were unhappy to give full approval to the suggested changes at the present meeting. The Chairman requested that three fund managers be invited to an informal meeting of the Board to help it to understand the approach being recommended. It was also suggested that a fee exercise be conducted (**Action Review ref: A20/14**).

Actions/Further Information to be Provided:

i. Three fund managers to be invited to an informal meeting of the Board to help it to understand the approach being recommended. A fee exercise also to be conducted.
ii. The Board to receive training on synthetic equities.

Resolved:

a. That the Pension Fund Board agrees to investing in a more risk aware manner relative to the Fund's liabilities with a view to the establishment of a liability driven investment strategy (LDI) portfolio. This should be set up on a relatively small scale initially with the level of liability protection increased as and when the funding level moves towards 100%.
b. That the Pension Fund Board agrees to explore leveraged gilts.
c. That the Pension Fund Board agrees to explore more diversified sources of return with a view to introducing Infrastructure Debt as a new asset category and increasing the existing allocation to diversified growth funds (DGF).
d. That the Pension Fund Board does not agree at this time to setting up a framework for a synthetic equity portfolio. However, the Chairman suggested that this would be a useful area to receive training on in the future (**Action Review ref: A21/14**).
e. That the Pension Fund Board agrees to implementing such changes in the short term, thus preparing a platform for the future strategy requirements, with the ultimate view to locking in some of the improvement in the funding level that has been seen since the valuation date of 31 March 2013.

f. That the Pension Fund Board agrees to receive ongoing training and Board reports in order to facilitate a definitive decision making process on these strategy issues at future Board meetings. This will include an informal meeting before the next formal Board meeting at which three fund managers will be present to help the Board understand the process being recommended.

Next steps:
None.

33/14 EXCLUSION OF THE PUBLIC [Item 18]

RESOLVED: That under Section 100(A) of the Local Government Act 1972, the public be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information under paragraph 3 of Part 1 of Schedule 12A of the Act.

THE FOLLOWING ITEMS OF BUSINESS WERE CONSIDERED IN PRIVATE BY THE COMMITTEE. HOWEVER, THE INFORMATON SET OUT BELOW IS NOT CONFIDENTIAL.

34/14 STANDARD LIFE GFS FUND (GLOBAL FOCUSED STRATEGIES) [Item 19]

Declarations of Interest:
None.

Key Points Raised During the Discussion:

1. The Strategic Manager – Pension Fund & Treasury introduced the report. The committee asked a number of questions which were answered by the officers and advisors present, before moving onto the recommendation.

Actions/Further Information to be Provided:
None.

Resolved:
That an additional £60m be invested into the Standard Life diversified growth funds; with a 70:30 ratio between GARS and GFS. The additional funding to be transferred from passive equities with Legal & General.

Next steps:
None.

The Board then returned to Item 6: Manager Issues and Investment Performance to give consideration to making a USD 20m commitment to the Standard Life Secondary Opportunities Fund II (SOF II).

Key Points Raised During the Discussion:

1. Concern was expressed about increasing the Fund's exposure to Standard Life.

2

2. Concern was expressed about the opportunity being a Fund of Funds. However, it was also pointed out that this meant the investment wasn't directly in Standard Life.
3. Members queried what other opportunities exist in the private equity field. The Strategic Manager – Pension Fund & Treasury pointed out that the benefit of this opportunity was that it was a Secondary Opportunities fund. The Mercer representative also reiterated his support for Secondary Opportunities. The Surrey Pension Fund Advisor also felt that this was a good opportunity to be invested in.
4. The Chairman pointed out that this was not a material amount of money.

Actions/Further Information to be Provided:
None.

Resolved:
That the Board approves making a USD 20m commitment to the Secondary Opportunities Fund II (SOF II).

Next steps:
None.

35/14 PUBLICITY FOR PART TWO ITEMS [Item 20]

RESOLVED: That the item considered under Part Two of the agenda should remain confidential and not be made available to the press and public.

36/14 DATE OF NEXT MEETING [Item 21]

The date of the next meeting was noted.

Meeting ended at: 3.50 pm

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Chairman

Surrey Pension Fund
Governance Assessment 2013/14

Taken as a group, the Board has the right background, experience, collective knowledge and
The Board has the right number of people to allow for effective and timely decision-making
The mix of the Board membership is appropriate
The roles, terms of reference and responsibilities of the Board are appropriate and well unders
The Board's approach to developing and maintaining its level of knowledge and understanding
Meetings allow sufficient focus on the "big picture" strategic issues (such as funding and inves
Board members are open, honest and effective in their communication with each other
All Board members have appropriate opportunities to contribute in meetings
The Board has the right level of access to the Pension Fund officers
The members of the Board have access to people with up-to-date investment knowledge, and
The Board receives adequate support from the officers and external advisors
The Chairman of the Board provides appropriate leadership and conducts meetings in a way v
The Chairman effectively drives accountability and measurement into the Board.
The Board meetings are well organised, efficient and effective
The frequency of Board meetings is appropriate
The Board meetings are well attended
The Board meetings are of appropriate length to allow discussion of relevant issues consisten
The Board's governance framework is appropriate and well documented
The Board spends adequate time on key strategic investment issues
The Board has sufficient time and resource to monitor the effectiveness of the Board's investr
Meetings are conducted in a way which encourages wide debate of the issues and timely deci
The Board considers compliance with the Myners/CIPFA principles on investment
The Board adequately monitors the performance of the Fund's administration function
The Board ensures that the Fund's risk assessments are adequate and reviews these regular
The Board has a clear view on the Fund's long-term funding objective
Meeting packs are complete, are received with enough lead time, and include the right informa
Minutes of Board meetings reflect activities, actions and recommendations discussed at meet
The Board reviews the statement of investment principles (SIP) on a regular basis

Page 17

2

	Member 1
skills to appropriately carry out the Board's responsibilities	2
	2
	2
stood	3
g is appropriate	2
stment strategy)	2
	1
	1
	1
l these skills, qualities and expertise are put to good use	2
	1
which encourages wide debate of the issues	2
	2
	2
	1
	2
t with the Board's responsibilities	1
	2
	2
nent manager arrangements and has appropriate review mechanisms in place	1
sion making	1
	2
	2
ly	2
	2
ation to allow meaningful discussion	2
ings	1
	2

Page 18

Member 2	Member 3	Member 4	Member 5	Member 6	Member 7	Member 8	Member 9
2	2	1	2	2	2	2	2
2	1	1	1	1	3	2	2
4	2	1	2	1	2	2	2
2	1	2	1	1	3	1	2
2	2	2	1	1	2	1	2
2	3	2	1	1	3	3	3
2	1	2	2	1	3	2	1
1	1	2	1	1	3	1	2
1	1	2	1	1	4	1	3
2	2	1	3	1	4	1	2
1	2	2	1	1	3	2	2
1	1	1	1	1	2	1	2
1	1	2	2	1	2	1	2
1	1	3	1	1	2	2	2
1	2	2	3	1	2	2	4
2	2	2	1	1	2	2	2
1	1	2	2	2	2	2	3
1	1	2	1	1	2	1	2
2	3	2	2	1	3	3	2
2	3	1	2	1	2	3	3
1	2	2	1	1	3	1	2
1	1	2	2	1	2	2	2
2	2	2	3	1	2	2	3
2	2	2	1	1	2	1	3
2	1	1	1	2	2	2	2
2	1	2	1	1	2	1	2
2	1	2	2	1	2	1	2
2	1	2	1	1	2	1	1

Page 19

2

Member 10	Average	Range
2	1.9	1 to 2
2	1.7	1 to 3
2	2	1 to 4
3	1.9	1 to 3
2	1.7	1 to 2
2	2.2	1 to 3
2	1.7	1 to 3
2	1.5	1 to 3
2	1.7	1 to 4
2	2	1 to 4
2	1.7	1 to 3
2	1.4	1 to 2
2	1.6	1 to 2
2	1.7	1 to 3
2	2	1 to 4
2	1.8	1 to 2
2	1.8	1 to 3
3	1.6	1 to 3
2	2.2	1 to 3
3	2.1	1 to 3
2	1.6	1 to 3
2	1.7	1 to 2
3	2.2	1 to 3
2	1.8	1 to 3
3	1.8	1 to 3
2	1.6	1 to 2
2	1.6	1 to 2
2	1.5	1 to 2

Page 20

Surrey Pension Fund

Governance Assessment Comments 2013/14

Member 1

It may be because I am relatively new to the Committee, but I do not call having seen any completed internal audit reports being placed on the agendas. Internal audit reports should provide a useful source of assurance to Committee members that control procedures and processes continue to operate effectively.

While training takes place regularly both at the Board meetings and at outside events, I wonder whether it might be worthwhile conducting a training needs analysis for members to identify individual knowledge gaps and skills so that training can be better targeted.

Member 2

Please stick with the agreed dates for meetings.

Given the transfer of risks to scheme members in the future, there should be more employee representation.

Pleased to see the increase in information on voting at AGMs.

I don't feel very informed about performance on private equity.

More training required on the alternative instruments that are being proposed. I feel very nervous about them.

Member 3

We need more time to challenge managers on future performance rather than historic. We need as a Board more discussion on our collective views on the future of markets, inflation, etc.

Member 4

No comments.

Member 5

Attendance is generally very good but early departures or missing the training sessions could be improved upon.

Perhaps an annual informal meeting with minimal agenda to look at pensions in the round could be useful.

Additional training suggestions: pensions law, changes to the LGPS

Page 21

2

Member 6

Excellent organisation makes the meetings well structured and this means quality decisions are made.

Again the structure and communications mean members are able to review and agree governance and any changes required.

Member training is available to all and is there to suit the requirements of individuals.

Member 7

With a challenging governance and investment agenda, sometimes there is the need for clarifying issues (away from committee) for individual members. Not clear whether this is possible with outside advisors.

The structure and leadership of the Board and its support officers and advisors is generally very good.

With a large Board, discussion is sometime restricted for individual members. Overall, there is confidence in the strategic direction being taken.

Member 8

Probably more informal round table discussions and various options for investment required. Also required, general discussions on financial threats and risk exposure.

I find it most helpful where fund managers organise seminars where board members can test their knowledge.

The Board must be alert to changes as opportunities arise. The pension fund is not fully funded, costs are high and leavers will make the fund more mature.

Board members could have individual responsibility for specific items and be tasked in specialist areas. Continuous learning is key.

Member 9

I think we need one or two more meetings per year for additional training.

Better asset/liability matching is required in the medium term.

Member 10

As a new member, I am still understanding the processes but my induction has been good and I have been encouraged to attend the organised training courses.

Page 22

KPI - DETAILED ACTIONS, TIMESCALE AND REPORTING REQUIREMENTS: To 31 March 2014 Annex 1

No	Description	Target	Lead Officer	Actual (Score and RAG)	Reporting Period	Previous Score	Date Last Reported	Improvement/Deterioration
1	**FUNDING**							
	IMPROVE FUNDING LEVEL Funding level to increase from current levels of 72%	**100%**	PT	**72.3%**	31/03/13	**72.0%**	31/12/10	0.30%
2	**PENSION ADMINISTRATION**							
	DEATH BENEFITS Notify potential beneficiary of lump sum death grant within 5 days	**95%**	PB	**100.00%**	3 months to 31 Mar 14	**100.00%**	3 months to 31 Dec 13	0.00%
	Write to dependant and provide relevant claim form within 5 days of notification of death	**90%**		**94.55%**	3 months to 31 Mar 14	**99.16%**	3 months to 31 Dec 13	-4.61%
	Pay death grant within 5 days of receipt of relevant documentation	**90%**		**100.00%**	3 months to 31 Mar 14	**97.22%**	3 months to 31 Dec 13	2.78%
	Issue notification of dependant's pension within 5 days of receipt of relevant claim forms	**90%**		**100.00%**	3 months to 31 Mar 14	**97.22%**	3 months to 31 Dec 13	2.78%
	RETIREMENTS Retirement options to members within 10 days	**90%**	PB	**95.93%**	3 months to 31 Mar 14	**95.76%**	3 months to 31 Dec 13	0.17%
	New retirement benefits processed for payment following receipt of election within 10 days	**95%**		**97.67%**	3 months to 31 Mar 14	**99.22%**	3 months to 31 Dec 13	-1.55%
	BENEFIT STATEMENTS ABS issued to 95% of eligible active members by 30th September	**95%**	PB	**100.00%**	3 months to 31 Mar 14	**100.00%**	3 months to 31 Dec 13	
	DBS issued to 85% of eligible deferred members by 30th June	**95%**		**100% issued by 26/09/13**	3 months to 31 Mar 14	**100% issued by 26/09/13**	3 months to 31 Dec 13	
	NEW JOINERS New starters processed within 20 days	**90%**	PB	**98.36%**	3 months to 31 Mar 14	**98.02%**	3 months to 31 Dec 13	0.34%
	TRANSFERS IN Non LGPS transfers-in quotations processed within 20 days	**90%**	PB	**98.77%**	3 months to 31 Mar 14	**100.00%**	3 months to 31 Dec 13	-1.23%
	Non LGPS transfers-in payments processed within 20 days	**90%**		**98.77%**	3 months to 31 Mar 14	**100.00%**	3 months to 31 Dec 13	-1.23%
	TRANSFERS OUT Non LGPS transfers-out quotations processed within 20 days	**90%**	PB	**100.00%**	3 months to 31 Mar 14	**100.00%**	3 months to 31 Dec 13	0.00%
	Non LGPS transfers out payments processed within 20 days	**90%**		**100.00%**	3 months to 31 Mar 14	**100.00%**	3 months to 31 Dec 13	0.00%
	MATERIAL POSTED ON WEBSITE Relevant Communications Material will be posted onto website within one week of being signed off	**95%**	PB	**100%**	3 months to 31 Mar 14	**100%**	3 months to 31 Dec 13	
3	**CUSTOMER SERVICE**							
	EMPLOYER SATISFACTION/SURVEY Overall satisfaction score for employers to be 80%	**80%**	PT/PB	**92%**	At Feb 14	**n/a**	n/a	
	MEMBER SATISFACTION/SURVEY Overall satisfaction score for members to be 80%	**80%**	PB	**95%**	3 months to 31 Mar 14	**92%**	3 months to 31 Dec 13	
4	**INVESTMENT PERFORMANCE**							
	INVESTMENT RETURNS/OVERALL FUND PERFORMANCE Returns to at least match the benchmark	**Benchmark**	PT	**BENCHMARK 7.1%**	12 months to 31 Mar 14	**BENCHMARK 12.5%**	12 months to 31 Dec 13	
				ACTUAL 8.6%	12 months to 31 Mar 14	**ACTUAL 15.7%**	12 months to 31 Dec 13	
5	**DATA**							
	DATA QUALITY Data quality within the Fund should be at least 90% accurate.	**90%**	PB	**99%**	12 months to 31 Mar 14	**99%**	12 months to 31 Mar 13	
6	**CONTRIBUTIONS**							
	CONTRIBUTIONS RECEIVED **Pension Fund** 98% (total value) of contributions to be received by 21st day of the ensuing period.	**98%**	PT	**98%**	Mar-14	**98%**	Dec-13	0.00%
7	**AUDIT**							
	CLEAN AUDIT REPORT Receive an unqualified audit opinion from the external auditors	**Clean Report**	PT/PB	**Achieved**	12 months to 31 Mar 13	**Achieved**	12 months to 31 Mar 12	
	Annual audit returns no significant findings	**No significant findings**		**Achieved**		**Achieved**		
8	**COST**							
	COST PER MEMBER Administration cost per member to remain in lowest CIPFA benchmarking quartile	**< lowest quartile**	PT/PB	**Achieved**	12 months to 31 Mar 13	**Achieved**	12 months to 31 Mar 12	

Page 23

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Page 24

HYMANS ROBERTSON

Consultation on LGPS investment structure

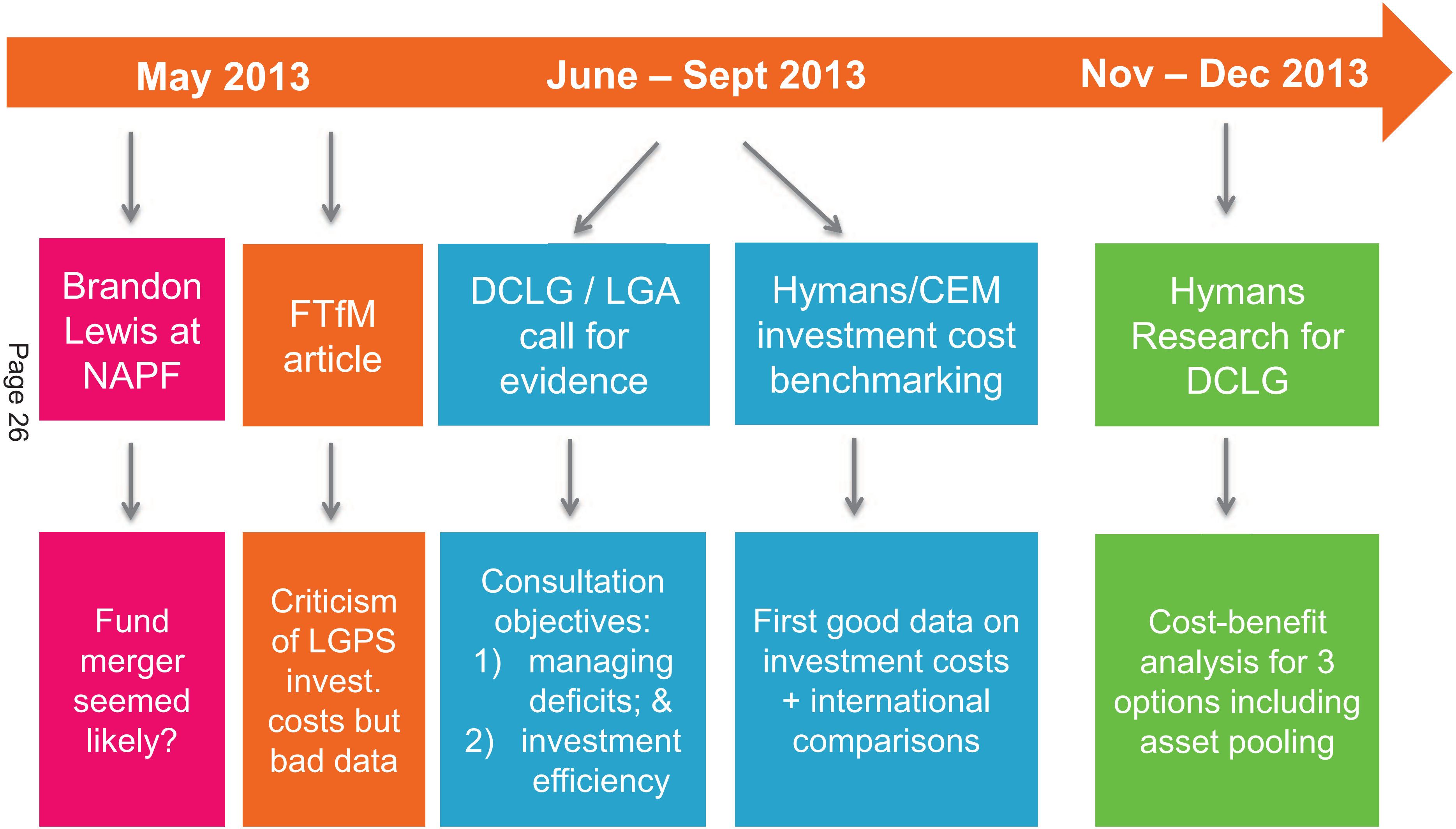
Briefing for Surrey Pension Fund Board

- John Wright
- Matt Woodman
- 15 May 2014

Page 25

Story so far

HYMANS ROBERTSON



Page 26

Story so far

HYMANS ROBERTSON

Jan 2014

SAB analysis of CfE responses & letter to minister

Themes:
-use of asset pooling?
-use of passive?
-use of in-house?
Consider options for managing deficits

Feb 2014

London Councils give London CIV green light

Collective Investment Vehicle for London Boroughs. Voluntary participation

May/July 2014

Next DCLG consultation

Merger ruled out Instead consulting on asset pooling and greater use of passive

Page 27

HYMANS ROBERTSON

Research for DCLG* (December 2013)

Question in brief	Finding
LGPS Investment costs	c£790m per annum
LGPS vs international peers	LGPS lower on some asset classes
Areas for savings	Implementation style (FoFs, passive)
Est savings from no longer using FoF on alternatives	£240m per annum after 10 years (13bps of assets, 136 bps of listed)
Savings if all listed investments passive	£230m per annum (12bps of assets, 15bps of listed)
Transition cost	£215m (£47m stamp duty)
Impact on aggregate LGPS performance for listed	Over last 10 years no impact on performance
Merger vs asset pooling	Merger delays emergence of savings and lost local decision making

"LGPS Structure Analysis", Hymans Robertson, December 2013

Page 28

New government consultation (May 2014)

- Merger no longer government’s preferred option
- Instead consulting on:
  - use of asset pooling (collective investment vehicles) for investment scale benefits
  - CIVs for alternatives and listed investments
  - greater use of passive for listed
  - governance aspects
- Consultation closes 11 July 2014

Page 29

HYMANS ROBERTSON

Consultation Qs

- Q1. Do you agree that CIVs would allow funds to achieve economies of scale and deliver savings for listed and alternative investments? Explain and evidence your view.
- Q2. Do you agree with proposal to keep decisions about asset allocation with local fund authorities?
- Q3. How many CIVs should be established and which asset classes should be separately represented in each of the listed and alternative asset CIVs?

Page 30

Consultation Qs

HYMANS ROBERTSON

- Q4. What type of CIV do you believe would offer the most beneficial structure? What governance arrangements should be established?
- Q5. In light of evidence on relative costs and benefits of active vs passive investment and aggregate LGPS performance data, which option for passive investment offers best value for tax-payers:
  - 1) Compulsion (all listed securities to be passive)
  - 2) Specified % age passive or progressive increase
  - 3) "comply or explain"
  - 4) Funds simply be expected to consider the benefits

Page 31

HYMANS ROBERTSON

Next

- Consultation closes 11 July 2014
- Date for government decision and action unknown
- Other related developments:
  - London CIV progressing – live 2015?
  - Closer look at ways of managing deficits (SAB)
  - Changes to investment regulations
  - Changes to local governance arrangements

Initial thoughts on consultation questions?

Page 32

APPENDICES

Page 33

HYMANS ROBERTSON

Research commissioned by Ministers - scope

- Quantify **investment costs** including turnover costs
- Identify potential **cost savings**
- Costs and benefits of active and passive strategies
- Since cannot look at costs in isolation, assess net of fees **performance** against market indices for LGPS in **aggregate**
- Estimate **cost of change** to new operational structures that might be used to deliver cost savings (collective investment vehicles or merged funds)
- Practical and legal impediments to implementation and the realisation of benefits

Research to inform next phase of consultation

Page 34

HYMANS ROBERTSON

Out of scope

- A recommendation on which option should be taken forward
- Dealing with deficits
- Member administration
- Quantification of any governance dividend
- Focus on “hard” costs, not “soft” outcomes

We were not asked to make any recommendation e.g. on the amount that should be invested passively or the most appropriate way forward

Page 35

HYMANS ROBERTSON

Total fees by asset class and active/passive

Asset class	% of total assets	Active fees (£000)	Passive fees (£000)	Total (£000)	% of total fees
Equities	65.8	256,963	31,103	288,068	**38.5**
Bonds and cash	17.6	54,535	7,141	61,674	**8.2**
Property	6.8	97,996	0	97,996	**13.1**
Alternatives	9.8	300,883	268	301,151	**40.2**
Total	**100.0**	**710,377**	**38,512**	**748,890**	**100.0**

Source: CEM Benchmarking Inc., data provided by 18 LGPS funds

Fees analysed by asset class and style of investment

Page 36

LGPS aggregate performance

10 years to 31 March 2013: Index and weighted ave. returns (% p.a.) gross of fees

Equity market	UK	North America	Europe ex UK	Japan	Developed Pacific ex Japan	Emerging Markets
FTSE Index	10.7	9.5	11.4	7.4	16.4	18.2
Aggregate LGPS	10.8	8.4	11.6	7.5	17.3	17.1
Excess active return	0.1	-1.1	0.2	0.1	0.9	-1.1
Extra cost p.a. of active	0.34*	0.27	0.20	n/a	0.49	0.53

Sources: State Street Investment Analytics (The WM Company), CEM Benchmarking Inc.

* This is our estimate of the extra cost which reflects the low fees that the LGPS in aggregate pay for active management of UK equities. The global cost premium is estimated by CEM as 0.56%

Page 37

HYMANS ROBERTSON

When to use active management?

Costs could be reduced by increasing the extent of passive management. This does not mean that we advocate 100% passive for all LGPS funds. The balance between active and passive should depend on:

- your governance budget
- your investment beliefs
- your investment objectives, e.g. any specific requirements you have for income or low absolute volatility
- the expected net of fee returns

Page 38

Reliances and limitations

- Data in our report: “LGPS Structure Analysis”, December 2013
- The information in our report is based upon our understanding of legislation and events as at 12 December 2013 and we have used all reasonable endeavours to ensure the accuracy or completeness of the information used in the report.
- We have relied on data and legal advice provided by our partner organisations in compiling the report, CEM and Squire Sanders, both under sub-contracting arrangements. Whilst reasonable efforts have been made to ensure the accuracy of the data and advice expressed, we cannot verify the accuracy of such advice and data and we cannot be held liable for any loss arising from use and/or reliance on such advice and data.
- It should be noted that we do not provide legal services and therefore, we accept no liability to any third parties in respect of the legal opinions expressed in our report. Third parties are advised to take independent legal advice in respect of any legal matters arising out of our report.

Page 39

HYMANS ROBERTSON

Thank you

Any questions?

Page 40

SURREY
COUNTY COUNCIL

5

Surrey Pension Fund Board
19 September 2014

ACTION TRACKER

PURPOSE OF REPORT:

For Members to consider and comment on the Board's action tracker.

INTRODUCTION:

An action tracker recording actions and recommendations from previous meetings is attached as **Annex A**, and the Board is asked to review progress on the items listed.

RECOMMENDATION:

The Committee is asked to monitor progress on the implementation of recommendations from previous meetings (Annex A).

REPORT CONTACT: Cheryl Hardman, Regulatory Committee Manager
020 8541 9075
cherylh@surreycc.gov.uk

Sources/background papers: None

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Surrey Pension Fund Board – ACTION TRACKING

ACTIONS

Number	Meeting Date	Item	Recommendation / Action	Action by whom	Action update
A10/14	15 May 14	Private Equity Investment Performance Review	Future reports on private equity performance to present a cash flow analysis of how payments are received over time.	Strategic Manager, Pension Fund & Treasury	To review at the meeting on 19 September 2014.
A12/14	15 May 14	Pension Fund Business Plan 2013/14: Outturn Report and Final 2014/15 Plan	A training needs analysis to be conducted later in the year.	Strategic Manager, Pension Fund & Treasury	A training needs analysis was circulated by email on 14 August 2014.
A16/14	15 May 14	Revised Statement of Investment Principles	The Statement of Investment Principles to be amended as agreed at the meeting.	Strategic Manager, Pension Fund & Treasury	To be addressed at the meeting of the Board on 19 September 2014.
A18/14	15 May 14	Pension Fund Administration Service Level Agreement	The Service Level Agreement to be published on the Pension Fund website.	Pensions Manager	Officers to update the Board on 19 September 2014.
A21/14	15 May 14	Investment Strategy Review	The Board to receive training on synthetic equities.	Strategic Manager, Pension Fund & Treasury	To be scheduled.

Surrey Pension Fund Board – ACTION TRACKING

COMPLETED ACTIONS

Number	Meeting Date	Item	Recommendation / Action	Action by whom	Action update
A5/14	14 Feb 14	Manager Issues and Investment Performance	The Strategic Manager – Pension Fund & Treasury agreed to check how much Surrey County Council charges for loans and report back to the Board.	Strategic Manager, Pension Fund & Treasury	The Strategic Manager – Pension Fund & Treasury reported back on 15 May 2014.
A9/14	15 May 14	Manager Issues and Investment Performance	Board to review whether to invite Newton to a future meeting after a further quarter's performance results are published.	Board	The Board is to interview Newton at an informal meeting on 17 September 2014.
A11/14	15 May 14	Pension Fund Business Plan 2013/14: Outturn Report and Final 2014/15 Plan	A report to be brought to the next meeting of the Surrey Pension Fund Board on how to address the results of the Governance Self-Assessment.	Strategic Manager, Pension Fund & Treasury	This is included within the Manager Issues and Investment Performance brought to the Board at the 19 September 2014 meeting.
A13/14	15 May 14	Pension Fund Risk Register	Risks to be reviewed to make the register more concise.	Strategic Manager, Pension Fund & Treasury	The risk register has been reviewed and is presented to the Board at its 19 September 2014 meeting.
A14/14	15 May 14	Pension Fund Risk Register	Risk 36 to be dropped from the register.	Strategic Manager, Pension Fund & Treasury	This has been removed.
A15/14	15 May 14	Pension Fund Risk Register	A risk to address the implementation of the proposed changes to the LGPS to be added.	Strategic Manager, Pension Fund & Treasury	This has been added to the Risk Register.

Surrey Pension Fund Board – ACTION TRACKING

A17/14	15 May 14	Key Performance Indicators	To include the estimated deficit of the Fund in future KPI Statements, while making it clear that it is estimated value and not an actuarial valuation.	Strategic Manager, Pension Fund & Treasury	See Key Performance Indicators report on the Board's agenda for 19 September 2014.
A19/14	15 May 14	National Changes to the LGPS	Strategic Manager – Pension Fund & Treasury to report back on the outcomes of the officer meeting on 28 May 2014 before the next meeting of the Surrey Pension Fund Board.	Strategic Manager, Pension Fund & Treasury	The outcomes of the meeting were communicated through the Manager Issues and Performance Report for the 19 September 2014 meeting, published on 8 September 2014.
A20/14	15 May 14	Investment Strategy Review	Three fund managers to be invited to an informal meeting of the Board to help it to understand the approach being recommended. A fee exercise also to be conducted.	Strategic Manager, Pension Fund & Treasury	The Board will meet three fund managers on 12 September 2014.

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SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

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SUBJECT: **MANAGER ISSUES AND INVESTMENT PERFORMANCE**

SUMMARY OF ISSUE:

This report is a summary of all manager issues that need to be brought to the attention of the Pension Fund Board, as well as manager investment performance.

RECOMMENDATIONS:

It is recommended that the Pension Fund Board:

1. approve the report and the decisions as laid out.
2. give consideration to making a £7m commitment each year for 2014/15, 2015/16 and 2016/17 to the Capital Dynamics LGPS Collective Private Equity Vehicle.
3. give consideration to making a USD 20m commitment to the Goldman Sachs Private Equity Managers (PEM) Fund.

REASON FOR RECOMMENDATIONS:

In order to achieve best possible performance alongside optimal risk.

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DETAILS:

1) Manager Issues during the Quarter

Manager	Issue	Status/Action Required
L&G	Possible Rebalancing	The asset allocation is within the Fund's policy control limits. The asset allocations at 30 June 2014 and 27 August 2014 are shown in Annex 1.
Standard Life	Global Focused Strategies	Members agreed to allocate £60m to Standard Life's Global Focused Strategies Fund at the Board meeting on 15 May 2014. This was achieved on 12 June 2014 with a transfer from equities run by Legal and General Investment Management to the Standard Life GFS Fund. An adjustment has been made to the Statement of Investment Principles (SIP) as a result.
Mirabaud	Client meeting	Update included in minutes of external fund manager meetings held on 17 September 2014.
Newton	Client meeting	Update included in minutes of external fund manager meetings held on 17 September 2014.
Western	Client meeting	Update included in minutes of external fund manager meetings held on 17 September 2014.
CBRE	Client meeting	Update included in minutes of external fund manager meetings held on 17 September 2014.
Capital Dynamics	Private Equity opportunity	Members are invited to consider the Capital Dynamics LGPS Collective Private Equity Vehicle opportunity set out in (9) below.
Goldman Sachs	Private Equity opportunity	Members are invited to consider the Goldman Sachs Private Equity Managers (PEM) Fund opportunity set out in (9) below.

2) Freedom of Information Requests

The table below summarises the Freedom of Information request responses provided by the Fund during the last quarter.

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Date	Requestor	Organisation	Request	Response
10/04/2014	Private Individual	n/a	Information relating to tobacco investment held by the Fund.	A spreadsheet containing the market value of directly held tobacco company assets over the previous 4 years, including both fixed income and equity investments
20/06/2014	Company	Pitchbook	Information pertaining to private equity investments made by the Fund	A spreadsheet with a breakdown of private equity investments held by the Fund.

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3) **Future Pension Fund Board Meetings/Pension Fund AGM**

The schedule of meetings for 2014 is as follows:

- 19 Sep 2014: Board meeting hosted at County Hall.
- 14 Nov 2014: Board meeting hosted at County Hall.
- 21 Nov 2014: Pension Fund Annual Meeting hosted at County Hall.

4) **Stock Lending**

In the quarter to 30 June 2014, stock lending earned a net income for the Fund of £105,519, with an average value on loan equal to £120.6m

5) **Share Voting**

The Strategic Manager will present a report at the Board meeting.

6) **Ill Health Insurance**

At the Board meeting on 14 February 2014, it was agreed that an ill health insurance policy with Legal & General would be taken out in order to insure the fund and scheme employers against the cost of ill health retirement benefits. This agreement was subject to receiving confirmation from the County's Head of Procurement that it was not necessary to formally tender for an insurance provider as it was understood that Legal & General was the only provider of this type of insurance product.

Discussions with procurement and legal colleagues are ongoing with a view to securing a way forward that does not breach EU procurement regulations. Preliminary advice received is that the administering authority could publish a VEAT (voluntary ex ante transparency) notice for ten days, advising that it is the intention for the administering authority to enter into a contract with Legal & General. This notice was published on 3 September 2014. If there is a credible alternative provider, there would be 30 days in which to challenge the intention to contract with Legal & General without first tendering.

7) **Private Equity**

A review of the private equity portfolio was presented to the Board at the meeting of 15 May 2014. Latest information was taken from the global custodian position reports and, where possible, information provided from the private equity managers themselves. Officers have since taken the opportunity to review the data and update where necessary. A revised valuation as at 31 March 2014 is shown at Annex 2.

8) **Internally Managed Cash**

The internally managed cash balance of the Pension Fund was £0.8m as at 30 June 2014.

9) Private Equity Opportunities

Capital Dynamics LGPS Collective Private Equity Vehicle 2014/2015

Capital Dynamics, one of the Fund's existing private equity managers, has developed its first Collective Private Equity Vehicle specifically designed for LGPS funds (LGPS CPEV) in response to the ongoing campaign to reduce management fees via collaboration. The sterling denominated pooled vehicle provides a means for LGPS funds to gain access to an optimally balanced portfolio of private equity strategies. 7

The global portfolio includes primary (65% minimum), secondary (up to 30%) and co-investment (5%) strategies. The primary investments are weighted 40% US, 40% Europe and 20% Asia/Emerging Markets. The secondary and co-investment proportion of the portfolio will be geographically opportunistic, but will have global diversification. The portfolio has been designed to minimise risk whilst preserving attractive target returns of between 12% and 15% net/net IRR (1.5x to 1.8x multiple of cost).

The fund raising period for each closed end Fund will span the fiscal year, i.e. from 1 April to 31 March. The investment period will be two years from the first close of each Fund. The reduced fund raising and investment periods, plus the secondary element of the fund will ensure that cash is returned to investors more efficiently, significantly mitigating the J-Curve effect.

The fee is 10bps for 80% of the Vehicle, i.e. 8bps per annum. 20% of the Vehicle will be invested directly into Capital Dynamics' secondary and co-investment funds with no additional layer of fees. Moreover, LGPS investors who commit to three annual programmes in advance will qualify for a management fee reduction of 50%, i.e., 4bps per annum. The performance fee of 7.5%, is payable after all capital invested has been returned to investors in cash plus a compounded 8% hurdle.

Surrey has previously invested in Capital Dynamics US Solar Fund and Capital Dynamics Clean Energy and Infrastructure Fund.

It is recommended that the Surrey Pension Fund give consideration to making a total £21m commitment to the Capital Dynamics LGPS Collective Private Equity Vehicle, optimising the fee discount offered over three annual programmes by investing £7m per vehicle.

Goldman Sachs Private Equity Managers (PEM) Fund

The Goldman Sachs Private Equity Mangers (GSAM) "PEM" 2014 is the fourth in a series of annual funds called the PEM Program that is managed by Goldman Sachs Asset Management's AIMS private equity team. This is the same team that manages Surrey Pension Fund's existing commitments to GSAM's Private Equity Partners ("PEP") and Vintage Funds.

The PEM 2014's primary focus will be on constructing a portfolio of six to eight private equity commitments with diverse strategies, which may include middle-market buyout, large buyout, distressed, growth equity, credit, venture capital and industry focused strategies. On an opportunistic basis, the PEM 2014 may also acquire interests in private equity funds from investors seeking liquidity prior to the termination of those vehicles (i.e. secondary investments).

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The investment objective for PEM 2014 is to realise long-term compounded returns in excess of those available through conventional investments in the public equity markets. For commitments of USD 20m and more into PEM 2014, the average annual management fee on committed capital is 47bps (assuming a 12-year fund life), without any performance fee charged by GSAM.

Goldmans expects the PEM to outperform equity markets by three to five percent (net of all fees) over the long term.

It is recommended that the Surrey Pension Fund give consideration to making a USD 20m commitment to the Goldman Sachs Private Equity Managers Fund.

10) Governance Strategies and Policies

All outstanding papers have now been drafted and presented to the Board.

The share voting framework and share voting policy are due for revision and revised papers will be presented to the Board on 14 November 2014, following publication of the changes to the UK Corporate Governance Code due to be published at the start of October 2014.

The list of strategies, policies and reporting frameworks approved by the Board since its first meeting on 31 May 2013 are as follows:

1. Business Plan Reporting Framework
2. Communication Policy Statement
3. Funding Strategy Statement
4. Governance Compliance Statement
5. Governance Policy Statement
6. Investment Performance Reporting Framework
7. Key Performance Indicator Reporting Framework
8. Knowledge and Skills Framework
9. Pension Abatement Policy
10. Pension Fund Administration Policy
11. Pension Fund Service Level Agreement
12. Private Equity Reporting Framework
13. Responsible Investment and Stewardship Policy
14. Risk Register Reporting Framework
15. Share Voting Reporting Framework
16. Statement of Investment Principles
17. Stewardship Code
18. Stock Lending Policy

11) Results of the Governance Self-Assessment Survey

The results of the Governance Self-Assessment completed by members of the Board were tabled at the 15 May 2014 Board meeting.

There were six important issues taken from the self-assessment process. Each is laid out below with action points to be undertaken by the Strategic Finance Manager.

1) The Board does not have enough time to be truly effective and that meetings do not allow sufficient focus on the ‘big picture’ strategic issues.

Where appropriate and where there is sufficient material on the agenda, board meetings will continue for the whole day (typically 9:30am to 3:30am). Strategic issues and an hour’s member training scheduled for each meeting will take overall priority. If an agenda is considered to be too time consuming, the investment manager meetings will take place on a separate day and these manager meetings will be open to Board members to attend. Minutes from those meetings will be taken directly to the next Board meeting for consideration. Investment manager meetings (both within Board meetings and held externally) will be subject to a pre-meeting briefing in order to decide what questions should be asked of the managers. 7

2) There is value in having additional training and informal discussions between formal Board meetings in order to develop a general consensus on where the market is headed and an understanding of what other Pension Fund Boards are doing.

A full range of quality training days will be offered to Board members as and when the opportunities are communicated to the Strategic Finance Manager. Typically, such opportunities are afforded to all LGPS funds with a resultant attendance of LGPS trustees from across the UK. Discussions between fund members at those meetings as to varying strategies being considered and implemented are encouraged.

3) There is value in holding pre-meetings with advisors and consultants in order to ensure that members are supported with the right questions when meeting fund managers.

Pre-meetings will be held ahead of all future meetings where investment managers are attending for presentation.

4) There is no value to be gained from increasing the number of formal Board meetings.

The standard quarterly meeting format will remain.

5) There is no value in setting up smaller sub-committees.

There are no plans to set up sub-committees.

6) The Fund’s Administration function is not adequately monitored.

The internal audit report of the Administration function was presented to the Board on 15 May 2014. Detailed performance on administration key performance indicators (KPIs) are presented at every Board meeting.

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12) National Changes to the LGPS: Collaboration

At the last Board meeting on 15 May 2014, the Strategic Finance Manager introduced a report with regard to possible future collaboration with the South East 7 counties. An officer meeting subsequently took place on 28 May 2014 to work on proposals. The outcome of the meeting produced the following to be worked on for the next meeting.

Response to 9 July 2014 CIV/Passive Consultation: authorities to share responses in the run up to the deadline. Achieved.

Society of County Treasurers LGPS Actuarial Survey: West Sussex to ascertain progress as it will be a helpful map as to where commonality exists.

DCLG Governance Consultation: authorities to share responses. Achieved.

Pension Fund Annual Report: new CIPFA guidance recently published. Authorities to share interpretations and ideas.

Current Activity: infrastructure and leveraged gilts (Surrey), transition manager and balanced growth (WSCC).

Potential Collaboration: Foreign exchange and transactions. WSCC to lead on this.

Committee meetings: Surrey Board on 19 September 2014 (all SE7 officers invited). WSCC Governance Working Group on 16 July 2014 (Phil Triggs attended).

Contractual settlement and income collection: WSCC conducting a study.

13 Fund Manager Meetings of 17 September 2014

Notes of the fund manager meetings of 17 September 2014 will be tabled at the Board meeting on 19 September.

Report of the Strategic Finance Manager

Financial and Performance Report

7

1. Funding Level

Table 1

Past Service Position	**30 June 2014 £m**
Past Service Liabilities	3,577
Market Value of Assets*	2,853
Deficit	(724)
Funding Level	79.8%

* This is an estimate of the fund market value prior to quarter end.

The funding level at the latest formal valuation at 31 March 2013 was 72.3%. As at 30 June 2014 the funding level has increased to 79.8%, a significant improvement. This is largely as a result of strong investment manager performance and an increase in gilt yields, resulting in a higher discount rate (5.0%), which places a lower value on the Fund's liabilities.

2. Market Value

The value of the Fund was £2,833.0m at 30 June 2014 compared with £2,771.1m at 31 March 2014. Investment performance for the period was +2.2%.

The increase is attributed as follows:

	£m
Market Value at 31/03/2014	**2,771.1**
Contributions less benefits and net transfer values	2.4
Investment income received	15.4
Investment expenses paid	-2.3
Market movements	46.4
Market Value at 30/06/2014	**2,833.0**
Market Value at 27/08/2014 (estimated)	**2,856.6**

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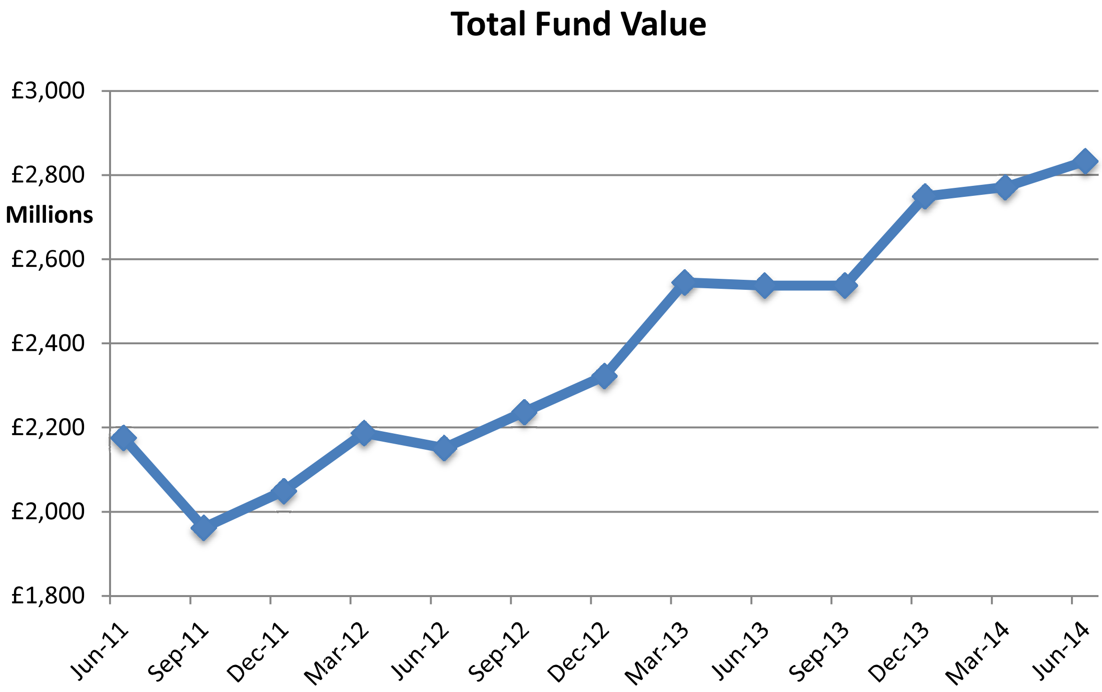
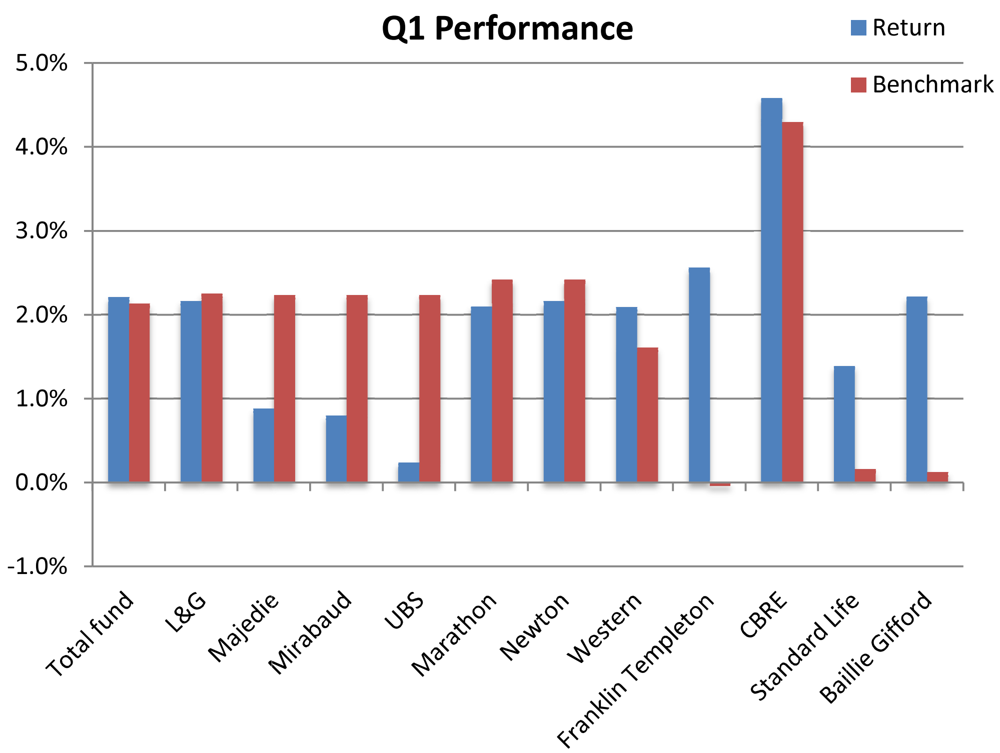


3. Fund Performance

Summary of Quarterly Results

Overall, the total fund returned +2.2% in Q1 2014/15 just above the SCC customised benchmark of 2.1%.



Both Baillie Gifford and Standard Life are absolute return funds with a benchmark based upon short term cash holdings.

Property provided the largest absolute return for the fund during the previous quarter with a performance of +4.6% with a +0.3% outperformance against the benchmark. Broadly other asset classes reported fairly even investment performance over the quarter. In relative terms, all three active UK equity managers underperformed the benchmark return of 2.2%

The table below shows manager performance for 2014/15 Q4 against manager specific benchmarks using custodian data.

7

Manager	**Performance %**	**Benchmark %**	**Relative %**
Total fund	2.2	2.1	0.1
L&G	2.2	2.3	-0.1
Majedie	0.9	2.2	-1.3
Mirabaud	0.8	2.2	-1.4
UBS	0.2	2.2	-2.0
Marathon	2.1	2.4	-0.3
Newton	2.2	2.4	-0.2
Western	2.1	1.6	0.5
Franklin Templeton	2.6	0.0	2.6
CBRE	4.6	4.3	0.3
Standard Life	1.4	0.2	1.2
Baillie Gifford	2.2	0.1	2.1

Franklin Templeton is measured against a US Dollar denominated benchmark which is then converted back to Sterling. This can cause a disparity between performance and benchmark given large currency movements.

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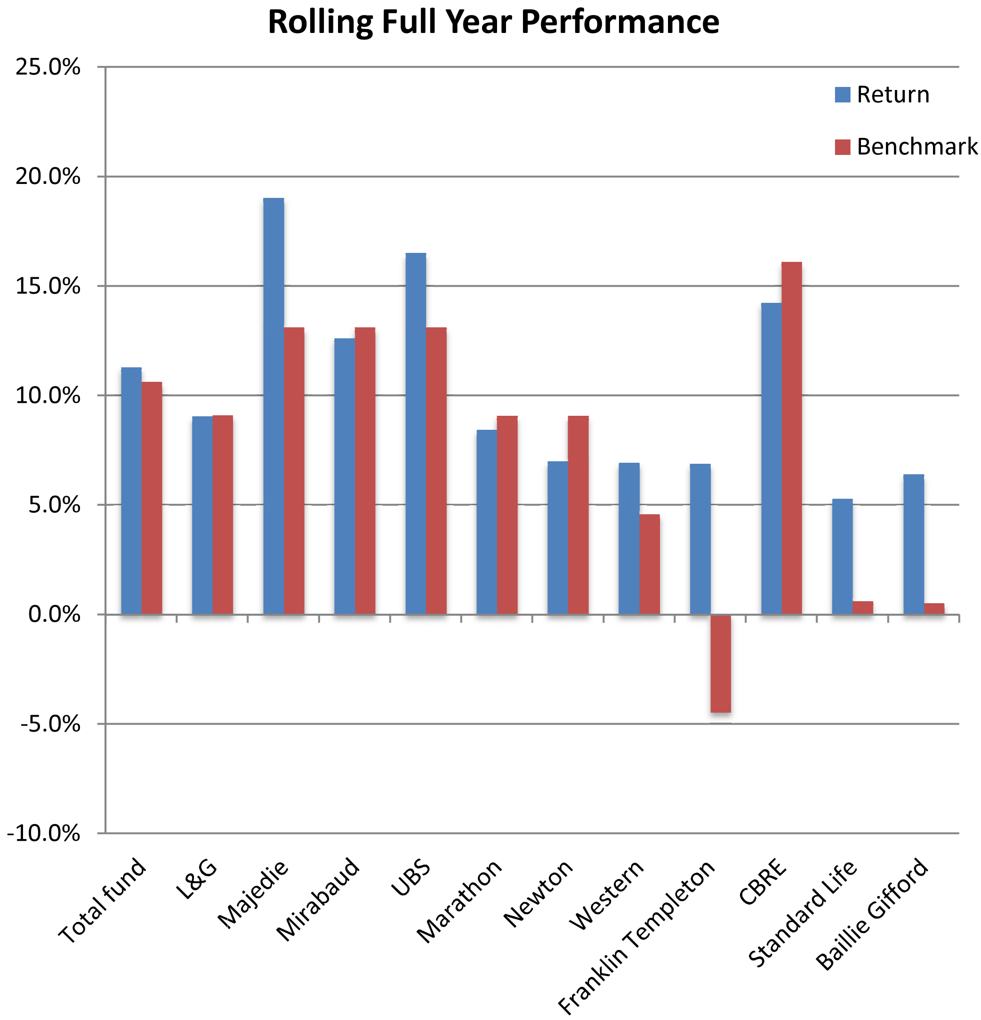
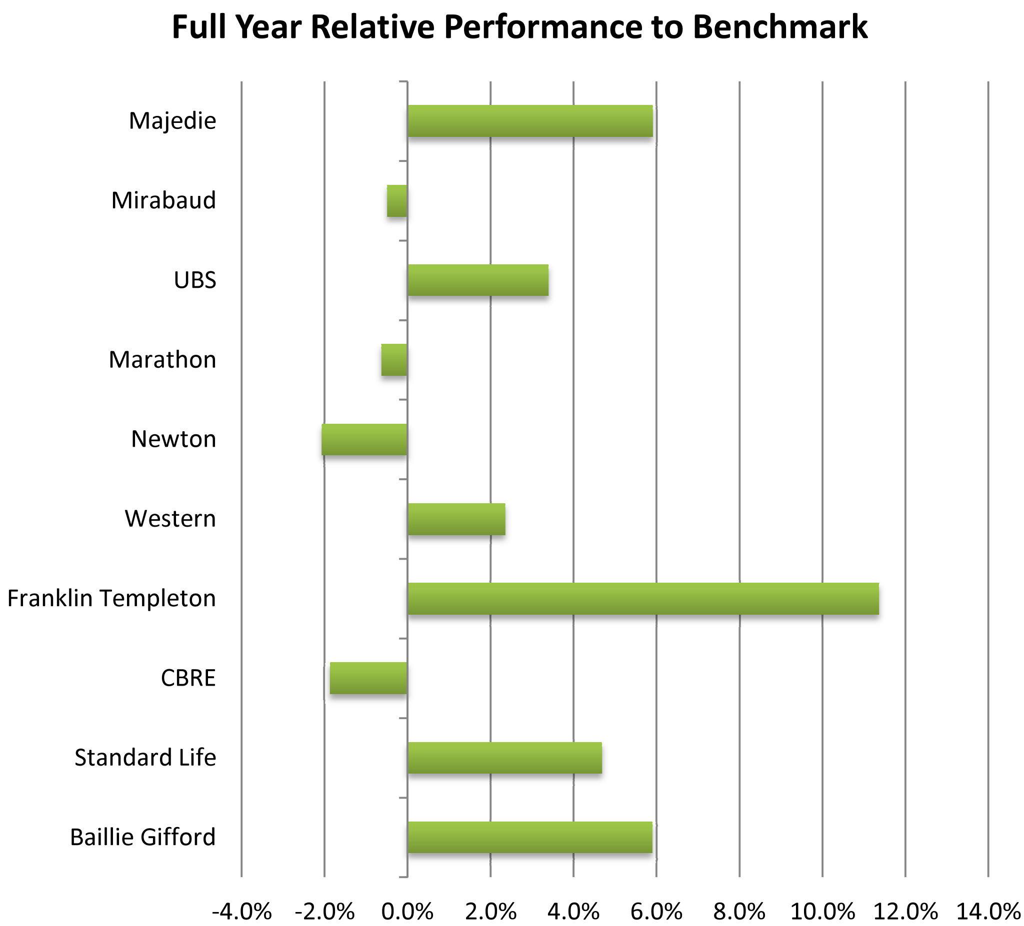
Summary of Full Year Results

During the course of the previous 12 months to 30 June 2014, the Fund returned +11.3% overall, an outperformance of 0.7% against the customised benchmark of +10.6%.



Domestic equity and property provided the largest return to the fund over the previous quarter with both asset classes securing double digit investment performance. Majedie and UBS recorded absolute returns of +19.0% and +16.5% respectively ahead of the UK equity benchmark of +13.1%.

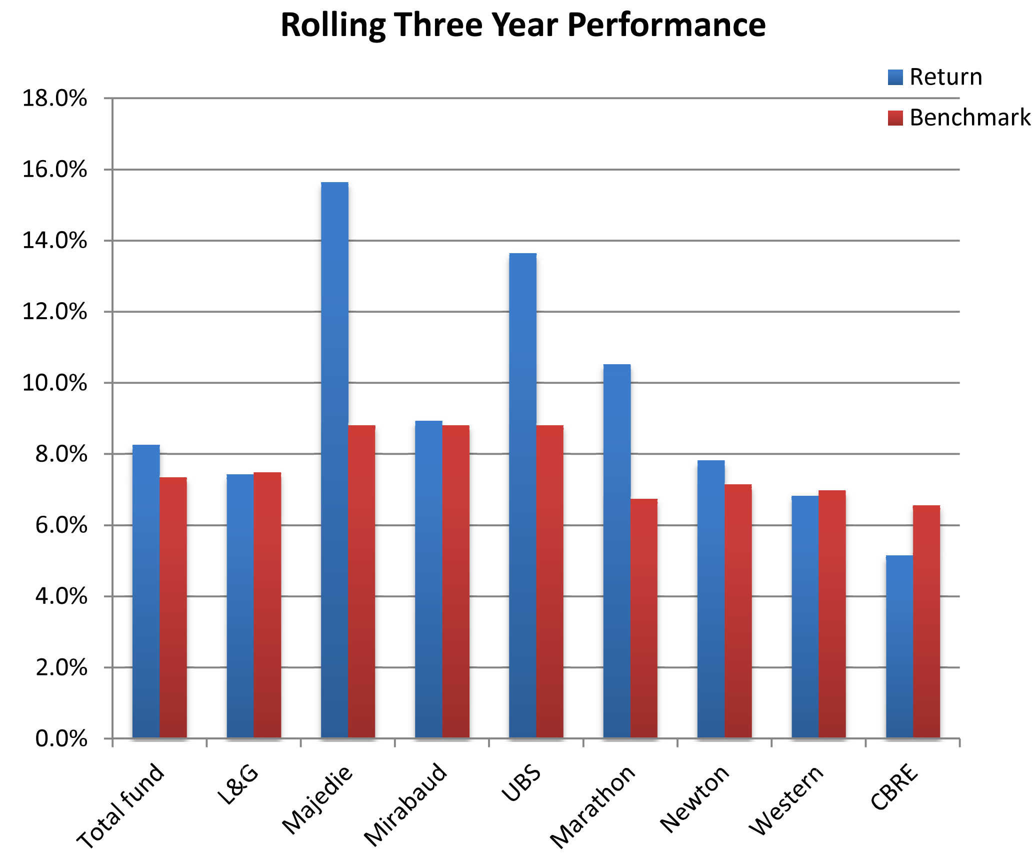
Franklin Templeton recorded a sizable +11.4% relative performance against the benchmark. The benchmark is an unhedged USD benchmark and when converted to sterling resulted in a underperformance of -4.6%. The benchmark performance in USD terms is +7.7%.



The table below shows manger performance for the year to 30 June 2014 against manager specific benchmarks using custodian data.

Manager	Performance %	Benchmark %	Relative %
Total fund	11.3	10.6	0.7
L&G	9.0	9.1	-0.1
Majedie	19.0	13.1	5.9
Mirabaud	12.6	13.1	-0.5
UBS	16.5	13.1	3.4
Marathon	8.4	9.1	-0.6
Newton	7.0	9.1	-2.1
Western	6.9	4.6	2.3
Franklin Templeton	6.9	-4.5	11.4
CBRE	14.2	16.1	-1.9
Standard Life	5.3	0.6	4.7
Baillie Gifford	6.4	0.5	5.9

Summary of Rolling Three Year Performance



The below table shows the annualised performance by manager for the previous three years

Manager	Performance %	Benchmark %	Relative %
Total fund	8.6	7.6	1.0
L&G	7.5	7.6	-0.1
Majedie	15.0	8.9	6.1
Mirabaud	8.8	8.9	-0.1
UBS	12.8	8.9	3.9
Marathon	10.6	7.3	3.3
Newton	8.5	8.0	0.5
Western	7.0	6.6	0.4
CBRE	6.0	7.4	-1.4

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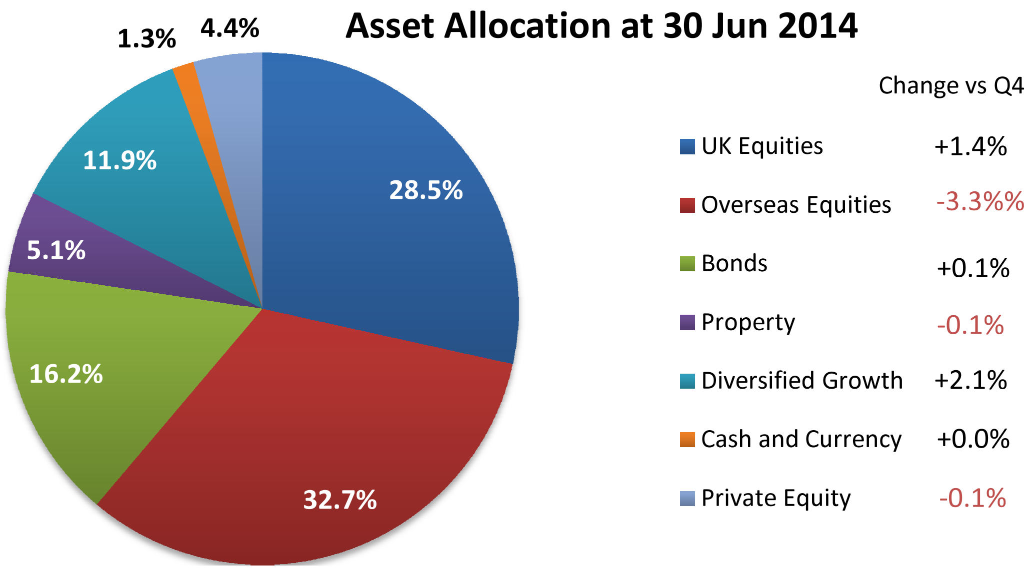
4. Asset Allocation

The graph and table below summarise the asset allocation of the managed elements of the fund, excluding private equity holdings and internally held cash balances. The sizable movement in equities and diversified growth is a result of the investment into Standard Life GFS Fund, funded by a divestment from passive equities held by L&G.



The table below compares the actual asset allocation as at 30 June 2014 against target asset weightings.

	TOTAL FUND £m	Actual %	Target %	Last Quarter £m	Last Quarter %
Fixed Interest					
UK Government	105.2	3.7	4.6	104.6	3.8
UK Non-Government	122.8	4.3	7.1	118.6	4.3
Overseas	61.9	2.2	0.0	60.2	2.2
Total Return	70.6	2.5	2.4	68.8	2.5
Index Linked	98.0	3.5	3.5	94.7	3.4
Equities					
UK	806.5	28.5	27.5	751.2	27.1
Overseas	925.9	32.7	32.3	996.0	35.9
Property Unit Trusts	145.1	5.1	6.2	145.8	5.3
Diversified growth	335.8	11.9	11.4	270.9	9.8
Cash	34.0	1.2	0.0	30.2	1.1
Currency hedge	4.7	0.2	0.0	7.7	0.3
Private Equity	122.5	4.3	5.0	122.5	4.4
TOTAL	**2,833.0**	**100.0**	**100.0**	**2,771.1**	**100.0**

5. Manager Allocation

The graph below shows the current manager allocation.

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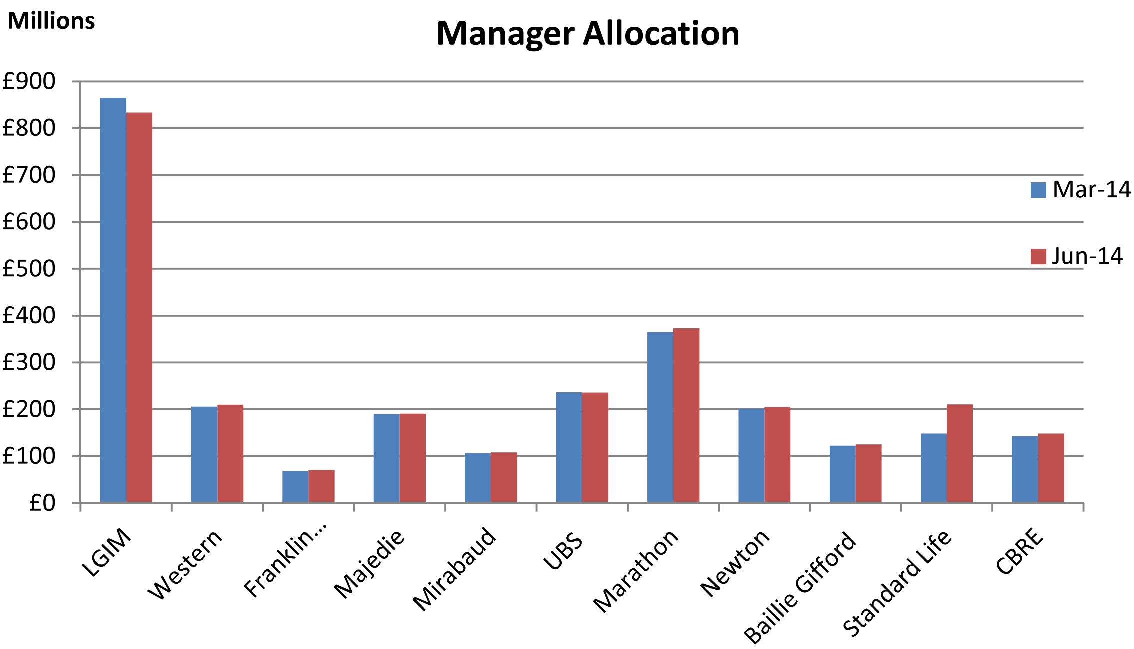

The table below includes the actual and target manager allocation weightings for those investments managed through the custodian Northern Trust as at 30 June 2014. This excludes internal cash and private equity portfolio.

Investment Manager	Asset Class	Market Value £m	Actual Allocation %	Target Allocation %
L&G	Multi-Asset	833.7	30.7	31.7
Western	Bonds	210.0	7.8	8.3
Franklin Templeton	Bonds	70.6	2.6	2.6
Majedie	UK Equity	190.9	6.9	7.0
Mirabaud	UK Equity	107.8	4.0	4.0
UBS	UK Equity	235.9	8.7	8.0
Marathon	Global Equity	372.9	13.8	12.0
Newton	Global Equity	205.3	7.6	8.0
Baillie Gifford	Diversified Growth	125.2	4.6	4.0
Standard Life	Diversified Growth	210.5	7.8	8.0
CBRE	Property	148.3	5.5	6.5
	Residual Cash	0.2	0.0	0.0
TOTAL		**2,711.3**	**100.0**	**100.0**

6. Fees

The following table shows a breakdown of fees paid during Q1 2014/15. The annualised fee for Q1 is lower than previous quarters as no performance fees were due this period.

Manager	Market Value 30/06/2014 £m	Manager Fee Paid Q4 £	Annualised Average Fee %
L&G	833.7	206,104	0.10
Western	210.0	120,918	0.23
Franklin Templeton*	70.6	122,693	0.70
Majedie	190.9	183,140	0.38
Mirabaud	107.8	183,667	0.68
UBS	235.9	70,992	0.12
Marathon	372.9	410,437	0.44
Newton	205.3	94,879	0.18
Baillie Gifford*	125.2	197,933	0.63
Standard Life*	210.5	249,378	0.47
CBRE	148.3	77,034	0.21
Total		**£1,917,175**	**0.28**

*Estimated

7. CIPFA Benchmarking

Officers have received the results of the CIPFA benchmarking exercise comparing administration costs amongst LGPS funds for 2013/14.

Surrey's administration costs remain in the lowest quartile as per the key performance indicator benchmark requirements.

The cost comparator with similar sized LGPS funds is shown as Annex 3 to the report.

CONSULTATION:

8 The Chairman of the Pension Fund Board has been consulted on this report.

RISK MANAGEMENT AND IMPLICATIONS:

7

9 Risk related issues have been discussed and are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

10 Financial and value for money implications are discussed within the report.

DIRECTOR OF FINANCE COMMENTARY

11 The Director of Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

12 There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

13 The approval of the various options will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

14 There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

15 The following next steps are planned:

- Implementation of the various recommendation approvals.

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman

Annexes:

1. Asset Allocation Policy and Actual as at 30 June 2014 and 27 August 2014
2. Table of private equity holdings
3. CIPFA Benchmark Study: LGPS Administration Costs 2013/14

Sources/background papers:
None

Annex 1

Asset Allocation Update

The table shows the actual managed asset allocation as at 30 June 2014 against the target allocation. The allocation for 27 August 2014 is shown overleaf.

	Category	Allocation Policy %	Allocation at 30/06/2014	Variance %
Equities		**63.0**	**65.0**	**+2.0**
UK				
Legal and General	*Passive*	*10.0*	*10.0*	*+0.0*
Majedie	*Concentrated Active*	*7.0*	*6.9*	*-0.1*
Mirabaud	*Concentrated Active*	*4.0*	*4.0*	*+0.0*
UBS	*Core Active*	*8.0*	*8.7*	*+0.7*
Overseas				
Legal and General	*Passive*	*14.0*	*14.0*	*+0.0*
Marathon	*Concentrated Active*	*12.0*	*13.8*	*+1.8*
Newton	*Core Active*	*8.0*	*7.6*	*-0.4*
Property		**6.5**	**5.5**	**-1.0**
CBRE	*Core Active*	*6.5*	*5.5*	*-1.0*
Alternatives		**12.0**	**12.4**	**+0.4**
Standard Life	*Diversified growth*	*8.0*	*7.8*	*-0.2*
Baillie Gifford	*Diversified growth*	*4.0*	*4.6*	*+0.6*
Bonds		**18.5**	**17.1**	**-1.4**
Fixed interest gilts				
Legal and General	*Passive*	*2.1*	*1.5*	*-0.6*
Western	*Core Active*	*2.75*	*2.4*	*-0.4*
Index linked gilts				
Legal and General	*Passive*	*3.7*	*3.5*	*-0.2*
Western	*Core Active*	*0.0*	*0.2*	*+0.2*
Corporate bonds				
Legal and General	*Passive*	*1.9*	*1.7*	*-0.2*
Western	*Core Active*	*5.5*	*5.2*	*-0.3*
Total Return				
Franklin Templeton	*Unconstrained*	*2.55*	*2.6*	*+0.1*
Total		**100.0**	**100.0**	

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Asset Allocation Update

The table shows the actual managed asset allocation as at 27 August 2014 against the policy.

	Category	Allocation Policy %	Allocation at 27/08/2014	Variance %
Equities		**63.0**	**64.9**	**+1.9**
UK				
Legal and General	*Passive*	*10.0*	*9.8*	*-0.2*
Majedie	*Concentrated Active*	*7.0*	*6.9*	*-0.1*
Mirabaud	*Concentrated Active*	*4.0*	*4.0*	*0.0*
UBS	*Core Active*	*8.0*	*8.7*	*+0.7*
Overseas				
Legal and General	*Passive*	*14.0*	*14.0*	*+0.0*
Marathon	*Concentrated Active*	*12.0*	*13.8*	*+1.8*
Newton	*Core Active*	*8.0*	*7.7*	*-0.3*
Property		**6.5**	**5.8**	**-0.7**
CBRE	*Core Active*	*6.5*	*5.8*	*-0.7*
Alternatives		**12.0**	**12.1**	**+0.1**
Standard Life	*Diversified growth*	*8.0*	*7.7*	*-0.3*
Baillie Gifford	*Diversified growth*	*4.0*	*4.4*	*+0.4*
Bonds		**18.5**	**17.2**	**-1.3**
Fixed interest gilts				
Legal and General	*Passive*	*2.1*	*1.5*	*-0.6*
Western	*Core Active*	*2.75*	*3.3*	*+0.5*
Index linked gilts				
Legal and General	*Passive*	*3.7*	*3.5*	*-0.2*
Western	*Core Active*	*0.0*	*0.2*	*+0.2*
Corporate bonds				
Legal and General	*Passive*	*1.9*	*1.7*	*-0.2*
Western	*Core Active*	*5.5*	*4.5*	*-1.0*
Total Return				
Franklin Templeton	*Unconstrained*	*2.55*	*2.5*	*-0.0*
Total		**100.0**	**100.0**	

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Annex 2

Manager	Investment	Vintage Year	Paid in Capital £000s	Outstanding Commitment £000s	Total Commitment £000s	Distributions Received £000s	Fair Value of Remaining Investments £000s	Total Value Distributions + Fair Value £000s	Total Value vs Paid in Capital	IRR	Date of Valuation
UK Funds											
HG Capital	MUST 4	2002	2,647	353	3,000	5,148	124	5,272	2.0	23.6	31/03/2014
HG Capital	HG 5	2006	7,752	498	8,250	8,478	5,398	13,876	1.8	13.2	31/03/2014
HG Capital	HG 6	2009	9,647	353	10,000	3,285	7,063	10,348	1.1	3.1	31/03/2014
HG Capital	HG7	2013	1,314	13,686	15,000	0	1,247	1,247	0.9	too early	31/03/2014
ISIS	ISIS III	2003	12,362	1,638	14,000	28,463	134	28,597	2.3	23.8	31/03/2014
ISIS	ISIS IV	2007	11,522	3,478	15,000	9,061	8,082	17,143	1.5	16.0	31/03/2014
ISIS	ISIS Growth	2013	2,261	7,739	10,000	0	1,794	1,794	0.8	too early	31/03/2014
Darwin	Leisure Property	2013	20,000	0	20,000	0	20,000	20,000	1	too early	30/09/2013
Euro Funds											
Standard Life	ESP II	2004	7,444	560	8,004	8,272	3,359	11,631	1.6	13.0	31/03/2014
Standard Life	ESP 2006 B	2006	10,401	1,606	12,006	3,548	8,510	12,058	1.2	3.4	31/03/2014
Standard Life	ESP 2008	2008	7,035	4,971	12,006	665	7,149	7,814	1.1	4.8	31/03/2014
Standard Life	ESF	2011	2,837	11,171	14,008	0	2,384	2,384	0.8	too early	31/03/2014
Dollar Funds											
BlackRock	Vesey Street I	2001	2,777	146	2,924	4,520	465	4,985	1.8	13.5	31/03/2014
BlackRock	Vesey Street II	2003	2,734	190	2,924	3,342	1,648	4,991	1.8	11.5	31/03/2014
BlackRock	Vesey Street III	2005	9,005	1,228	10,233	4,791	6,761	11,551	1.3	4.2	31/03/2014
Goldman Sachs	GS PEP 2000 LP	2000	5,934	104	5,555	8,777	1,048	9,825	1.7	14.4	31/03/2014
Goldman Sachs	GS PEP 2004 LP	2004	6,075	89	5,847	5,094	3,679	8,773	1.4	7.8	31/03/2014
Goldman Sachs	GS PEP 2005 LP	2006	9,541	864	9,940	4,164	6,776	10,940	1.1	2.4	31/03/2014
Goldman Sachs	GS PEP X LP	2008	7,945	3,113	10,525	2,134	7,908	10,043	1.3	9.9	31/03/2014
Goldman Sachs	GS PEP XI LP	2011	5,485	18,059	23,389	215	5,069	5,284	1	too early	31/03/2014
Goldman Sachs	GS Vintage VI	2013	1,169	10,525	11,695	364	1,231	1,596	1.4	too early	31/03/2014
Capital Dynamics	US Solar	2011	13,110	1,508	14,618	2168	11,520	13,688	1	too early	31/03/2014
Capital Dynamics	Clean Energy	2012	11,695	2,924	14,618	0	12,318	12,318	1.1	too early	31/03/2014
Standard Life	SOF	2013	821	10,874	11,695	0	821	821	1.0	too early	31/03/2014
TOTAL			**171,513**	**95,677**	**265,237**	**102,489**	**124,488**	**226,979**	**1.3**		

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **SURREY PENSION FUND ACCOUNTS 2013/14**

SUMMARY OF ISSUE:

This report presents the audited financial statements of the Pension Fund for the year ended 31 March 2014, with respect of the County Council's obligations as the administering authority under the Local Government Pension Scheme (LGPS) Regulations.

The external auditor (Grant Thornton) has issued an unqualified opinion on the accounts and this is outlined in the Audit Findings for Surrey Pension Fund Report.

RECOMMENDATIONS:

It is recommended that the Pension Fund Board:

1 Note and approve the financial statements set out in Annex 1.

2 Note the content of the Audit Findings for Surrey Pension Fund Report as set out in Annex 2.

3 Note the Letter of Representation as set out in Annex 3.

4 Note the External Auditor's Report as set out in Annex 4.

REASON FOR RECOMMENDATIONS:

The Pension Fund Board must approve all financial statements produced for the Pension Fund.

DETAILS:

1 The Pension Fund statement of accounts was presented to the Audit and Governance Committee at its meeting on 31 July 2014 and approved, subject to the final completion of the external audit.

2 The external auditor is required to report on the Pension Fund financial statements. During the external audit, Grant Thornton identified some minor issues, which led to minor amendments being made to the 2013/14 draft financial statements and related notes to the accounts.

3 A copy of the financial statements and notes to the accounts included in Annex 1 will be published in the Pension Fund Annual Report 2014.

4 The Audit Findings for Surrey Pension Fund Report is presented at Annex 2 and sets out a summary of the work carried out, the conclusions reached and recommendations made. The Pension Fund Board will note that Grant Thornton issued an unqualified opinion on the financial statements.

5 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. The letter of representation, signed by the Director of Finance is included at Annex 3. A copy of the External Auditor's Report is shown at Annex 4.

8

6 It should be noted that the accounts were closed in record time this year, by the end of 23 May 2014, and were audited in time for presentation to the Audit and Governance Committee on 31 July 2014. The statutory deadline for completion of this process is 30 September.

CONSULTATION:

7 The Chairman of the Pension Fund has been consulted on the financial statements and has confirmed full support on the outcome.

RISK MANAGEMENT AND IMPLICATIONS:

8 There are no risk related issues contained within the report's proposals.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

9 Financial and value for money implications are contained within the financial statements and the Audit Findings Report.

DIRECTOR OF FI NANCE COMMENTARY

10 The Director of Finance has overseen the full process of the compilation of the financial statements and the external audit process.

LEGAL IMPLICATIONS – MONITORING OFFICER

11 There are no legal implications or legislative requirements associated with this report.

EQUALITIES AND DIVERSITY

12 The approval of the financial statements will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

13 There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

14 The following next steps are planned:

- Approval of the financial statements.
- Inclusion of the financial statements in the Pension Fund Annual Report 2014.

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman

Annexes:

1. Surrey Pension Accounts 2013/14
2. External Audit Finding Report
3. Director of Finance's Letter of Representation
4. External Auditor's Report

Sources/background papers:
None

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SURREY PENSION FUND ACCOUNTS 2013/2014

8

The accounts on the following pages give a stewardship report on the financial transactions of the Surrey Pension Fund during 2013/2014 and of the disposition of its assets at 31 March 2014.

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 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 2013 and 31 March 2014 are:

31 Mar 2013		31 Mar 2014
30,608	Employees in the fund	32,530
20,553	Pensioners	21,598
27,648	Deferred pensioners	30,639
78,809	**Total**	**84,767**

Surrey pension fund account

2012/2013 £000		Note	2013/2014 £000
	Contributions and benefits		
159,544	Contributions receivable	7	**149,615**
13,833	Transfers in	8	**14,751**
173,377			**164,366**
-113,893	Benefits payable	9	**-119,223**
-7,945	Payments to and on account of leavers	10	**-6,255**
-1,867	Administrative expenses	14	**-1,928**
-123,705			**-127,406**
49,672	**Net additions from dealings with members**		**36,960**
	Return on investments		
41,687	Investment income	17	**47,758**
-1,042	Taxes on income	16	**-1,081**
278,985	Change in market value of investments	18	**175,422**
-6,856	Investment management expenses	15	**-10,275**
312,774	**Net return on investments**		**211,824**
362,446	**Net increase in the fund during the year**		**248,784**
	Net assets of the fund		
2,196,270	**At 1 April**		**2,558,716**
2,558,716	**At 31 March**		**2,807,500**

Net asset statement

31 Mar 2013 £000		Note	31 Mar 2014 £000
	Investment assets	18	
347,863	Fixed interest securities		**352,134**
99,100	Index linked securities		**94,675**
1,574,687	Equities		**1,747,131**
120,748	Property unit trusts		**165,824**
238,986	Diversified growth		**270,937**
90,336	Private equity		**101,814**
	Derivatives	18c	
-	- Futures		**31**
2,153	- Foreign exchange contracts		**7,865**
59,723	Cash		**39,212**
11,128	Other investment balances	18b	**9,676**
	Investment liabilities		
	Derivatives	18c	
-310	- Futures		**-66**
-7,500	- Foreign exchange contracts		**-3**
-3,810	Other investment balances	18b	**-7,718**
-	Borrowings		**-4,500**
2,533,104	**Net investment assets**		**2,777,012**
16,335	**Long-term debtors**	12	**14,520**
13,582	**Current assets**	11	**20,761**
-4,305	**Current liabilities**	13	**-4,793**
2,558,716	**Net assets of the fund at 31 March**		**2,807,500**

The financial statements 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 on an International Accounting Standard (IAS) 19 basis is disclosed at note 26 of these accounts.

8

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 county council is the reporting entity for this pension fund.

The following description of the fund is a summary only. For more detail, reference should be made to the Surrey Pension Fund Annual Report 2013/14 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 Superannuation Act 1972. The fund is administered in accordance with the following secondary legislation:

- The LGPS (Benefits, Membership & Contributions) Regulations 2007 (as amended)
- The LGPS (Administration) Regulations 2008 (as amended)
- The LGPS (Management & Investment of Funds) Regulations 2009

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 2013/14 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 7.5% of pensionable pay for the financial year ending 31 March 2014. 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 will apply from April 2014 onwards. Currently employer contribution rates range from 12.0% to 30.0% of pensionable pay.

d) Benefits
Pension benefits accrued under the LGPS to 31 March 2014 are based on final pensionable pay and length of pensionable service.

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).
The LGPS was changed on the 1st April 2008 adjusting the method by which entitlements are accrued. Benefits earned prior to the change are unaffected.

8

	Service pre 1 April 2008	**Service 1 April 2008 until 31 March 2014**
Basis of pension	1/80th 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

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.

8

	Service 1 April 2008 until 31 March 2014	LGPS 2014 scheme
Basis of pension	Final salary	Career average revalued earnings
Accrual rate	1/60th of salary	1/49th 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	
Pensionable payroll banding	Contribution rate
Up to £13,500	5.5%
£13,501 to £21,000	5.8%
£21,001 to £34,000	6.5%
£34,001 to £43,000	6.8%
£43,001 to £60,000	8.5%
£60,001 to £85,000	9.9%
£85,001 to £100,000	10.5%
£100,001 to £150,000	11.4%
More than £150,000	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 2013/14 financial year and its position at the year end at 31 March 2014. The accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 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 26 of these accounts. 8

These accounts have been prepared on a going concern basis.

Note 3: Summary of significant accounting policies

Fund account – revenue recognition

a) Contribution income

Normal contributions, both from the members and from the employer, are accounted for on an accruals basis at the percentage rate recommended by the fund actuary 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/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 in 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

8 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.

Fund account – expense items

d) 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.

e) 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 2014 is reported as a current liability.

f) Administration expenses

Pensions administrative expenses reflect the costs incurred in the payment of pensions and other benefits, actuarial advice, dealing with transfer values and the maintenance of member records. 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 pensions administration team are recharged to the fund. Management, accommodation and other overheads are apportioned to the fund in accordance with council policy.

g) Investment management 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.

Investment management expenses also include fees for investment advice and performance measurement services together with the county council costs incurred on administration and monitoring of investment related issues.

Net assets statement

8

h) 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, and financial liabilities 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 in 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.
- 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.

iv) Limited partnerships
Fair value is based on the net asset value ascertained from periodic valuations provided by those controlling the partnership.

v) 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.

i) 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.

j) 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 contacts 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.

k) 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.

l) 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.

m) 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.

n) 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. 8

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 polices

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 2014 was £102 million (£90 million at 31 March 2013).

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 26. 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 as at 31 March 2014 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

8

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 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 £102 million. There is a risk that this investment may be over or under stated in the accounts.

Note 6: Events after the balance sheet date

The Statement of Accounts will be authorised for issue by the Chief Financial Officer in July 2014. 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

2012/2013 £000		2013/2014 £000
109,514	Employers	115,441
31,880	Members	34,174
18,150	Magistrates Court Services deficit funding	-
159,544		**149,615**

2012/2013 £000		2013/2014 £000
78,045	Administering authority	77,812
50,889	Scheduled bodies	59,663
12,460	Admitted bodies	12,140
18,150	Magistrates Court Services deficit funding	-
159,544		**149,615**

Magistrates Court Services deficit funding for 2012/13 reflects the merger of the Magistrates Court Services. A detailed explanation is shown in note 12 long term debtors.

Note 8: Transfers in from other pension funds

2012/2013 £000		2013/2014 £000
-	Group transfers from other schemes	-
13,833	Individual transfers in from other schemes	14,751
13,833		**14,751**

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Note 9: Benefits payable

By category

2012/13 £000		2013/14 £000
94,191	Pensions	99,529
16,818	Commutation and lump sum retirement benefits	17,092
2,840	Lump sum death benefits	2,519
44	Interest on late payment of benefits	83
113,893		**119,223**

By employer

2012/2013 £000		2013/2014 £000
54,388	Administering Authority	55,943
50,875	Scheduled Bodies	53,503
8,586	Admitted Bodies	9,694
113,849		**119,140**

The total does not include interest on late payment of benefits £83,427 (£43,874 2012/13)

Note 10: Payments to and on account of leavers

2012/2013 £000		2013/2014 £000
96	Group transfers to other schemes	0
7,814	Individual transfers to other schemes	6,222
30	Refunds of contributions	31
5	Payments for members joining state schemes	2
7,945		**6,255**

Note 11: Current assets

2012/2013 £000		2013/2014 £000
2,445	Contributions - employees	3,364
9,239	Contributions - employer	13,314
1,898	Sundry debtors	4,083
13,582		**20,761**

8

Analysis of current assets

2012/2013 £000		2013/2014 £000
713	Central government bodies	1,984
10,907	Other local authorities	16,980
1,962	Other entities and individuals	1,797
13,582		**20,761**

Note 12: Long term debtors

2012/2013 £000		2013/2014 £000
16,335	Central government bodies	14,520
16,335		**14,520**

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 a that 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 2014 remains £16.335m but £1.815m is due in 2014/15, leaving a long term debtor of £14.520m.

8

Note 13: Current liabilities

2012/2013 £000		2013/2014 £000
4,257	Sundry creditors	4,731
48	Benefits payable	62
4,305		**4,793**

Analysis of current liabilities

2012/2013 £000		2013/2014 £000
1,157	Central government bodies	1,225
1,592	Other local authorities	1,550
1,556	Other entities and individuals	2,018
4,305		**4,793**

Note 14: Administrative expenses

2012/2013 £000		2013/2014 £000
901	Employee related	941
826	Support services	626
20	External audit fee	27
6	Legal and other professional fees	1
114	Actuarial fees	333
1,867		**1,928**

Note 15: Investment expenses

2012/2013 £000		2013/2014 £000
6,446	Management fees	9,929
252	Custody fees	218
7	Performance measurement services	7
151	Investment consultancy fees	87
-	Interest paid	34
6,856		**10,275**

Note 16: Taxes on Income

2012/2013		2013/2014
£000		£000
697	Withholding tax - equities	790
345	Withholding tax - property	291
1,042		**1,081**

8

Note 17: Investment income

2012/2013		2013/2014
£000		£000
	Fixed interest	
8,143	UK	5,859
3,051	Overseas	5,554
	Index linked	
55	UK	2
	Equities	
15,648	UK	18,017
8,317	Overseas	10,244
5,116	**Property unit trusts**	6,069
1,118	**Diversified growth**	1,788
239	**Cash**	152
-	**Other**	73
41,687		**47,758**

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.

8

Note 18a: Reconciliation of movements in investments and derivatives

	Market value at 31 Mar 2013 £000	Purchases during the year and derivate payments £000	Sales during the year and derivative payments £000	Market movements £000	Market value at 31 Mar 2014 £000
Fixed interest securities	**347,863**	65,341	-52,108	-8,962	**352,134**
Index linked securities	**99,100**	3,190	-4,096	-3,519	**94,675**
Equities	**1,574,687**	397,612	-362,932	137,764	**1,747,131**
Property unit trusts	**120,748**	49,281	-13,330	9,125	**165,824**
Diversified growth	**238,986**	25,135	0	6,816	**270,937**
Private equity	**90,336**	48,404	-37,804	878	**101,814**
Derivatives					
- Futures	**-310**	347	-345	273	**-35**
- Forex contracts	**-5,347**	5,727	-25,720	33,202	**7,862**
	2,466,063	**595,037**	**-496,335**	**175,577**	**2,740,342**
Cash	**59,723**			-155	**39,212**
Other investment balances	**7,318**				**1,958**
Borrowing	**-**				**-4,500**
	2,533,104			**175,422**	**2,777,012**

18

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	Market value at 1 April 2012	Purchases during the year and derivate payments	Sales during the year and derivative payments	Market movements	Market value at 31 Mar 2013
	£000	£000	£000	£000	£000
Fixed interest securities	**309,600**	209,052	-190,222	19,433	**347,863**
Index linked securities	**79,752**	74,945	-64,442	8,845	**99,100**
Equities	**1,510,160**	878,231	-1,051,499	237,795	**1,574,687**
Property unit trusts	**120,306**	12,745	-8,685	-3,618	**120,748**
Diversified growth	**-**	224,025		14,961	**238,986**
Private equity	**84,776**	13,283	-17,890	10,167	**90,336**
Derivatives					
- Futures	**126**	192	-763	135	**-310**
- Forex conts	**6,525**	13,027	-16,271	-8,628	**-5,347**
	2,111,245	**1,425,500**	**-1,349,772**	279,090	**2,466,063**
Cash	**70,564**			-105	**59,723**
Other investment balances	**9,984**				**7,318**
Borrowing					
	2,191,793			**278,985**	**2,533,104**

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.

Transaction costs are included in the cost of purchases and sale proceeds. Transaction costs include costs charged directly to the scheme such as commissions, stamp duty and other fees.

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.

8

Note 18b: Analysis of investments

	31 Mar 2013	31 Mar 2014
Fixed interest securities	**£000s**	**£000s**
UK public sector & quoted	137,890	136,448
UK pooled funds	87,769	86,739
Overseas public sector & quoted	52,316	60,175
Overseas pooled fund	69,888	68,772
	347,863	**352,134**
Index linked securities		
UK public sector & quoted	2,945	2,199
UK pooled funds	96,155	92,476
	99,100	**94,675**
Equities		
UK quoted	452,587	513,497
UK pooled funds	209,571	237,645
Overseas quoted	423,779	460,880
Overseas pooled funds	488,750	535,109
	1,574,687	**1,747,131**
Property unit trusts	**120,748**	**165,824**
Diversified growth	**238,986**	**270,937**
Private equity		
Limited partnerships	38,683	49,201
Fund of funds	51,653	52,613
	90,336	**101,814**
Derivatives		
Futures	-310	-35
FX forward contracts	-5,347	7,862
	-5,657	**7,827**
Cash deposits	**59,723**	**39,212**
Borrowings		**-4,500**
Other investment balances		
Outstanding sales	5,008	3,291
Outstanding purchases	-3,810	-7,693
Tax due on accrued income		-25
Accrued income - dividends and interest	6,120	6,385
	7,318	**1,958**
Total investments	**2,533,104**	**2,777,012**

20

Note 18c: 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 2014 the fund had two futures contracts in place with a net unrealised loss of £35,740 (net unrealised loss of £310,410 at 31 March 2013).

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2013/14

Contract	Expiration date	Expiration date within	Type of underlying investment	Economic exposure £'000	Asset £'000	Liability £'000
Futures	20/06/2013	3 Months	UK Equity	3,992	31	
Futures	26/06/2013	3 Months	UK Government Bonds	10,077		-66

2012/13

Contract	Expiration date	Expiration date within	Type of underlying investment	Economic exposure £'000	Asset £'000	Liability £'000
Futures	28/06/2013	3 Months	Exchange traded UK government bonds	16,867	0	-310

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 2014 the Fund had forward currency contracts in place with a net unrealised gain of £7,862,075 (net unrealised loss of £5,346,696 at 31 March 2013).

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2013/14

No of contracts	Contract settlement date within	Currency Bought	Currency Sold	Notional amount (local currency) Bought (000)	Notional amount (local currency) Sold (000)	Asset £'000	Liability £'000
1	One month	AUD	HKD	8	-56		
1	One month	EUR	DKK	31	-234		
11	One month	EUR	GBP	260	-215		
6	Two months	GBP	EUR	105,885	-127,629	351	
1	One month	GBP	HKD	34	-443		
3	Two months	GBP	JPY	55,062	-9,092,353	2,079	
5	One month	GBP	USD	1,918	-3,191	4	
10	Two months	GBP	USD	242,455	-395,044	5,431	
1	One month	HKD	SGD	495	-80		
3	One month	JPY	GBP	80,204	-470		-3
1	One month	USD	AUD	9	-9		
						7,865	**-3**

22

2012/13

No of contracts	Contract settlement date within	Currency Bought	Currency Sold	Notional amount (local currency) Bought (000)	Notional amount (local currency) Sold (000)	Asset £'000	Liability £'000
2	One month	CHF	GBP	106	-74		
1	One month	DKK	GBP	545	-62		
1	One month	EUR	GBP	117	-99		
2	One month	GBP	DKK	10	-88		
2	One month	GBP	EUR	11	-12		
6	Two months	GBP	EUR	70,636	-81,796	1,433	
3	One month	GBP	JPY	234	-33,380		
4	Two months	GBP	JPY	33,187	-4,854,833		-834
1	One month	GBP	MYR	125	-588		
1	One month	GBP	SEK	110	1,083		
3	One month	GBP	USD	472	-715		
9	Two months	GBP	USD	210,711	-329,676		-6,558
1	One month	JPY	GBP	500	-4		
1	One month	JPY	USD	329,446	-3,522	26	-38
1	Four months	USD	EUR	3,207	-2,439	118	-70
1	One month	USD	GBP	221	-146		
1	Two months	USD	GBP	2,623	-1,661	67	
1	Four months	USD	GBP	5,963	-3,704	225	
1	One months	USD	JPY	3,936	-329,446	284	
						2,153	**-7,500**

Stock Lending

During the financial year 2013/14 the fund instigated a stock lending programme in partnership with the fund custodian. As at 31 March 14 the value of quoted securities on loan was £83.2m in exchange for collateral held by the fund custodian at fair value of £89.0m

8

Note 18d: Investments analysed by fund manager

Market value 31 March 2013 £000	%	Manager	Market value 31 March 2014 £000	%
792,326	32.8	Legal & General Investment Management	865,106	32.6
158,471	6.6	Majedie Asset Management	190,067	7.2
98,382	4.1	Mirabaud Asset Management	106,845	4.0
198,809	8.2	UBS Asset Management	236,582	8.9
341,002	14.1	Marathon Asset Management	365,046	13.8
190,680	7.9	Newton Investment Management	200,853	7.6
202,813	8.4	Western Asset Management	205,702	7.8
67,681	2.8	Franklin Templeton Investments	68,772	2.6
143,613	5.9	Standard Life Investments	148,437	5.6
95,372	3.9	Baillie Gifford Life Limited	122,500	4.6
128,307	5.3	CBRE Global Multi-Manager	143,060	5.4
2,417,456			**2,652,970**	

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 2013 £000	% of total fund	Security	Market value 31 March 2014 £000	% of total fund
366,009	14.4	Legal & General World Developed Equity Index	410,273	14.8
197,336	7.8	Legal & General UK Equity Index	221,203	8.0
143,613	5.7	Standard Life Global Absolute Return Strategies	148,437	5.3

Note 19a: 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 2013				As at 31 March 2014		
Designated as fair value though profit and loss	Loans and receivables	Financial liabilities at amortised costs		Designated as fair value though profit and loss	Loans and receivables	Financial liabilities at amortised costs
£000	£000	£000		£000	£000	£000
			Financial assets			
347,863			Fixed interest securities	352,134		
99,100			Index linked securities	94,675		
1,574,687			Equities	1,747,131		
120,748			Property unit trusts	165,824		
238,986			Diversified growth	270,937		
90,336			Private equity	101,814		
2,154			Derivatives	7,896		
	59,723		Cash		39,212	
11,128			Other investment balances	9,676		
	29,916		Debtors		35,281	
2,485,002	**89,639**			**2,750,087**	**74,493**	
			Financial liabilities			
-7,810			Derivatives	-69		
-3,810			Other investment balances	-7,718		
		-4,305	Creditors			-4,793
			Borrowings	-4,500		
-11,620		**-4,305**		**-12,287**		**-4,793**
2,473,382	**89,639**	**-4,305**		**2,737,800**	**74,493**	**-4,793**

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Note 19b: 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 2014	Quoted market price Level 1	Using observable inputs Level 2	With significant unobservable inputs Level 3	Total
	£000	£000	£000	£000
Financial assets				
Financial assets though profit & loss	2,537,799	70,289	141,999	2,750,087
Total financial assets	**2,537,799**	**70,289**	**141,999**	**2,750,087**
Financial liabilities				
Financial liabilities though profit & loss	-12,287			-12,287
Total financial liabilities	**-12,287**			**-12,287**
Net financial assets	**2,525,512**	**70,289**	**141,999**	**2,737,800**

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31 March 2013	Quoted market price Level 1	Using observable inputs Level 2	With significant unobservable inputs Level 3	Total
	£000	£000	£000	£000
Financial assets				
Financial assets though profit & loss	2,322,578	62,068	100,356	2,485,002
Total financial assets	**2,322,578**	**62,068**	**100,356**	**2,485,002**
Financial liabilities				
Financial liabilities though profit & loss	-11,620			-11,620
Total financial liabilities	**-11,620**			**-11,620**
Net financial assets	**2,310,958**	**62,068**	**100,356**	**2,473,382**

Note 19c: Book cost

The book cost of all investments at 31 March 2014 is £2,284,926,883 (£2,107,273,868 at 31 March 2013).

Note 20: Outstanding commitments

At 31 March 2014 the Fund held part paid investments on which the liability for future calls amounted to £107,414,081 (£101,599,103 as at 31 March 2013).

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Note 21: 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.

8

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 2013/14 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. The percentage change for

Asset type	Value at 31 March 2014 £000	Change	Value on increase £000	Value on decrease £000
UK equities	751,142	11.94%	840,828	661,456
Overseas equities	995,989	12.11%	1,116,603	875,375
Total bonds	352,134	5.55%	371,677	332,591
ILG	94,675	8.32%	102,552	86,798
Cash	39,212	0.02%	39,220	39,204
Property	165,824	2.40%	169,804	161,844
Diversified Growth Fund	270,937	4.43%	282,940	258,934
Total Investment Assets (1)	**2,669,913**	**8.49%**(2)	**2,896,589**	**2,443,237**

(1) The above table excludes private equity, derivatives and other investment balances.

(2) 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.

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Asset type	Value at 31 March 2013 £000	Change	Value on increase £000	Value on decrease £000
UK equities	662,158	13.10%	748,901	575,415
Overseas equities	912,529	12.70%	1,028,420	796,638
Total bonds	347,863	5.30%	366,300	329,426
ILG	99,100	8.00%	107,028	91,172
Cash	59,723	0.00%	59,723	59,723
Property	120,748	2.40%	123,646	117,850
Total Investment Assets (1)	**2,202,121**	**8.31%**(2)	**2,385,117**	**2,019,125**

(1) The above table excludes diversified growth funds, private equity, derivatives and other investment balances.

(2) 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. In February 2013 50% of UK gilts managed by Western were redeemed and the proceeds were invested in Franklin Templeton's Global Total Return Fund. This has a more diverse range of fixed income investment opportunities reducing the overall interest rate risk, as there is less exposure to individual interest rate movements.

The fund's direct exposure to interest rate movements as at 31 March 2014 and 31 March 2013 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value.

As at 31 March 2013 £000		As at 31 March 2014 £000
59,723	Cash & cash equivalents	39,212
347,863	Fixed interest securities	352,134
407,586	**Total**	**391,346**

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.

8

Asset type	Carrying amount as at 31 March 2014	Change in net assets	
		+100 bps	- 100 bps
	£000	£000	£000
Cash & cash equivalents	39,212	392	-392
Fixed interest securities	352,134	3,521	-3,521
Total	**391,346**	**3,913**	**-3,913**

Asset type	Carrying amount as at 31 March 2013	Change in net assets	
		+100 bps	- 100 bps
	£000	£000	£000
Cash & cash equivalents	59,726	597	-597
Fixed interest securities	347,863	3,479	-3,479
Total	**407,589**	**4,076**	**-4,076**

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 2013/14 reporting period due to exchange rate movements.

The analysis assumes all other variables remain constant. A significant proportion of overseas assets are invested via pooled funds denominated in Sterling.

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Asset type	Value at 31 March 2014 £000	% Change	Value on increase £000	Value on decrease £000
Overseas equities	526,139	5.30%	554,024	498,254
Fixed interest	12,268	5.30%	12,918	11,618
Property and Private Equity	83,469	5.30%	87,893	79,045
Cash and Other Assets	-388,294	5.30%	-408,874	-367,714
Total	**233,582**	**5.30%**	**245,961**	**221,203**

For comparison last year figures are included below.

Asset type	Value at 31 March 2013 £000	% Change	Value on increase £000	Value on decrease £000
Overseas equities	488,369	6.10%	518,160	458,578
Fixed interest	2,207	6.10%	2,342	2,072
Property unit trust	11,432	6.10%	12,129	10,735
Cash	2,701	6.10%	2,866	2,536
Total	**504,709**	**6.10%**	**535,497**	**473,921**

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 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'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. 8

The fund has a call account with NatWest Bank. In line with the treasury strategy, the maximum deposit level allowed with each counterparty is £15 million. The NatWest call account has a rating of A (or equivalent) with all three credit rating agencies

Balance at 31 March 2013 £000		**Balance at 31 March 2014 £000**
	Call account	
15,000	NatWest	
	Money market fund	
3,910	Royal Bank of Scotland	
	Current account	
343	HSBC	-402
19,253	Internally Managed Cash	-402
40,470	Externally Managed Cash	39,614
59,723	**Total Cash**	**39,212**

The fund's cash holding under its treasury management arrangements as at 31 March 2014 was £-0.4 million (£19.3 million at 31 March 2013).

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.

8

The fund has immediate access to the internally managed cash holdings at NatWest. Whilst fixed term deposits are allowed under the pension fund treasury strategy, no investment of this type has been made since the implementation of the pension fund bank account in April 2011.

The fund is able to borrow cash to meet short-term cash requirements, The fund exercised this ability on a number of occasions during 2013/14 with one loan outstanding as at the 31 March 2014 for the value of £4.5m.

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.

8

Note 22: Related party transactions

i) Employer pension contributions paid by Surrey County Council in 2013/14 amounted to £59,321,037.33 (£55,659,746 in 2012/13).

2012/2013 £000		2013/2014 £000
37,035	Employers' current service contributions	42,483
17,354	Lump sum payments to recover the deficit in respect of past service	16,379
1,271	Payments into the fund to recover the additional cost of early retirement liabilities	459
55,660		**59,321**

ii) Surrey Pension Fund paid Surrey County Council £1,502,911 for services provided in 2013/14 (£1,537,236 in 2012/13).

2012/2013 £000		2013/2014 £000
198	Treasury management, accounting and managerial services	188
1,339	Pension administration services	1,315
1,537		**1,503**

iii) Net amounts owed by Surrey County Council to the fund as at 31 March 2014 were £9,819,633 (£5,866,326 at 31 March 2013).

Note 23: 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.

2012/13 £	Position	2013/14 £	
19,991	Chief Finance Officer	20,057	1
58,456	Pension Fund & Treasury Manager	74,780	2
51,994	Senior Accountant	48,054	3
130,441		**142,891**	

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

8

Note 24: Custody

Custody arrangements for securities and cash balances are provided by the fund's global custodian, The Northern Trust Company. 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
ISIS Capital	Lloyds Banking Group
Standard Life	State Street Global Advisors, Deutsche Bank & JP Morgan
Capital Dynamics	Bank of America

Note 25 : Actuarial statement for 2013/14 - funding arrangements

This statement has been prepared in accordance with Regulation 34(1)(d) of the Local Government Pension Scheme (Administration) Regulations 2008, and Chapter 6 of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the UK 2013/14.

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. 8

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 my 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:

8

	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 slightly better than expected since the last valuation (excluding the effect of any membership movements). Real bond yields have risen and asset returns have been broadly in line with that expected meaning that funding levels are likely to have improved since the 2013 valuation.

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

Barry McKay

Fellow of the Institute and Faculty of Actuaries

For and on behalf of Hymans Robertson LLP

3 June 2014

Note 26: Actuarial present value of future retirement benefits

CIPFA’s Code of Practice on Local Authority Accounting 2013/14 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 2014 £m	31 March 2013 £m
Present value of promised retirement benefits	4,151	3,982

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 2013 comprises £1,768m in respect of employee members, £818m in respect of deferred pensioners and £1,565m in respect of pensioners. The approximation involved in the roll forward model means that the split of scheme liabilities between the three classes of members 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 2014 is to increase the actuarial present value by £68m.

Financial assumptions

My recommended financial assumptions are summarised below:

Year ended	31 March 2014	31 March 2013
Inflation/pension increase rate	2.8%	2.8%
Salary increase rate	4.1%	5.1%*
Discount rate	4.3%	4.5%

*Salary increases are 1% p.a. nominal until 31 March 2015 reverting to long term rate thereafter

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:

8

	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.

Please note that the assumptions have changed since the previous IAS26 disclosure for the Fund.

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 2014 for IAS19 purposes' dated 14 April 2014. 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

3 June 2014

For and on behalf of Hymans Robertson LLP

Note 27: Additional Voluntary Contributions

Market Value 2012/13 £000	Position	Market Value 2013/14 £000
7,602	Prudential	8,242
7,602		**8,242**

Additional Voluntary Contributions, net of returned payments, of £1,428,220 were paid directly to prudential during the year (£1,134,656 during 2012/13).

Note 28: 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 29: Annual report

The Surrey Pension Fund Annual Report 2013/2014 provides further details on the management, investment performance and governance of the Fund.

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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.

Grant Thornton

The Audit Findings Report for Surrey County Council Pension Fund

Year ended 31 March 2014

31 July 2014

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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.

Contents

DRAFT

Section 1: Executive summary

DRAFT

Executive summary

Purpose of this report
This report highlights the key issues arising from the audit of Surry County Council Pension Fund's ('the Fund') financial statements for the year ended 31 March 2014. 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.

Under the Audit Commission's Code of Audit Practice we are required to report whether, in our opinion, the Fund's financial statements present a true and fair view of the financial position, the financial transactions of the Fund during the year and whether they have been properly prepared in accordance with the Code of Practice on Local Authority Accounting.

Introduction
In the conduct of our audit we have not had to alter or change our planned audit approach, which we communicated to you in our Audit Plan dated May 2014.

Our audit is nearing completion. We are finalising our procedures in the following areas:

Procedures nearing completion, subject to provision of evidence:
- finalising of our testing of investment balances, where we are awaiting third party confirmations
- finalising of our testing of purchases and sales, where are awaiting details from the custodian.

Procedures to be performed as part of audit closing procedures:
- receipt and review of the final version of the financial statements
- receipt and review of the final version of the annual report
- obtaining and reviewing the management letter of representation
- updating our post balance sheet events review, to the date of signing the opinion
- final senior audit management and quality reviews

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

Key issues arising from our audit
Financial statements opinion
We anticipate providing an unqualified opinion on the Fund's financial statements.

We have identified one adjustment affecting the Fund's reported financial position. The draft and unaudited financial statements recorded net assets carried forward of £2,803 million; the audited financial statements show net assets carried forward of £2,808 million. This change is a result of an amendment of investment market returns and the cash balance as set out in section two of this report. We have also agreed with officers, a small number of adjustments to improve the presentation of the financial statements.

8

Executive summary

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

- the financial statements provided to audit on 16 June 2014 were complete and prepared in accordance with the CIPFA's Code of Practice for Local Authority Accounting
- officers produced high quality working papers to support the financial statements and provided timely responses to audit queries
- officers agreed to amend the financial statements for all recommended accounting and disclosure changes we identified.

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 2014

Section 2: Audit findings

Audit findings

In this section we present our findings in respect of matters and risks identified at the planning stage of the audit and additional matters that arose during the course of our work. We set out on the following pages the work we have performed and findings arising from our work in respect of the audit risks we identified in our audit plan, presented to the Audit and Governance Committee on 29 May 2014. We also set out the adjustments to the financial statements from our audit work and our findings in respect of internal controls.

Changes to Audit Plan

We have not made any changes to our Audit Plan as previously communicated to you.

Audit opinion

We anticipate that we will provide an unqualified opinion as set out in Appendix A.

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 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.	**Revenue** Under ISA 240 there is a presumed risk that revenue (which for the purposes of the Surrey County Council Pension Fund we have considered as investment income, transfers into the scheme and contributions) may be misstated due to the improper recognition of revenue.	We rebutted this presumption and did not consider this to be a significant risk for Surrey County Council Pension Fund since: • The nature of the Pension Fund's revenue is in many respects relatively predictable and does not generally involve cash transactions. • The split of responsibilities between the Pension Fund, its fund managers and the custodian provides a very strong separation of duties reducing the risk around investment income. • Revenue contributions are made by direct salary deductions and direct bank transfers from admitted /scheduled bodies and are supported by separately sent schedules. They are directly attributable to gross pay making any improper recognition unlikely. • Transfers into the scheme are all supported by an independent actuarial valuation of the amount which should be transferred. They are subject to agreement between the transferring and receiving funds.	Our audit work has not identified any issues in respect of revenue recognition.
2.	**Management override of controls** Under ISA 240 there is a presumed risk of management over-ride of controls	• review of accounting estimates, judgements and decisions made by management • testing of journals entries • review of unusual significant transactions	Our audit work has not identified any evidence of management override of controls. In particular the findings of our review of journal controls and testing of journal entries has not identified any significant issues. We set out later in this section of the report our work and findings on key accounting estimates and judgements.

DRAFT

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.

Transaction cycle	Description of potential risk	Work completed	Assurance gained & issues arising
Investments	• Investments not valid • Alternative investments not valid • Investment activity not valid • Fair value measurements not correct	We have undertaken the following work in relation to this risk: • We have reviewed the reconciliation between information provided by the fund managers, the custodians and the Pension Fund's own records and are satisfied with the explanations for any material variances. • We selected a sample of the individual investments held by the Fund at the year end and tested the valuation of the sample by agreeing prices to third party sources (quoted investments) or by review of the valuation methodology used to ensure it represents fair value (unquoted investments and direct property investments). • We confirmed the existence of investments directly with independent custodian and/or fund managers. • We tested a sample of sales and disposals during the year back to detailed information provided by the custodian and fund managers.	During the audit one misstatement relating to investment market returns and cash balances was identified. This is set out on page12. Subject to the satisfactory resolution and completion of outstanding matters set out on page 5 of this report, our audit work has not identified any other significant issues in relation to the risk identified.
Benefit Payments	• Benefits improperly computed/ liability understated	• We selected a sample of individual transfers, pensions in payment (new and existing), lump sum benefits and refunds and tested them by reference to the benefit calculation on their member file. • We rationalised pensions paid with reference to changes in pensioner numbers and increases applied in year. We did not identify any unusual trends. • We completed testing on transfers out and lump sum payments. • We compared the movements on membership statistics by reference to starters, leavers and changes in circumstances.	Our audit work has not identified any significant issues in relation to the risk identified.

Audit findings against other risks (continued)

Transaction cycle	Description of potential risk	Work completed	Assurance gained & issues arising
Contributions	• Recorded contributions not correct	• We confirmed the existence of controls operated by the Pension Fund to ensure that it receives all expected contributions from member bodies. • We rationalised contributions received with reference to changes in member body payrolls and number of contributing pensioners.	Our audit work has not identified any significant issues in relation to the risk identified.
Member data	• Member data not correct	• We confirmed the existence of controls and reconciliations covering the determination of member eligibility, the input of evidence onto the Pensions Administration System and the maintenance of member records. • We tested the key controls identified.	Our audit work has not identified any significant issues in relation to the risk identified.

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Accounting policies, estimates & 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.

Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	• Income to the fund is accounted for on an accruals basis	• The Fund's accounting policies are appropriate under IAS 18 Revenue and the Code of Practice on Local Authority Accounting. • Accounting policies are adequately disclosed in the financial statements.	●
Judgements and estimates	• Key estimates and judgements include; – Investment valuation – Promised value of future retirement benefits	• The policies adopted for accounting estimates are appropriate under the Fund's accounting framework • Our testing indicates that estimates included in the financial statements have been calculated based on reasonable judgements and assumptions. Estimates are calculated based on the best available information. • The level of judgement required by the Fund is low . Estimates used are generally supported by adequate working papers. • Disclosure of accounting policies in the financial statements is in line with the recommended disclosures .	●
Other accounting policies	• We have reviewed the Fund's policies against the requirements of the CIPFA Code and accounting standards.	• Our review of accounting policies has not highlighted any issues which we wish to bring to your attention	●

Assessment
- ● Marginal accounting policy which could potentially attract attention from regulators
- ● Accounting policy appropriate but scope for improved disclosure
- ● Accounting policy appropriate and disclosures sufficient

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Adjusted misstatements

A number of adjustments to the draft financial statements have been identified during the audit process. We are required to report all misstatements to those charged with governance, whether or not the financial statements have been adjusted by management. The table below summarises the adjustments arising from the audit which have been processed by management.

Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the financial statements.

	Detail	Fund Account £'000	Net Asset Statement £'000	Impact on net assets carried forward £000
1	The Fund has amended investment market returns re-analysed and purchase and sales transactions following the identification of differences to fund manager confirmations. This has resulted in changes to the net assets statement, fund account and a number of other notes. The adjustment is:			
	Change in Market Value of Investments	(4,400)		
	Cash		4,400	4,400
	Overall impact	**£4,400**	**(£4,400)**	**£4,400**

Misclassifications & disclosure changes

During the audit we identified a number of narrative presentation and disclosure items in the financial statements and recommended additional disclosures to enhance the presentation of the financial statements. All amended disclosures have been agreed and applied in the Pension Fund accounts.

There are no unadjusted misstatements.

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Internal controls

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

Our audit included consideration of internal control 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. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

From the work we completed we did not identify any significant weaknesses in internal controls.

Assessment

- Significant deficiency – risk of significant misstatement
- Deficiency – risk of inconsequential misstatement

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Other communication requirements

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

	Issue	Commentary
1.	**Matters in relation to fraud**	• We have previously discussed the risk of fraud with the Audit and Governance Committee. We have not been made aware of any incidents in the period and no other issues have been identified during the course of our audit.
2.	**Matters in relation to laws and regulations**	• We are not aware of any significant incidences of non-compliance with relevant laws and regulations.
3.	**Written representations**	• A standard letter of representation has been requested from the Fund.
4.	**Disclosures**	• Our review found no material omissions in the financial statements.
5.	**Matters in relation to related parties**	• We are not aware of any related party transactions which have not been disclosed.
6.	**Going concern**	• Our work has not identified any reason to challenge the Fund's decision to prepare the financial statements on a going concern basis.

Section 3: Fees, non audit services and independence

Fees, non audit services and independence

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 £
Fund audit	27,105	27,105
Total audit fees	**27,105**	**27,105**

Fees for other services

Service	Fees £
None	Nil

Independence and ethics

We confirm 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 we are independent and are able to express an objective opinion on the financial statements.

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

Section 4: Future developments

Developments relevant to your Pension Fund and the audit

Developments and other requirements

1. Financial reporting

There are no significant emerging issues affecting the Pension Fund expected for the year ending 31 March 2014 although PRAG has formed a working party to update the Pensions SORP. An updated version is expected later in 2014.

2. LGPS 2014

Planning for the impact of the implementation of the Career Average Re-valued Earnings scheme (CARE), effective from 1 April 2014.

3. Triennial valuation

Following the 31 March 2013 actuarial valuation the Council is in the process of considering the level of additional employer deficit contributions required and how to fund them.

4. Financial Pressures

Pension Funds are increasingly disinvesting from investment assets to fund cash flow demands on benefit and leaver payments that are not covered by contributions and investment income. Pension Fund investment strategies need to be able to respond to these demands as well as the changing nature of investment markets.

Our response

1. Financial reporting

We will carry out our usual substantive testing to ensure that the pension fund complies with the requirements of the CIPFA Code of Practice.

2. LGPS 2014

We will discuss the impact of the changes through our regular meetings with management.

Where appropriate, we will report any observations we have from our work and the implementation of new administration systems software to successfully process benefit payments under both the old and new schemes from 1 April 2014.

3. Triennial valuation

We will maintain regular dialogue with management to assess the impact this has on the administration of the Pension Fund and any required disclosures in the 2013/14 pension fund financial statements.

4. Other issues

We will monitor the changes being made to the Pension Fund investment strategy through our regular discussions with management.

We will consider the impact of changes on the nature of investments held by the pension fund and adjust our testing strategy as appropriate.

Section 5: Communication of audit matters

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Communication of audit matters to those charged with governance

International Standards on Auditing (ISA) 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 the Audit Commission (www.audit-commission.gov.uk).

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. 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 ('the Code') issued by the Audit Commission and includes nationally prescribed and locally determined work. Our work considers the Fund's key risks when reaching our conclusions under the Code.

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		✓
Compliance with laws and regulations		✓
Expected auditor's report		✓
Uncorrected misstatements		✓
Significant matters arising in connection with related parties		✓
Significant matters in relation to going concern		✓

Appendices

8

Appendix A: Audit opinion

We anticipate that we will provide the Fund with an unmodified audit report

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

Opinion on the pension fund financial statements

We have audited the pension fund financial statements of Surrey County Council for the year ended 31 March 2014 under the Audit Commission Act 1998. The pension fund financial statements comprise the Surrey Pension Fund Account, the Net Assets 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 2013/14.

This report is made solely to the members of Surrey County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010. 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 Chief Financial Officer and auditor

As explained more fully in the Statement of the Chief Financial Officer's Responsibilities, the Chief Financial Officer 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, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the 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 fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Chief Financial Officer; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the explanatory foreword and the annual report to identify material inconsistencies with the audited 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's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2014 and the amount and disposition of the fund's assets and liabilities as at 31 March 2014 and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 and applicable law.

Opinion on other matters

In our opinion, the information given in the explanatory foreword and the content of the Annual Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Darren Wells
Director
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

Grant Thornton
Fleming Way
Manor Royal
Crawley
RH10 9GT

July 2014

DRAFT

Page 143

Grant Thornton

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SURREY
COUNTY COUNCIL

Finance
G40, County Hall
Penrhyn Road
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Andy Mack
Grant Thornton UK LLP
Grant Thornton House
Melton Street
Euston Square
London
NW1 2EP

31 July 2014

Dear Sirs

Surrey County Council Pension Fund:
Financial Statements for the Year Ended 31 March 2014

This representation letter is provided in connection with your audit of the financial statements of the Surrey County Council Pension Fund (the Fund) for the year ended 31 March 2014 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 2014, and of the amount and disposition at that date of its assets and liabilities, other than liabilities to pay pensions and benefits after the end of the Fund year, in accordance with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 (the Code).

Financial Statements

1 We have fulfilled our responsibilities for the preparation of the financial statements in accordance with the Code; in particular, the financial statements show a true and fair view in accordance therewith, and for keeping records in respect of contributions received in respect of active members.

2 We acknowledge our responsibility for the design and implementation of internal control to prevent and detect error and fraud.

3 Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

4 Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of the Code.

5 All events subsequent to the date of the financial statements, and for which the Code requires adjustment or disclosure, have been adjusted or disclosed.

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6 The financial statements are free of material misstatements, including omissions.

7 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.

8 We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

9 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 judgment 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.

Information Provided

10 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 determine it necessary to obtain audit evidence.

11 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.

12 All transactions have been recorded in the accounting records and are reflected in the financial statements.

13 We are not aware of any 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.

14 We have no knowledge of any allegations of fraud, or suspected fraud, affecting the Fund's financial statements communicated by employees, former employees, analysts, regulators or others.

15 We are not aware of any instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

16 There have been no communications with The Pensions Regulator or other regulatory bodies during the fund year or subsequently concerning matters of non-compliance with any legal duty.

17 We are not aware of any reports having been made to The Pensions Regulator by any of our advisors.

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

19 We confirm that no member of the Surrey Pension Fund Board or the Audit and Governance Committee is connected with, or is an associate of, Grant Thornton UK LLP which would render Grant Thornton UK LLP ineligible to act as auditor to the Fund under section 27 of the Pensions Act 1995.

Other

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20 We confirm that the Fund is a Registered Pension Fund. We are not aware of any reason why the tax status of the Fund should change.

21 We confirm that we are not aware of any late contributions or breaches of the payment schedule that have arisen which we considered required reporting under the easement introduced under The Occupational Pension Funds (Miscellaneous Amendments) Regulations 2000.

22 We have not commissioned any advisory reports which may affect the conduct of your work in relation to the Fund's financial statements and payment schedule.

Yours faithfully

Sheila Little
Director of Finance and Administrator of Surrey Pension Fund

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

Opinion on the pension fund financial statements

We have audited the pension fund financial statements of Surrey County Council for the year ended 31 March 2014 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets 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 2013/14.

This report is made solely to the members of Surrey County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010. 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 the Director of Finance's 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, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the 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 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 financial statements. In addition, we read all the financial and non-financial information in the explanatory foreword to identify material inconsistencies with the audited 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.

8

Opinion on the pension fund financial statements

In our opinion the pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2014 and the amount and disposition of the fund's assets and liabilities as at 31 March 2014; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 and applicable law.

Opinion on other matters

In our opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

Darren Wells
Director
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

Grant Thornton House
Melton Street
Euston Square
London
NW1 2EP

4 August 2014

SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **PENSION FUND RISK REGISTER**

SUMMARY OF ISSUE:

Surrey County Council, as administering authority for the Surrey Pension Fund, is responsible for the delivery of benefit promises made to members of the Surrey Pension Fund. It achieves this by setting objectives and goals with varying timeframes. Risks lie in failing to meet the intended goals.

Risks that are established as an issue must be identified and evaluated via a risk register. The risks must be prioritised with existing controls or new controls implemented to mitigate the risks. This should be recorded in a risk register, which needs monitoring on a quarterly basis.

RECOMMENDATIONS:

It is recommended that:

1. Members assess the revised Risk Register in Annex 1, making any suggestions for amendment/additions as necessary.

REASON FOR RECOMMENDATIONS:

A solid framework of risk management is required in order to manage the considerable risk environment surrounding the governance and investment of the pension fund.

DETAILS:

Background

1 A review of the current risk register for the Pension Fund will give the Pension Fund Board the opportunity to influence and drive the Pension Fund risk management process for 2014-2015.

Risk Management Process

2 The risk management policy of the Surrey Pension Fund is to adopt best practice in the identification, evaluation and control of risks in order to ensure that the risks are recognised, and then either eliminated or reduced to a manageable level. If neither of these options is possible, then means to mitigate the implications of the risks should be established.

3 The Pension Fund & Treasury Manager has identified a number of risks associated with the Pension Fund. The risks are grouped as follows:

- Investment
- Financial
- Funding
- Operational
- Governance

4 Each of the risk areas has been assessed in terms of its impact on the Fund as a whole, on the fund employers, and on the reputation of the Pension Board and Surrey County Council as the administering authority. Assessment has also been given as to the likelihood of the risk.

5 Each of the three areas of impact identified above is assessed on a scale of one to four, with four implying the highest level of impact. The likelihood of the risk description (between one and five) is then applied to the combined impact score, which produces an overall risk score. Depending on the score, the risks are then identified as Red, Amber or Green.

9

6 To comply with best practice, a scoring process has been implemented, which will reassess the risk scores after the mitigating action taken to control and reduce the risks. The risk register includes a revised impact score and net risk score as a result of those mitigating actions.

7 Within the residual red risks, cost ranges are provided on the implications where possible.

Review

8 Board members requested an overhaul of the risk register at its meeting on 15 May 2014. The revised, streamlined register is shown in Annex 1. The register will continue to be reviewed on a quarterly basis.

CONSULTATION:

9 The Chairman of the Pension Fund Board has been consulted and has offered full support for the quarterly scrutiny process.

RISK MANAGEMENT AND IMPLICATIONS:

10 The risk related issues are contained within the report's Annex 1.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

11 There are no expected additional costs from compiling, maintaining and monitoring a risk register.

DIRECTOR OF FINANCE COMMENTARY

12 The Director of Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed and that the risk register will provide officers with a suitable platform for the monitoring and control of pension fund risks.

LEGAL IMPLICATIONS – MONITORING OFFICER

13 There are no legal implications or legislative requirements associated with this report.

EQUALITIES AND DIVERSITY

14 The creation of a risk register will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

15 There are no potential implications for council priorities and policy areas. 9

WHAT HAPPENS NEXT

16 The following next steps are planned:

- Monitoring by officers and reporting to the Board every quarter.

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board members.

Annexes:
List the annexes attached to this report.
Annex 1: Pension Fund Risk Register

Sources/background papers:
None

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ANNEX 1

Risk Group	Risk Ref.	Previous	Risk Description	Impact				Likelihood	Total risk score	Mitigation actions	Revised Likelihood	Net risk score
				Fund	Employers	Reputation	Total					
Funding	1	1	Bond yields fall leading to a increase in value of liabilities: a 0.1% reduction in the discount rate will increase the liability valuation by 2%	4	4	4	12	4	48	TREAT-1) IAS19 data is received annually and provides an early warning of any potential problems. 2) Early consultation with the actuary will take place with regard to the 2013 valuation. 3) Training on hedging this future cost provided to the Pension Fund Board. Curent investment strategy review will address liability protection.	4	48
Funding	2	2	Pay & price inflation is significantly more or less than anticipated: an increase in CPI inflation by 0.1% will increase the liability valuation by 1.4%	4	4	4	12	4	48	TREAT- 1) Fund employers should monitor own experience. 2) Assumptions made on pay and price inflation (for the purposes of IAS19/FRS17 and actuarial valuations) should be long term assumptions. 3) The fund holds investment in index linked bonds to mitigate some of the risk. 4) Training on hedging this future cost provided to the Pension Fund Board. Current investment strategy review will address liability protection.	4	48
Funding	3	3	Pensioners living longer: adding one year to life expectancy will increase the future service rate by 0.8%	4	4	1	9	5	45	TREAT- 1) Hymans Robertson use long term longevity projections in the actuarial valuation process. 2) SCC has joined Club Vita, which looks at mortality rates that are employer specific.	5	45
Funding	4	4	Mismatching of assets and liabilities, inappropriate long-term asset allocation or investment strategy, mistiming of investment strategy	4	3	3	10	4	40	TREAT- 1) Active investment strategy and asset allocation monitoring from Board, officers and consultants. 2) 2014/15 Investment strategy review is underway. 3) Separate source of advice from Fund's independent advisor. 4) Setting of Fund specfic benchmark relevant to the current position of fund liabilities. 5) Fund manager targets set and based on market benchmarks or absolute return measures.	3	30
Operational	5	7	Rise in ill health retirements impact employer organisations	1	4	1	6	4	24	TREAT- 1) Insuring against the cost and impact (approved at 14/02/14 meeting but not yet implemented).	4	24
Governance	6	8	Changes to LGPS regulations	4	3	1	8	4	32	TREAT-1) Fundamental change to LGPS regulations to be implemented from 1 April 2014. 2) Impact on contributions and cashflows will need to be considered during the 2013 valuation process. 3) Fund will respond to consultations.	3	24
Investment	7	9	Investment Managers fail to achieve performance targets over the longer term: a shortfall of 0.1% on the investment target will result in an annual impact of £2.6m	4	4	4	12	3	36	TREAT- 1) The Investment Management Agreements clearly state SCC's expectations in terms of performance targets. 2) Investment manager performance is reviewed on a quarterly basis. 3) The Pension Fund Board should be positioned to move quickly if it is felt that targets will not be met. 4) Having LGIM as a rebalancing/transition manager facilitates quick changes. 5) The Fund's investment management structure is highly diversified, which lessens the impact of manager risk compared with less diversified structures.	2	24
Financial	8	10	Financial loss of cash investments from fraudulent activity	4	4	4	12	3	36	TOLERATE - 1) Policies & procedures are in place which are regularly reviewed to ensure risk of investment loss is minimised. Governance arrangements are in place in respect of the Pension Fund. External advisors assist in the development of the Investment Strategy. Fund Managers have to provide SAS 70 or similar (statement of internal controls).	2	24
Operational	9	11	Financial failure of a fund manager leads to increase costs and service impairment	4	3	4	11	3	33	TREAT- 1) Fund is reliant upon current adequate contract management activity. 2) Fund is reliant upon alternative suppliers at similar price being found promptly. 3) Fund is reliant on LGIM as transition manager.	2	22
Funding	10	12	Impact of government policy on the employer workforce	3	3	1	7	4	28	TREAT- 1) Hymans Robertson use prudent assumptions on future of workforce. Employers to flag up potential for major bulk transfers. The potential for a significant reduction in the workforce as a result of the pressures that the public sector is under may have an additional impact on the Fund. 2) Need to make worst case assumptions about diminishing workforce when carrying out the actuarial valuation.	3	21
Investment	11	13	Investment markets fail to perform in line with expectations leading to deterioration in funding levels and increased contribution requirements from employers	4	3	3	10	3	30	TREAT- 1) Proportion of asset allocation made up of equities, bonds, property funds, diversified growth funds and private equity, limiting exposure to one asset category. 2) The investment strategy is continously monitored and periodically reviewed to ensure optimal asset allocation. 3) Actuarial valuation and asset/liability study take place automatically every three years. 4) IAS19 data is received annually and provides an early warning of any potential problems. 5) The actuarial assumption regarding asset outperformance of 1.6% over gilts is regarded as achievable over the long term when compared with historical data.	2	20
Funding	12	5	Impact of increases to employer contributions following the actuarial valuation	3	3	3	9	3	27	TREAT- 1) Officers to consult and engage with employer organisations in conjunction with the actuary. 2) Actuary will assist where appropriate with stabilisation and phasing in processes.	2	18
Governance	13	14	Failure to take difficult decisions inhibits effective Fund management	3	2	4	9	3	27	TREAT-1) Ensure activity analysis encourages decision making on objective empirical evidence rather than emotion. Ensure that basis of decision making is grounded in ALM Study/SIP/FSS/Governance statement and that appropriate advice is sought.	2	18
Funding	14	6	Structural changes in an employer's membership or an employer fully/partially closing the scheme. Employer bodies transferring out of the pension fund or employer bodies closing to new membership. An employer ceases to exist with insufficient funding or adequacy of bond	4	3	1	8	3	24	TREAT- 1) Administering Authority actively monitors prospective changes in membership. 2) Maintain knowledge of employer future plans. 3) Contributions rates and deficit recovery periods set to reflect the strength of the employer covenant. 4) The terms of admission agreements/bonds provide for regular review of bond adequacy. 5) The Fund considers seeking a guarantor for new admitted bodies.	2	16
Operational	15	16	Poor data quality results in poor information and decision making	2	2	4	8	3	24	TOLERATE 1) Northern Trust provides 3rd party validation of performance and valuation data. 2) Pension Fund team and pension board members are able to intergrate data to ensure accuracy.	2	16
Operational	16	17	Insufficient attention to environmental, social and governance (ESG) leads to reputational damage	1	1	3	5	4	20	TREAT-1) Review SIP in relation to published best practice (e.g. Stewardship Code) 2) Ensure fund managers are encouraged to engage and to follow the requirements of the published SIP. 3) The Fund is a member of the Local Authority Pension Fund Forum (LAPFF), which raises awareness of ESG issues and facilitates engagement with fund managers. 4) The Fund has approved a Stewardship Code and a share voting policy which provides specific guidance in the voting of company resolutions.	3	15
Governance	17	New entry	Implementation of proposed changes to the LGPS does not conform to plan or cannot be achieved within time scales	1	2	4	7	3	21	TREAT- 1) Officers consult and engage with DCLG, LGPS Advisory Board, consultants, peers, seeminars, conferences. 2) Officers engage in early planning for implemntation against agreed deadlines.	2	14
Operational	18	18	Concentration of knowledge in small number of officers and risk of departure of key staff	2	3	2	7	3	21	TREAT-1) 'How to' notes in place. 2) Development of team members & succession planning needs to be improved. 3) Officers and members of the Pension Fund Board will be mindful of the proposed CIPFA Knowledge and Skills Framework when setting objectives and establishing training needs.	2	14
Governance	19	19	Change in membership of Pension Fund Board leads to dilution of member knowledge and understanding	4	1	1	6	4	24	TREAT- 1) Succession planning process to be implemented. 2) Ongoing training of Pension Fund Board members. 3) Pension Fund Board new member induction programme. 4) Training to be based on the requirements of CIPFA Knowledge and Skills Framework and the results of the test undertaken in 2012. New Board members to take the test.	2	12
Operational	20	20	Inaccurate information in public domain leads to damage to reputation and loss of confidence	1	1	4	6	3	18	TOLERATE- 1) Ensure that all requests for information (Freedom of Information, Member & Public questions at Council, etc) are managed appropriately and that Part 2 items remain so. 2) Maintain constructive relationships with employing bodies to ensure that news is well managed.	2	12
Operational	21	21	Financial failure of third party supplier results in service impairment and financial loss	2	2	2	6	3	18	TOLERATE-1) Performance of third parties (other than fund managers) monitored. 2) Review of Northern Trust took place in January 2009, ahead of decision on whether to retain (Jan 2009) - a fee reduction was secured in 2011). 3) Actuarial and investment consultancies are provided by two different providers.	2	12
Operational	22	22	Procurement processes may be challenged if seen to be non-compliant with OJEU rules. Poor specifications lead to dispute. Unsuccessful fund managers may seek compensation following non compliant process	1	1	4	6	3	18	TOLERATE - Ensure that assessment criteria remains robust and that full feedback is given at all stages of the procurement process.	2	12
Governance	23	23	Failure to comply with legislative requirements e.g. SIP, FSS, Governance Policy, Freedom of Information requests	4	1	4	9	2	18	TOLERATE -1) Publication of all documents on external website. 2) Managers expected to comply with SIP and IMA. 3) Pension Board self-assessment to ensure awareness of all relevant documents. 4) Annual audit review.	1	9
Financial	24	15	Counterparty risk within the SCC treasury management operation	2	2	2	6	2	12	TOLERATE - 1) A separate bank account exists for the pension fund 2) Lending limits with approved banks are set at prudent levels 3) The pension fund treasury management strategy is based on that of SCC.	1	6
Financial	25	25	Incorrect, failed or late employee/employer contributions payments received	1	4	1	6	2	12	TOLERATE- 1) Monthly monitoring of pensions contributions against expectation. 2) Reminders sent to employers when they fail to meet payment deadline. 3) Scope to report persistent late payment to OPRA.	1	6
Financial	26	24	Inaccurate cash flow forecasts or drawdown payments lead to shortfalls on cash levels and borrowing becomes necessary to ensure that funds are available	2	1	1	4	2	8	TOLERATE- 1) Borrowing limits with banks are set at levels that are more than adequate should cash be required at short notice. 2) Cashflow analysis of pension fund undertaken at regular intervals.	1	4

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SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **REVISED STATEMENT OF INVESTMENT PRINCIPLES**

SUMMARY OF ISSUE:

With adjustments to asset allocation within the Pension Fund, it is necessary to approve a revised Statement of Investment Principles (SIP).

RECOMMENDATIONS:

It is recommended that the Pension Fund Board:

1 Approve the revised Statement of Investment Principles shown in Annex 1.

REASON FOR RECOMMENDATIONS:

The Pension Fund Board must approve all working documents produced for the Pension Fund.

DETAILS:

Background

1 In accordance with Regulation 12 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, as an administering authority, the Council must prepare and maintain a written statement of the principles governing its decisions on the investment of the pension fund. It also has to review the policy from time to time and revise it if considered necessary following such a review, as is recommended here in the light of changes made to the Fund's portfolio.

Revised Statement

2 The revised Statement of Investment Principles (SIP) is shown as Annex 1. There are changes to specific investment parameters, following the allocation of additional monies to diversified growth funds, namely the Global Focused Strategies (GFS) Fund run by Standard Life.

3 Given the slight increase to diversified growth funds (funded by the overweight equities allocation), balancing pro rata adjustments have been made to the portfolio's fixed income and property allocations.

Monitoring and Review

4 The SIP is kept under constant review and will be submitted for approval to future Board meetings when any revision is required.

CONSULTATION:

5 The Chairman of the Pension Fund has been consulted on the revised draft and has offered full support for the proposals.

RISK MANAGEMENT AND IMPLICATIONS:

6 There are no risk related issues contained within the report's proposals.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

7 There are no financial and value for money implications.

DIRECTOR OF FINANCE COMMENTARY

8 The Director of Finance is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed and that the proposed SIP offers a clear structure, reflecting the current investment strategies approved by the Pension Fund Board.

LEGAL IMPLICATIONS – MONITORING OFFICER

9 There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

10 The approval of the SIP will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

11 There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

12 The following next steps are planned:

- Adoption of the revised SIP
- SIP is kept under review

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman

Annexes:
Revised Statement of Investment Principles

Sources/background papers:
None

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Statement of Investment Principles 2014/15

Statement of Investment Principles

1. Overall Responsibility

The County Council is the designated statutory body responsible for administering the Surrey Pension Fund on behalf of the constituent Scheduled and Admitted Bodies. The Council is responsible for setting investment policy, appointing suitable persons to implement that policy and carrying out regular reviews and monitoring of investments. The content of this Statement reflects the County Council's compliance with the requirements of the Myners Review of Institutional Investment, which can be found at Annex 2. 10

The Local Government Pension Scheme (England and Wales) (Amendment) (No 2) Regulations 2005 came into effect on 14 December 2005. The Regulations provide the statutory framework within which LGPS administering authorities are required to publish a governance policy statement.

A copy of the Surrey Pension Fund's current governance policy statement can be found on the County Council's website. **www.surreypensionfund.org**

Investment policy and associated monitoring and review are delegated to the Surrey Pension Fund Board, which is made up of:

- six nominated members of the County Council;
- two representatives from the Borough/District Councils nominated by the Surrey Local Government Association;
- one representative from the external employers;
- one representative of the members of the Fund.

The Pension Fund Board is advised by a representative of the Fund's professional investment advisor, an independent advisor, the Chief Finance Officer and the Strategic Finance Manager (Pension Fund and Treasury).

The Pension Fund Board meets on a quarterly basis.

2. Investment Objectives

The Pension Fund Board seeks to ensure that the Pension Fund has sufficient assets to be able to meets its long term obligations to pay pensions to the Fund's members, i.e., over the long term to be at or above a 100% funding level. It also has an objective to maintain employer contribution rates as reasonably stable and affordable as possible. In order to meet these objectives, a number of secondary objectives have been agreed:

i) To have a clearly articulated strategy for achieving and maintaining a fully funded position over a suitable long term time horizon; the Board recognises that funding levels can be volatile from year to year depending as they do both on investment market levels and on estimates of liability values, so the long-term strategy needs to be capable of steering a steady course through changing market environments.

ii) To have a strategic asset allocation that is both well diversified and expected to provide long term investment returns in excess of the anticipated rise in the Fund's liabilities.

iii) To appoint managers that the Board believes can consistently achieve the performance objectives set and to give each appointed manager a clearly defined benchmark and performance objective against which they can be judged.

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iv) To ensure investment risk is monitored regularly both in absolute terms (the risk of losing money) and relative to the Fund's liabilities (the risk of funding shortfalls); the Board will have regard to best practice in managing risk.

v) To have sufficient liquid resources available to meet the Fund's ongoing obligations.

vi) To achieve an overall Fund return 1% per annum in excess of the overall benchmark over rolling three-year periods.

3. Investment Style and Management

The Board has delegated day-to-day management of various parts of the Fund to external fund managers each of which has been given an explicit benchmark and performance objective. The Board retains responsibility for ensuring the mix of managers and by implication the overall asset allocation is suitable for the long-term objectives defined above.

The Board has appointed two different types of manager: 'Index Relative' who seek to achieve a return relative to a market index within a specified asset type and 'Absolute Return' who seek to achieve a desired return outcome by moving between different asset types.

Index Relative managers

The managers in this category have been set differing performance targets and will take accordingly differing levels of risk relative to the benchmark index they are given.

Passive mandates seek to replicate the market index as closely as possible and are expected to take very little relative risk. Typically, such portfolios will have the largest number of individual holdings each of which will be close to the index weighting. The expected performance should be within 0.5% of the index return in any year.

Core active mandates seek to achieve a performance between 0.75% per annum and 2% per annum ahead of the relevant market index. Typically, core active mandates have diversified portfolios and take medium levels of relative risk. Most managers will only be appointed to manage a single asset class (for example, global equities, bonds or property).

Concentrated active mandates seek to outperform their relevant index by 3% per annum or more and take larger relative risks by owning a smaller number of individual holdings. The Pension Fund Board usually confines such mandates to specialist managers in regional equities.

Absolute Return managers

The managers in this category are all expected to achieve returns well ahead of cash or inflation in the long-term.

Diversified Growth managers use a very broad range of asset classes and actively vary allocations between asset types depending on investment market conditions. They will also use derivatives from time to time to limit the scope for large falls in value. The expected returns from such mandates will be close to the long term return from equity markets but with much less volatility. 10

Absolute return managers also seek to achieve good long term returns with dampened down volatility, but typically they are focused on a particular investment area. The desired outcome is similar to Diversified Growth mandates but with possibly greater variability across mandate types and usually with a much smaller amount invested in each capability.

Fees

The level of fees paid to managers varies greatly according to the complexity of the mandate and the geographic area involved. Fees are usually expressed as a proportion of assets under management. There may also be additional performance related fee charges.

Fees for passive mandates tend to be very low, particularly in developed markets where information is readily available. Fees are higher for mandates that require greater manager skill. Typically a concentrated active mandate will have a higher fee rate than a core active manager and a small absolute return mandate will have a higher fee rate than a larger diversified growth mandate.

Current Manager Structure

The table below shows the current asset allocation and manager structure of the Fund.

10

	Category	Allocation Policy %	Fund %	Control Range% +/-
Equities			**63.0**	**+/-3.0**
UK			29.0	
Legal and General	*Passive*	*10.0*		
Majedie	*Concentrated Active*	*7.0*		
Mirabaud	*Concentrated Active*	*4.0*		
UBS	*Core Active*	*8.0*		
Overseas			34.0	
Legal and General	*Passive*	*14.0*		
Marathon	*Concentrated Active*	*12.0*		
Newton	*Core Active*	*8.0*		
Property			**6.5**	**+/-3.0**
CBRE	*Core Active*	6.5		
Alternatives			***12.0***	**+/-3.0**
Standard Life	*Diversified growth*	*8.0*		
Baillie Gifford	*Diversified growth*	*4.0*		
Bonds			**18.5**	**+/-3.0**
Fixed interest gilts			4.85	
Legal and General	*Passive*	*2.1*		
Western	*Core Active*	*2.75*		
Index linked gilts			3.7	
Legal and General	*Passive*	*3.7*		
Corporate bonds			7.4	
Legal and General	*Passive*	*1.9*		
Western	*Core Active*	*5.5*		
Total Return			*2.55*	
Franklin Templeton	*Unconstrained*	*2.55*		
Total			**100.0**	

The Fund also has a commitment to invest up to 5% of the fund in private equity. This allocation is achieved by investing both in fund of funds and direct funds, managed by a number of private equity specialists. The investments are funded through cash flow. The Pension Fund Board reviews the private equity strategy on an annual basis and makes commitments in order to achieve the target commitment level of 5% of the Fund.

Fees paid to managers vary due to the levels of risk taken and the geographic areas in which the manager is invested. Fees are generally expressed as a proportion of assets under management. Performance fees are in place for a number of the Fund's managers. The following table shows the Fund's private equity investments as at 31 March 2013.

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Name	Currency	Inception	Commitment
UK Funds			**£/€/$m**
HG Capital MUST 3	£	2001	2.0
HG Capital MUST 4	£	2002	3.0
HG Capital 5	£	2006	10.0
HG Capital 6	£	2009	10.0
HG Capital 7	£	2013	15.0
ISIS II	£	1999-2002	12.0
ISIS III	£	2003	14.0
ISIS IV	£	2007	15.0
ISIS Growth Fund	£	2013	10.0
Darwin Property Fund	£	2013	20.0
Euro Fund of Funds			
Standard Life ESP II	€	2004	10.0
Standard Life ESP 2006	€	2006	15.0
Standard Life ESP 2008	€	2008	15.0
Standard Life ESF	€	2011	17.5
Standard Life SOF I	$	2013	20.0
Standard Life SOF II	$	2014	20.0
US Fund of Funds			
Blackrock Div PEP I	$	2001	5.0
Blackrock Div PEP II	$	2003	5.0
Blackrock Div EP III	$	2005	17.5
GSAM PEP 2000	$	2000	10.0
GSAM PEP 2004	$	2004	10.0
GSAM PEP 2005	$	2006	17.0
GSAM PEP X	$	2008	18.0
GSAM PEP XI	$	2011	18.0
GSAM Vintage Fund VI	$	2013	20.0
US Funds			
Capital Dynamics US Solar Fund	$	2011	25.0
Capital Dynamics Energy/Infra	$	2013	25.0

4. Policy on Kinds of Investment

The Pension Fund Board, having regard to funding levels, cash needs and risk tolerance, determines the overall Fund asset mix. The following table shows the strategic asset allocation benchmark for both the managed Fund (i.e. excluding private equity) and the total fund:

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	Target Allocation exc. Private Equity	Target Allocation inc. Private Equity
Bonds	%	
Gilts	4.85	4.6
Corporate Bonds	7.4	7.1
Index-Linked gilts	3.7	3.5
Unconstrained	2.55	2.4
Property	6.5	6.2
Total Bonds/Property	25.0	23.8
UK Equity	29.0	27.5
Overseas Equity	34.0	32.3
Global	30.0	28.5
Emerging markets	4.0	3.8
Total Equity	63.0	59.8
Diversified Growth	12.0	11.4
Private Equity	n/a	5.0
TOTAL	100.0	100.0

Acceptable asset classes are:

- UK Equities
- UK Fixed Interest
- UK Index Linked Gilts
- UK Property through pooled funds
- Overseas Equities, major classes being:
  - North America
  - Europe
  - Pacific Rim including Japan
  - Emerging Markets
- Global Bonds
- Overseas Index Linked Stocks
- Unquoted Equities via Pooled Funds
- Emerging Market Equities via Pooled Funds, unless specifically authorised
- Direct investment in private equity funds or fund of funds

The use of derivatives and other financial instruments is permitted within pre-agreed limits for specific purposes such as asset allocation switches and currency hedging. Underwriting is permitted provided that the underlying stock is suitable on investment grounds and complies with existing investment criteria.

Stock lending is permitted. The Pension Fund Board approved Northern Trust's appointment to operate the Pension Fund's lending programme in order to generate an additional income stream for the Pension Fund within approved risk parameters.

There are statutory limits on the proportion of the Fund that can be invested in certain types of investment as determined by the Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2013. 10

5. Investment Performance Targets and Benchmarks

Manager	Portfolio	Benchmark Index	Performance Target
UBS	UK Equities	FTSE All Share	+2.0% p.a. (gross of fees) over rolling 3-year periods
Mirabaud	UK Equities	FTSE All Share	+2.5% p.a. (gross of fees) over rolling 3-year periods
Marathon	Global Equities	MSCI AC World	+2.0% p.a. (gross of fees) over rolling 3-year periods
Majedie	UK Equities – Long Only UK Equities – Directional Long/Short	FTSE All Share FTSE All Share	+2.5% p.a. (gross of fees) over rolling 3-year periods Absolute return focused, but aims to out-perform the FTSE All Share Index by an unspecified amount over the long term
Newton	Global Equities	MSCI AC World	+2.0% p.a. (gross of fees) over rolling 3-year periods
Western	Fixed Income	70.0%: Markit i Boxx £ Non-Gilts ex-BBB All Stocks 30.0%: FTSE A UK Gilts – All Stocks	+0.75% p.a. (gross of fees) ove rolling 3-year periods
Franklin Templeton	Unconstrained Global Fixed Income	Barclays Multiverse Index	+4% to 7% p.a. (gross of fees) over rolling 3-year periods
LGIM	Multi-Asset Equities and Bonds N - UK Equity Index RX - World (ex UK) Dev Equity Index HN – World Emerging Markets Equity Index AA - All Stocks Gilts Index	 FTSE All Share FTSE AW – Dev'd World (ex UK) FTSW AW – All Emerging FTSE A UK Gilts All Stocks	To track the performance of the respective indices within a lower level of tracking deviation (gross of fees) over rolling 3-year periods

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	CN - AAA-AA-A Bonds - All Stocks Index Y - All Stocks Index-Linked Gilts	Markit iBoxx GBP Non Gilts ex BBB All stock FTSE A Index-Linked All Stocks	
CBRE	Property	IPD UK All Balanced Funds	+0.5% p.a. (gross of fees) over rolling 3-year periods
Baillie Gifford	Diversified Growth	UK Base Rate	+3.5% p.a. (net of fees) over rolling 5-year periods
Standard Life	Diversified Growth GARS	6 month LIBOR	+5.0% p.a. (gross of fees) over rolling 5-year periods
Standard Life	Diversified Growth GFS	6 month LIBOR	+7.5% p.a. (gross of fees) over rolling 3-year periods
Internal	Private Equity	MSCI World Index	+5% p.a. (net of fees) over the life of the contract
Internal	Cash	LIBID 7-day rate	LIBID 7 day rate

The overriding aim is to run the Pension Fund in accordance within the relevant legislation and subject to the following performance target: “to outperform the Surrey benchmark by 1% per annum over rolling 3-year periods, with a maximum underperformance of -2% in any one year.”

The overall Surrey benchmark is shown below in detail.

Type of funds	Level of Risk	Target Return Out-Performance p.a.
Passive (index-tracker)	Low	0 – 0.5%
Core Active	Medium	0.75% - 2.0%
Concentrated Active	High	2.0 - 2.5%
Diversified growth	Medium	3.5% - 5%
Unconstrained	Medium	4% - 7%
Total	Medium	1%

The performance target for the private equity Funds is to outperform returns on quoted UK Equities (FTSE All Share Index) by 2% per annum.

6 Risk Measurement and Management

There are a number of risks to which any investment is exposed. The Pension Fund Board recognises that, whilst increasing risk increases potential returns over a long period, it also increases the risk of a shortfall in returns relative to that required to cover the Fund’s liabilities as well as producing more short term volatility in the funding position.

In addition to targeting an appropriate overall level of investment risk, the Pension Fund Board seeks to spread risks across a range of different sources, believing that diversification limits the impact of any single risk. The Pension Fund Board aims to take on those risks for which a reward, in the form of excess returns, is expected over time.

The following risks are recognised and considered by the Pension Fund Board:

Mismatch risk: the primary risk upon which the Pension Fund Board focuses is the arising of a mismatch between the Fund's assets and its liabilities.

Sponsor Covenant risk: the financial capacity and willingness of the sponsoring employers to support the Fund is a key consideration of the Pension Fund Board and is reviewed on a regular basis.

Diversification risk: the Pension Fund Board recognises the risks that may arise from the lack of diversification of investments. Subject to managing the risk from a mismatch of assets and liabilities, the Pension Fund Board aims to ensure that the asset allocation policy results in an adequately diversified portfolio. 10

Concentration risk: the Pension Fund Board is also aware of concentration risk which arises, for example, when a high proportion of the Fund's assets are invested in securities, whether debt or equity, of the same or related issuers or in the same or similar industry sectors. The overall investment arrangements are intended to provide an appropriate spread of assets by type and spread of individual securities within each asset class.

Liquidity risk: the Pension Fund Board recognises that there is liquidity risk in holding assets that are not readily marketable and realisable. Given the long term investment horizon, the Pension Fund Board believes that a degree of liquidity risk is acceptable, given the potential return. The majority of the Fund's assets are realisable at short notice.

Manager risk: the Fund's assets are invested with a number of managers to provide appropriate diversification.

Regulatory and political risk: across all of the Fund's investments, there is the potential for adverse regulatory or political change. Regulatory risk arises from investing in a market environment where the regulatory regime may change. This may be compounded by political risk in those environments subject to unstable regimes. The Pension Fund Board will attempt to invest in a manner which seeks to minimise the impact of any such regulatory or political change should such a change occur.

Exchange rate risk: this risk arises from unhedged investment overseas. The Fund has a currency hedging policy in place: 50% of its exposure to the US dollar, Euro and Yen.

The documents governing the appointment of each investment manager include a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the Fund. The Investment Managers are prevented from investing in asset classes outside their mandate without the Pension Fund Board's prior consent.

Arrangements are in place to monitor the Fund's investments to help the Pension Fund Board check that nothing has occurred that would bring into question the continuing suitability of the current investments. To facilitate this, the Pension Fund Board meets with the Investment Managers from time to time, and receives regular reviews from the Investment Managers and its investment advisors.

The safe custody of the Fund's assets is delegated to professional custodians (either directly or via the use of pooled vehicles).

10 Should there be a material change in the Fund's circumstances, the Pension Fund Board will review whether and to what extent the investment arrangements should be altered; in particular whether the current risk exposure remains appropriate.

7 Policy on Balance Between Different Kinds of Investment

The Council has set target asset allocation ranges for each kind of investment within the overall benchmark. Fund Managers are required to report quarterly their current country, sector or asset allocation positions, whichever is relevant, against their strategy, and to seek approval for variations to their strategies.

8 Policy on Realisation of Investments

Fund Managers are required to maintain portfolios that consist of assets that are readily realisable. Any investment within an in-house or pooled fund, which is not readily tradable, requires specific approval.

9 Monitoring and Review

The target funding level is set triennially, consequent upon the actuarial review. The statutory requirement is to move towards 100% funding over a period of time, agreed with the Fund Actuary as the average expected future working lifetime of the scheme membership (20 years).

Investment strategy will be reviewed annually, with a major review taking place no later than every five years. The SIP will also be reviewed annually. A review of investment management arrangements is carried out at least every three years.

Investment management performance is reviewed annually upon receipt of the third party performance information. The individual manager's current activity and transactions are presented quarterly in discussion with the Pension Fund Board.

An Annual Meeting is held in November each year and is open to all Fund employers.

10 Stewardship and Responsible Investment

The Council wishes to have an active influence on issues of environmental, social or governance (ESG) concern with companies in which the Pension Fund is a shareholder. It will seek to codify its approach with Fund Managers and will use the services of specialist agencies as necessary to identify issues of concern. The Council requires the Fund Managers to take into account the implications of substantial “extra-financial” considerations, e.g., ESG or reputational issues that could bring a particular investment decision into the public arena.
Whilst the Fund has no specific policy on investing or divesting in stock with regard to ESG issues, in comparing potential investment decisions, and where differences in predicted returns are deemed immaterial, external fund managers could deploy ESG considerations in deciding upon selection. 10

The Pension Fund also holds expectations of its fund managers to hold companies to account on the highest standards of behaviour and reputational risk management which may damage long term performance, and for those issues to be part of their stock selection criteria.

The Fund wishes to be an active shareholder and exercise its voting rights to promote and support good corporate governance principles. Share voting is undertaken in-house, after consultation with fund managers, and consultation with the Pension Fund Board on potentially contentious issues. A quarterly report will be posted to the Fund website.

The Fund is a member of the Local Authority Pension Fund Forum (LAPFF), a membership group of LGPS funds that campaigns on corporate governance issues, thus demonstrating a commitment to sustainable investment and the promotion of high standards of corporate governance and responsibility.

11 Custody

Managers are required to hold cash and stocks in an account managed by Northern Trust, the Fund’s independent global custodian, or by agreement otherwise as appropriate. The Pension Fund aims to hold only a minimum working cash balance. A separate bank account is in place to hold any excess funds held by the administering authority for the purpose of day-to-day cash management of the pension fund.

12 Administration

Funds officers prepare a quarterly report to the Pension Fund Board, preparing the audited annual report and financial statements in line with statutory deadlines, and maintain an up to date record of cash balances at Surrey to ensure surplus cash is invested promptly and resources are available to meet the benefit outflow as it arises.

Annex 1

Myners Investment Principles – Compliance Statement

Principle 1: Effective Decision-making

Administering authorities should ensure that:

- decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to make them effectively and monitor their implementation; and

- those persons or organisations have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.

10 ✓ **Full compliance**
The Pension Fund Board is supported in its decision making role by the Chief Finance Officer and the Pension Fund and Treasury Manager.

Members of the Pension Fund Board participate in regular training delivered through a formal programme. Training is provided at every quarterly meeting.

Principle 2: Clear Objectives

An overall investment objective should be set out for the fund that takes account of the scheme's liabilities, the potential impact on local taxpayers, the strength of the covenant for non-local authority employers, and the attitude to risk of both the administering authority and scheme employers, and these should be clearly communicated to advisors and investment managers.

✓ **Full compliance**
The Fund's overall objectives are defined in the Funding Strategy Statement and are directly linked to the triennial actuarial valuation. The investment objectives are clearly stated in the Statement of Investment Principles.

The content of the Funding Strategy Statement reflects discussions held with individual scheme employers during the actuarial valuation process. Employers understand that contribution rates are set, having given consideration to the key tenets of affordability, sustainability and stability but also with the understanding that any decisions made must be prudent. To this end, the strength of the employer covenant is considered when setting contribution rates.

Principle 3: Risk and liabilities

In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities. These include the implications for the local taxpayers, the strength of the covenant for participating employers, the risk of their default and longevity risk.

✓ **Full compliance**

The Fund's actuary reviews the funding position of each employer every three years and this valuation includes an assessment of the gap between the employer's share of the Fund assets and the liabilities specific to each employer. The strength of the employer covenant is considered when setting contribution rates.

The Fund's investment strategy is reviewed following each triennial valuation to ensure that the investment strategy will achieve the expected returns assumed during the valuation process.

As a member of Club Vita, a bespoke set of assumptions are specifically tailored to fit the membership profile of the Surrey Fund. The assumptions selected are intended to make an appropriate allowance for future improvements in longevity, based on the actual experience of the Fund.

Principle 4: Performance assessment

Arrangements should be in place for the formal measurement of performance of the investments, investment managers and advisors.

Administering authorities should also periodically make a formal assessment of their own effectiveness as a decision-making body and report on this to scheme members.

✓ **Full compliance**

Each manager's performance is measured quarterly against benchmark targets, which are specified in the contract between the Fund and the manager. The Fund's global custodian produces performance data for each manager and for the Fund as a whole. The target outperformance for the Fund as a whole is specified within the Statement of Investment Principles. The Fund performance is also assessed with reference to the local authority peer group.

Performance data is reported to Pension Fund Board on a quarterly basis. Fund managers present to the officers or the Pension Fund Board on at least an annual basis and officers hold four additional meetings with managers per quarter to discuss the portfolio composition, strategy and performance.

Consideration has been given to quantitative measures to assess the performance of the Pension Fund Board, although options other than measuring meeting attendance and the success of the Board's implemented strategies are limited.

Principle 5: Responsible ownership

Administering authorities should:

- Adopt, or ensure their investment managers adopt, the Stewardship Code.
- Include a statement of their policy on responsible ownership in the statement of investment principles.
- Report periodically to scheme members on the discharge of such responsibilities.

✓ **Full compliance**

All new investment mandates will be expected to include a statement of a manager's adoption of the Stewardship Code.

The Council wishes to have an active influence on issues of environmental or ethical concern with companies in which the Pension Fund is a shareholder. It will seek to codify its approach with Fund Managers and will use the services of specialist agencies as necessary to identify issues of concern. The Council requires the Fund Managers to take into account the implications of substantial "extra-financial" considerations, e.g., environmental, social or reputational issues that could bring a particular investment decision into the public arena.

The Fund wishes to be an active shareholder and exercise its voting rights to promote and support good corporate governance principles. In addition, the Fund is a member of the Local Authority Pension Fund Forum (LAPFF), thus demonstrating a commitment to sustainable investment and the promotion of high standards of corporate governance and responsibility.

All of the Fund's managers are signed up to the Stewardship Code, which provides a framework for investors to consider environmental, social and corporate governance issues when making investment decisions.

Principle 6: Transparency and reporting

Administering authorities should:

- Act in a transparent manner, communicating with stakeholders on issues relating to their management of investments, its governance and risks, including performance against stated objectives
- Provide regular communication to scheme members in the form they consider most appropriate

✓ **Full compliance**

The Fund's annual report includes all of the Fund's policies including the governance policy statement, governance policy compliance statement, communications policy statement, responsible investment and stewardship policy, funding strategy statement and statement of investment principles. The annual report can be found on the council's website together with standalone versions of each of these documents.

Quarterly reports to the Pension Fund Board on the management of the Fund's investments are publicly available on the council's committee administration website.

Pensions newsletters are sent to all Fund members.

SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **KEY PERFORMANCE INDICATORS**

SUMMARY OF ISSUE:

In line with best practice, Pension Fund Board members will be supplied with Pension Fund key performance indicators (KPIs) on a quarterly basis, covering investment and administration practices.

RECOMMENDATIONS:

It is recommended that:

1 The Pension Fund Board note the KPI statement shown in Annex 1.

REASON FOR RECOMMENDATIONS:

To comply with best practice.

DETAILS:

Requirement

1 In line with best practice, future Pension Fund Board meetings will be supplied with a schedule of Pension Fund key performance indicators (KPIs), covering investment and administration practices.

Key Performance Indicators

2 The KPIs cover the following areas:

- Funding level
- Death benefit administration
- Retirement administration
- Benefit statements
- New joiners
- Transfers in and out
- Material posted on website
- Employer and member satisfaction
- Investment performance
- Data quality
- Contributions monitoring
- Audit
- Overall administration cost

3 The KPI schedule is shown as Annex 1.

4 Periods covered in the schedule range from one month, three months and twelve months.

5 Members are invited to discuss the performances set out in the schedule.

CONSULTATION:

6 The Chairman of the Pension Fund has been consulted and has offered full support regarding the content, structure and performances achieved set out in the schedule.

RISK MANAGEMENT AND IMPLICATIONS:

7 There are no risk related issues contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

8 There are no financial and value for money implications.

CHIEF FINANCE OFFICER COMMENTARY

9 The Chief Finance Officer is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed and that the proposed KPI model offers an effective framework for the monitoring of the essential pension fund KPIs.

LEGAL IMPLICATIONS – MONITORING OFFICER

10 There are no legal implications or legislative requirements associated with this report.

EQUALITIES AND DIVERSITY

11 The reporting of such information will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

12 There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

13 The following next steps are planned:

- Continued improvement in the indicators.
- Further refinement and additions of useful data.

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman.

Annexes:
Annex 1: Schedule of Key Performance Indicators

Sources/background papers:
None

11

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KPI - DETAILED ACTIONS, TIMESCALE AND REPORTING REQUIREMENTS: To 30 June 2014 Annex 1

11

No	Description	Target	Lead Officer	Actual (Score and RAG)	Reporting Period	Previous Score	Date Last Reported	Improvement/Deterioration
1	**FUNDING**							
	IMPROVE FUNDING LEVEL Funding level to increase from current levels of 72%	**100%**	PT	**79.8%**	30/06/14	**78.8%**	31/03/14	1.00%
2	**PENSION ADMINISTRATION**							
	DEATH BENEFITS Notify potential beneficiary of lump sum death grant within 5 days	**95%**	PB	**100.0%**	3 months to 30 June 14	**100.0%**	3 months to 31 Mar 14	0.00%
	Write to dependant and provide relevant claim form within 5 days of notification of death	**90%**		**91.5%**	3 months to 30 June 14	**94.6%**	3 months to 31 Mar 14	-3.05%
	Pay death grant within 5 days of receipt of relevant documentation	**90%**		**90.0%**	3 months to 30 June 14	**100.0%**	3 months to 31 Mar 14	-10.00%
	Issue notification of dependant's pension within 5 days of receipt of relevant claim forms	**90%**		**90.0%**	3 months to 30 June 14	**100.0%**	3 months to 31 Mar 14	-10.00%
	RETIREMENTS Retirement options to members within 10 days	**90%**	PB	**83.7%**	3 months to 30 June 14	**95.8%**	3 months to 31 Dec 13	-12.10%
	New retirement benefits processed for payment following receipt of election within 10 days	**95%**		**95.7%**	3 months to 30 June 14	**99.2%**	3 months to 31 Dec 13	-3.49%
	BENEFIT STATEMENTS ABS issued to 95% of eligible active members by 30th September	**95%**	PB	**100.0%**	3 months to 30 June 14	**100.0%**	3 months to 31 Mar 14	
	DBS issued to 85% of eligible deferred members by 30th June	**95%**		**100% issued by 26/09/13**	3 months to 30 June 14	**100% issued by 26/09/13**	3 months to 31 Mar 14	
	NEW JOINERS New starters processed within 20 days	**90%**	PB	**98.8%**	3 months to 30 June 14	**98.4%**	3 months to 31 Mar 14	0.41%
	TRANSFERS IN Non LGPS transfers-in quotations processed within 20 days	**90%**	PB	**100.0%**	3 months to 30 June 14	**98.8%**	3 months to 31 Mar 14	1.23%
	Non LGPS transfers-in payments processed within 20 days	**90%**		**100.0%**	3 months to 30 June 14	**98.8%**	3 months to 31 Mar 14	1.23%
	TRANSFERS OUT Non LGPS transfers-out quotations processed within 20 days	**90%**	PB	**100.0%**	3 months to 30 June 14	**100.0%**	3 months to 31 Mar 14	0.00%
	Non LGPS transfers out payments processed within 20 days	**90%**		**100.0%**	3 months to 30 June 14	**100.0%**	3 months to 31 Mar 14	0.00%
	MATERIAL POSTED ON WEBSITE Relevant Communications Material will be posted onto website within one week of being signed off	**95%**	PB	**100%**	3 months to 30 June 14	**100%**	3 months to 31 Mar 14	
3	**CUSTOMER SERVICE**							
	EMPLOYER SATISFACTION/SURVEY Overall satisfaction score for employers to be 80%	**80%**	PT/PB	**Not available**	At May 14	**92%**	At Feb 14	
	MEMBER SATISFACTION/SURVEY Overall satisfaction score for members to be 80%	**80%**	PB	**Not available**	3 months to 30 June 14	**95%**	3 months to 31 Mar 14	
4	**INVESTMENT PERFORMANCE**							
	INVESTMENT RETURNS/OVERALL FUND PERFORMANCE Returns to at least match the benchmark	**Benchmark**	PT	**BENCHMARK 11.3%**	12 months to 30 June 14	**BENCHMARK 7.1%**	12 months to 31 Mar 14	
				ACTUAL 10.6%	12 months to 30 June 14	**ACTUAL 8.6%**	12 months to 31 Mar 14	
5	**DATA**							
	DATA QUALITY Data quality within the Fund should be at least 90% accurate.	**90%**	PB	**99%**	12 months to 31 Mar 14	**99%**	12 months to 31 Mar 13	
6	**CONTRIBUTIONS**							
	CONTRIBUTIONS RECEIVED **Pension Fund** 98% (total value) of contributions to be received by 21st day of the ensuing period.	**98%**	PT	**98%**	Jun-14	**98%**	Mar-14	0.00%
7	**AUDIT**							
	CLEAN AUDIT REPORT Receive an unqualified audit opinion from the external auditors	**Clean Report**	PT/PB	**Achieved**	12 months to 31 Mar 14	**Achieved**	12 months to 31 Mar 13	
	Annual audit returns no significant findings	**No significant findings**		**Achieved**		**Achieved**		
8	**COST**							
	COST PER MEMBER Administration cost per member to remain in lowest CIPFA benchmarking quartile	**< lowest quartile**	PT/PB	**Achieved**	12 months to 31 Mar 14	**Achieved**	12 months to 31 Mar 13	

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SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **CORPORATE GOVERNANCE SHARE VOTING**

SUMMARY OF ISSUE:

This report provides a summary of the Fund's share voting process in Q1 2014/15.

RECOMMENDATIONS:

It is recommended that the Pension Fund Board:

1 Note the report.

REASON FOR RECOMMENDATIONS:

The Pension Fund Board must approve all pension fund working documents.

DETAILS:

Background

1 The informed use of shareholder votes, whilst not a legal duty, is a responsibility of shareholders and an implicit fiduciary duty of pension fund trustees and officers to whom they may delegate this function. Such a process requires the adherence to an approved share voting policy and the advice of a consultant skilled in this particular field.

2 The Surrey Pension Fund appointed Manifest in 2013 to provide consultancy advice on share voting and the whole spectrum of company corporate governance. Manifest has assisted in ensuring that the Fund's stewardship policy reflects the most up-to-date standards and officers learn of the latest developments and can reflect these developments in the Fund's share voting policy and the Statement of Investment Principles (SIP).

Responsible Investment and Stewardship Policy

3 The Financial Reporting Council (FRC) is currently consulting on its two-yearly review of changes to the UK Corporate Governance Code. This review follows earlier consultations on directors' remuneration, risk management, internal control and the going concern basis of accounting. The proposed changes to the UK Corporate Governance Code are due to be published at the start of October 2014.

4 A report with the new Code and revised share voting policy will be presented to the 14 November 2014 Board meeting. A schedule of the abbreviations used in the report is shown as Annex 1 and the current share voting policy is shown as Annex 2.

Meetings Voted: Q1 2014/15

5 Table 1 shows that 274 meetings were voted in total during Q1 2014/15, comprising 257 AGMs and 17 other meetings. The main peak AGM season is captured in this quarter, including the whole Japanese season. Due to the early peak seasons in some European markets (Scandinavia in particular), this explains the position of Japan above Europe (Developed) at the top of the list.

Table 1: Meetings Voted

Region	Meeting Type					Total
	AGM	EGM	GM	SGM	Class	
UK & Ireland	92	-	7	1	-	100
Japan	58	-	-	-	-	58
Europe – Developed	52	-	-	-	-	52
Asia & Oceania – Developed	25	4	-	-	1	30
Asia & Oceania – Emerging	10	1	-	-	-	11
South & Central America	7	3	-	-	-	10
North America	6	-	-	-	-	6
Europe – Emerging	5	-	-	-	-	5
Africa	2	-	-	-	-	2
Total	257	8	7	1	1	274

12

Resolutions

6 Table 2 shows the total number of resolutions voted by region, broken down by meeting type. This clearly shows the high volume of voting decisions that AGMs bring compared with other meetings. In Table 1, AGMs comprise over 90% of the meetings while Table 2 shows AGMs account for over 99% of the resolutions. During the quarter, 4,298 resolutions were voted, with the bulk of these in the UK & Ireland (1,886), Europe (Developed) (916) and Japan (803).

Table 2: Resolutions Voted

Region					Meeting Type	Total
	AGM	GM	EGM	Class	SGM	
UK & Ireland	1,870	15	-	-	1	1,886
Europe – Developed	916	-	-	-	-	916
Japan	803	-	-	-	-	803
Asia & Oceania – Developed	250	-	4	1	-	255
Asia & Oceania – Emerging	131	-	2	-	-	133
Europe – Emerging	110	-	-	-	-	110
North America	87	-	-	-	-	87
South & Central America	52	-	6	-	-	58
Africa	50	-	-	-	-	50
Total	4,269	15	12	1	1	4,298

7 Month by month during Q1 2014/15, the peak of annual voting activity becomes increasingly apparent as ever more numerous AGMs are held. The very high concentration of AGMs in this quarter, especially May 2014, highlights the logistical challenges faced by investors and analysts in processing the high volumes of very important information that are consumed at this time of year. Such concentration of workload volume places stresses on the whole process and therefore poses a valid question about the capacity required to ensure well considered voting decisions.

8 Manifest research therefore now identifies the lead audit partner for each UK company, outlining other companies for whom they also act as lead audit partner, and when the financial year ends are for each. This is to highlight the potential pitfalls of such high workloads concentrated into one quarter of the year.

Table 3: Resolutions Voted per Month (April to June)

Event	April	May	June	Total
AGM	1,311	1,755	1,203	4,269
GM	-	9	6	15
EGM	1	5	6	12
Class	-	-	1	1
SGM	1	-	-	1
Total	1,313	1,769	1,216	4,298

12

Voting Patterns

9 This section examines some patterns of voting by resolution category and voting policy. Table 4 shows some important perspective on the type of voting decisions being made. As part of the research analysis, Manifest categorises each resolution according to the governance considerations to which they relate. Firstly, over half of all of the resolutions voted during the quarter relate to the company board, which includes director election resolutions, the single most numerous resolution type at AGMs. However, of the main categories (i.e. those which occur most frequently), it is one of the two least contentious in terms of Surrey's voting policy (other than Audit & Reporting), with fewer than 10% of the resolutions placing a vote against management.

10 The data suggests that Surrey votes against management in a targeted way on specific issues, with much higher than average opposition levels on the more specific resolution types such as sustainability, shareholder rights, remuneration, and audit and reporting (including a large number of report and accounts resolutions). Secondly, the table shows the breakdown of resolutions on which Surrey's votes were cast in opposition to the recommendation of company management, and what proportion of the total this represents. One resolution category where Surrey has voted against management frequently is Remuneration, where 111 of the 441 votes have been cast against management.

Table 4: Votes Against Management By Resolution Category

Resolution Category	Total Resolutions	Voted Against Management	% votes against Management
Board	2,251	214	9.5%
Capital	698	115	16.5%
Audit & Reporting	530	12	2.3%
Remuneration	441	111	25.2%
Shareholder Rights	246	69	28.1%
Corporate Actions	48	0	0.00%
Sustainability	44	34	77.3%
Other	40	23	57.5%
Total	4,298	578	13.5%

Shareholder Proposed Resolutions

11 There were 53 resolutions proposed by shareholders, shown in Table 5. The largest number of those identifiable, i.e., not simply classified as "other" due to the vague nature of the proposal, related to shareholder rights (18), which is the main resolution category on which Surrey has most frequently opposed management. Telefon AB LM Ericsson (7) and Total SA (5) accounted for 12 of the 18 resolutions on shareholder rights. Ericsson shareholders had requests relating to representation rights (board representation and equal meeting voting rights). Total SA was subject to shareholder requests relating to board attendance fees, committee composition to include employee representatives, executive compensation links to safety, the introduction of a loyalty dividend, and request for a quarterly newsletter.

12

12 Shareholder proposed resolutions often attract relatively high levels of votes against management, especially where the matter at hand is one on which investors have strong views. The tabling of a shareholder proposal is one way in which shareholders can put pressure on a company, by highlighting an issue and potentially garnering public support for their cause. The flipside danger is of course the possibility of a very public rejection of the question by other shareholders. Included in Other are single instances of issues, including appropriation of profits, removal of directors, ethical business practices, meeting procedures, non-executive and other remuneration, share buybacks and return of capital and treasury shares. Surrey has consistently supported proposals which would have the effect of enhancing shareholder rights.

Table 5: Shareholder Proposed Resolutions

Resolution Sub-category	Shareholder Proposals	Voted Against Management	% Against Management
Other	20	19	95.0%
Directors – Elect	6	2	33.3%
Other Articles of Association	6	3	50.0%
Shareholder Rights	5	5	100.0%
Corporate Governance	3	1	33.3%
Meeting Formalities	3	3	100.0%
Dividends	2	2	100.0%
Other	8	8	100.0%
Total	53	43	81.1%

Remuneration

13 Table 6 sets out Surrey's voting record with regard to remuneration. The most common remuneration related resolution for Surrey to oppose is the Remuneration Report, comprising 88 of the 111 remuneration-related resolutions voted against management by Surrey during the period.

14 The specific aspects of Surrey's policy against which UK companies are most frequently coming up short with regard to remuneration resolutions are:

- where the upper limit on bonus is too high (60 UK companies, including BAE Systems, BP, Centrica, HSBC Holdings, Lloyds Banking Group, Rio Tinto, Legal and General Group, Standard Life, Tesco, WM Morrison, ITV, Glencore and International Consolidated Airlines);
- where the Remuneration Committee contains a non-independent director (28 UK companies including BP, Centrica, Rio Tinto, International Consolidated Airlines (all of whom had bonus cap issues), GlaxoSmithKline, National Express and bwin.party digital entertainment);
- absence of claw back on long and/or short term incentives (24 UK companies, including BP, Rio Tinto, International Consolidated Airlines, Legal and General group (all of whom were also flagged for bonus cap concerns), Merlin Entertainments and WPP;
- where performance targets are not measured against a benchmark (11 UK companies, including Tesco (who will shortly be changing CEO), Merlin Entertainments and ITV who all were flagged for bonus cap concerns) 12

15 Reckitt Benckiser is notable as the only company who was flagged for all of the concerns above, and received a very low "C" grade for their Manifest Remuneration Assessment. The assessment correctly anticipated that shareholders would express significant concern at the meeting, where 42% of shareholders opposed the remuneration report and 21% opposed the remuneration policy, compared with average approval levels of 90% for remuneration reports and policy votes in the UK.

Table 6: Remuneration

Resolution Category	Total Resolutions	Voted Against Management	% Against Management
Remuneration Report	141	88	62.4%
Remuneration Policy	93	2	2.2%
Policy (Long-term Incentives)	72	5	6.9%
Non-executive Remuneration	59	8	13.6%
Amount (Total, Collective)	28	1	3.6%
Other	22	2	9.1%
Policy (Short-term Incentives)	11	5	45.5%
Amount (Total, Individual)	5	0	0.0%
Policy (Contracts)	5	0	0.0%
Policy (Other Component)	5	0	0.0%
Total	441	111	25.2%

Monitoring and Review

16 The share voting policy is kept under constant review and will be submitted for approval to a future Board meeting when the current proposed revisions to the Corporate Governance Code have been published in October 2014.

CONSULTATION:

17 The Chairman of the Pension Fund has been consulted on the current position and has offered full support for the proposals.

RISK MANAGEMENT AND IMPLICATIONS:

18 There are no risk related issues contained within the report's proposals.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

19 There are no financial and value for money implications.

DIRECTOR OF FINANCE COMMENTARY

20 The Director of Finance is satisfied that the share voting policy offers an effective framework for the sound share voting of the pension fund, subject to the proposed revision to be presented to the Board when possible.

12

LEGAL IMPLICATIONS – MONITORING OFFICER

21 There are no legal implications or legislative requirements associated with this report.

EQUALITIES AND DIVERSITY

22 The approval of a share voting policy will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

23 There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

24 The following next steps are planned:

- Adoption and implementation of the share voting policy
- Policy is kept under review

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman

Annexes:

Annex 1: List of abbreviations
Annex 2: Fund's current share voting policy

Sources/background papers:
None

12

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AGM

An Annual General Meeting of shareholders, normally required by law.

EGM

An Extraordinary General Meeting of shareholders, where a meeting is required to conduct business of an urgent or extraordinary nature. Such business may require a special quorum or approval level.

GM

A General Meeting of shareholders, often used interchangeably with the term EGM or OGM, depending on the term used by the issuer in question.

OGM

An Ordinary General Meeting of shareholders, which is a meeting at which ordinary business is to be conducted (i.e. business which does not require a special quorum or approval level).

Court

A meeting of shareholders which is convened by a Court as opposed to by management. This is often used in the UK in order to effect a scheme of arrangement during a corporate transaction.

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Responsible Investment and Stewardship Policy

1 Introduction

1.1 Surrey Pension Fund (the Fund) aims to be an informed and responsible long-term shareholder of the companies in which it invests. The Fund has a commitment to encourage responsible corporate behaviour, which is based upon the belief that active oversight and stewardship of companies encourages good long-term value and performance. The Fund has a duty to protect and enhance the value of its investments, thereby acting in the best interests of the Fund's beneficiaries.

1.2 The Fund takes seriously its responsibility to ensure that its voting rights are exercised in an informed, constructive and considered manner.

1.3 The fund complies with the Myners Principles of investment management and the UK Stewardship Code, the seven principles of which are shown below at section 5.

1.4 The Fund will review its Responsible Investment and Engagement Policy annually at the same time it reviews its Statement of Investment Principles. The Fund's officers will carry out this review and propose any changes to the Investment Committee for consideration

2 Scope

2.1 The Fund aims to vote its shares in all markets wherever practicable. However, due to the relative size of its holdings, we will focus our attention on the quality of our major asset holdings, i.e., UK, EU, US, Far East and emerging markets assets. 12

2.2 The Fund supports the 'comply or explain' principles of The United Kingdom Corporate Governance Code (the Code) and will seek to take all relevant disclosures into account when exercising its votes. While the Fund expects companies to take appropriate steps to comply with the Code, we recognise that departure from best practice may be justified in certain circumstances. In these situations, the Fund expects a considered explanation from the company.

2.3 Corporate governance principles and standards vary from market to market and so the Fund's voting policy allows for some flexibility and discretion with due consideration to local circumstances.

3 General Principles

3.1 In general, the Fund aims to support corporate management in their stewardship role. This document sets out the Fund's high level voting principles and the circumstances where the Fund may override support for company management proposals. In general, where the Fund cannot support management it will positively abstain or withhold a vote but, in certain cases, reserves the right to vote against company management.

3.2 In ordinary circumstances, the Fund delegates individual corporate engagement activity to its investment managers. The Fund will, however, consider engaging on a collective basis with other investors on issues of mutual interest.

4 Voting Policy

4.1 Audit & Accountability

The audit process affords investors significant protections by ensuring that management has effective internal controls and financial reporting systems.

Auditor independence may be compromised if the same firm has audited the company for a long time (three years or more) or where the firm earns significant fees from non-audit services. In order to help maintain auditor objectivity we would expect companies to consider submitting the audit function to periodic tender and to disclose their policy on tendering, including when the audit was last put to tender.

- **Approval of Financial Statements**

Where there is a qualified audit statement, or restatements of annual results made in the previous year (apart from where adapting to new regulations), or where there are concerns of fundamental significance, the Fund will consider approval on a case by case basis.

- **Removal of Auditors**

Surrey Pension Fund will normally vote with management on proposals for the removal of auditors, unless the proposal is for alleged financial irregularities. In this instance, the Fund will judge on a case by case basis.

12

- **Extra Financial Reporting**

Companies should have regard to the environmental and societal risks and impacts of their operations as these can have a material impact on shareholder returns over a variety of time horizons. We believe that it is good management practice to assess and report on material "Extra Financial" risks associated with the governance of environmental and sustainability issues; where we consider that disclosure on these risks is inadequate the Fund will withhold its vote on the annual report or, where available, the sustainability report.

4.2 The Board & Committees

- **Nomination & Succession Planning**

There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board. The board should have plans in place for orderly succession and the policies relating to this should be disclosed in the Company's annual report.

- **Committee Independence**

Audit, Remuneration and Nomination Committees are key components of effective governance for companies. These Committees should be composed entirely of independent non-executive directors; the Fund may therefore abstain from a director's election if they are an executive or non-independent director on the Remuneration Committee.

- **Separation of Chairman & CEO**

The Fund believes the roles of Chairman and CEO should be separate. There may be individual circumstances where it is necessary to combine the roles for a specified purpose or over a period of time in which case we will take account of the explanations provided. In all other circumstances, the Fund will abstain on the election of the Chairman.

- **Board Balance & Diversity**

Companies should seek to ensure that their boards are balanced for appropriate skills, competence and experience. Diversity of gender and experience are equally important and we expect to see clear disclosure from companies about their efforts to address gender imbalance and, in particular, how they aim to reach at least 30% female representation.

- **Notice Periods**

Director notice periods are significantly important. Where an executive director's notice period exceeds 12 months or where severance pay exceeds an equivalent of twelve months, the Fund may abstain from voting.

- **Removal of Directors**

Where there is a proposal to remove a director, the Fund will vote against it unless the proposal has Board support and it is uncontested by the individual concerned. Where the proposal is contested by the individual concerned, the Fund will consider its position on a case by case basis.

4.3 Executive Remuneration

Executive remuneration should be determined by a formal procedure which is independent of the executives in question. The remuneration committee, in addition to demonstrating independent membership should have written terms of reference and receive independent advice which is wholly separate from other corporate activities such as, for example, audit or HR. 12

There should be comprehensive, transparent and comprehensible disclosure of directors pay and policy. Policy in particular should fully explain the aims and objectives of reward strategies in the context of corporate objectives.

- **Approval of Long Term Incentive Schemes**

The Fund's policy on executive remuneration is that companies should develop equitable reward systems that genuinely incentivise directors to deliver sustainable, long-term shareholder value, avoiding reward for results over the short term. The Fund wishes to encourage companies to move away from "one-size-fits-all" performance conditions and to introduce objective performance conditions related to the company's long-term strategy. Discretionary share options and other Long Term Incentive Plans can, subject to appropriate safeguards, be acceptable elements of a director's remuneration.

The Fund will vote in favour of executive reward plans when:

- The company has a remuneration structure that encourages participation across the workforce.
- There is a capital commitment on the part of executive participants at the inception of the scheme.
- Where the exercise of options or the vesting of shares for executive participants is based on performance targets which reflect outstanding and sustainable performance and which are insulated from a particular treatment in the accounts or general market factors.
- Where disclosure is adequate to enable the assessment of rewards under the scheme and the cost to the company.

- Where the performance period for any long term scheme is five years or more.
- Where the participants are not eligible for multiple share-based incentives.
- Where the scheme does not have the potential to involve the issuing of shares which will unduly dilute existing holdings or involve a change in control of the company.

The Fund will abstain from supporting an all employee share scheme where non-executives are also permitted to participate.

4.4 Shareholders' Rights & Capital Structures

Surrey will consider resolutions relating to shareholder rights on a case by case basis. The following outlines the principles that we expect our companies to adhere to:

- **Pre-emption right for issues of new capital**

The Fund does not support resolutions that are inconsistent with rules of the Pre-emption Group.

- **"One Share One Vote"**

The Fund does not support issues of shares with restricted or differential voting rights, nor any action which effectively restricts the voting rights of shares held by it.

12

- **Share Repurchases**

The Fund will normally vote in favour of an authority for share repurchases, provided that it complies with the Listing Rule guidelines (e.g. limit of 15% of issued share capital) and that directors demonstrate that this is the most appropriate use of a company's cash resources. Companies should adopt equal financial treatment for all shareholders. The Fund therefore supports measures that limit the company's ability to buy back shares from a particular shareholder at higher-than-market prices.

4.5 Mergers & Acquisitions

Surrey supports mergers and acquisitions that enhance shareholder returns in the longer term and encourages companies to disclose fully relevant information and provide for separate resolutions on all issues which require the shareholders to vote, for example, the effect of a merger on the compensation and remuneration packages of the individual Board members.

Due to the investment implications of M&A activity, the fund will liaise with its portfolio managers prior to making a final voting decision in support of takeovers.

Companies should seek shareholder approval on any action which alters the fundamental relationship between shareholders and the Board. This includes anti-takeover measures.

4.6 Article Changes

The Fund does not support proposed changes to Articles of Association and/or constitutional documents that reduce shareholder rights or do not reflect generally accepted good governance practices.

4.7 Political & Charitable Donations

The Fund considers that making of donations to political parties is not an appropriate use of shareholders' fund and so will vote against any authority to make such donations.

Charitable donations are acceptable if they are reasonable and further the company's wider corporate social responsibilities. The Fund encourages the issue of a policy statement by companies relating to such donations and full disclosure of the amounts given to the main beneficiaries.

4.8 Shareholder Resolutions

All such proposals will be reviewed on a case-by-case basis. We will generally support requests for improved corporate disclosure, notably relating to sustainability reporting. In other circumstances the fund will generally vote against shareholder resolutions not supported by management.

4.9 Other Business

Where a resolution proposes moving to an unregulated market or de-listing, the Fund will consider issues on a case by case basis. Schemes of arrangement, significant transactions and bundled resolutions are also considered on a case by case basis.

Where a resolution is proposed to allow for any other business to be conducted at the meeting without prior shareholder notification, the Fund will not support such resolutions.

5 The Principles of the UK Stewardship Code

In order to conform with the principles of the UK Stewardship Code, institutional investors, such as the Surrey County Council Pension Fund, should:

1. Publicly disclose their policy on how they will discharge their stewardship responsibilities.
2. Have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.
3. Monitor their investee companies.
4. Establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.
5. Be willing to act collectively with other investors where appropriate.
6. Have a clear policy on voting and disclosure of voting activity.
7. Report periodically on their stewardship and voting activities.

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SURREY COUNTY COUNCIL

SURREY PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **LOCAL GOVERNMENT PENSION SCHEME: DRAFT GOVERNANCE REGULATIONS**

SUMMARY OF ISSUE:

The report explains the planned changes to the governance of the Local Government Pension Scheme (LGPS) as a result of the Public Service Pensions Act 2013 and draft Regulations recently issued. A key requirement is for a proposed new local Pension Scrutiny Board to monitor compliance with rules and standards.

RECOMMENDATIONS:

It is recommended that the Pension Fund Board:

1 Note the report.

2 Note the response to the consultation from the Surrey Pension Fund.

REASON FOR RECOMMENDATIONS:

The Pension Fund Board must be aware of all governance Regulations for the administration of the Pension Fund.

DETAILS:

Background

1 The changes introduced by the Public Service Pensions Act 2013 Act are aimed at achieving a more coherent and consistent system to provide assurance that benefits are paid, contributions are received and the Code of Practice is followed in accordance within the law and subject to good practice. The new arrangements are due to be in place by 1 April 2015 and draft Regulations have been published.

2 The recently published draft Regulations are shown as Annex 1.

Distinct Roles set out by the Act

3 The Act sets out four distinct roles to be performed for each of the public service pension schemes.

4 Under the Act, the Responsible Authority is the person who makes Regulations for the scheme. In the case of the LGPS, this is the Secretary of State for Communities and Local Government. Although not mentioned in the Act, the Secretary of State will continue to be responsible for policy. Clause 3(5) of the Act provides that the consent of HM Treasury is required before any regulations can be made.

5 The **Scheme Manager** is ‘the person responsible for managing or administering’ the scheme and any other statutory scheme connected with it. For the LGPS, the Scheme Manager is the administering authority as currently defined by LGPS regulations, i.e., Surrey County Council for the Surrey Pension Fund. The Surrey Pension Fund Board has delegated authority to take decisions pertaining to the running of the pension fund.

6 The **Pension Board** (overseeing/scrutiny Board) is a new creation and will have responsibility for assisting the Scheme Manager in securing compliance with scheme Regulations, other legislation covering governance and administration, and the requirements of the Pensions Regulator. Such boards will operate at the Fund level for the LGPS.

7 The **National Scheme Advisory Board** has responsibility for providing advice to the Responsible Authority and the Pension Boards. The remit and membership of this Board will be set out in Regulations, which have yet to be published. In order to assist that process a shadow board has been set up in order to put this structure to the test before setting it out in regulation.

8 The role of the **Pensions Regulator** was established by the Pensions Act 2004 to regulate work based pensions. Its primary statutory objectives are to protect member benefits, to promote and to improve understanding of the administration of work based pension schemes and to maximise employer compliance with employer duties and employment safeguards. The Pensions Regulator will now play a key role within the LGPS, linking the Scheme Advisory Board and Local Boards to the Secretary of State. They will have Regulatory oversight, must produce a code of practice and report on any breaches.

Scrutiny Board

9 One of the provisions of the Public Service Pensions Act 2013 will be the requirement to establish the new Pension Board to provide for oversight and scrutiny of the Fund.

10 The new Pension Board has responsibility for assisting the scheme manager in relation to the following matters:
(a) securing compliance with the scheme Regulations and other legislation relating to the governance and administration of the scheme;
(b) securing compliance with requirements imposed in relation to the scheme and any connected scheme by the Pensions Regulator;
(c) such other matters as the scheme Regulations may specify, i.e. statutory guidance, risk register, KPIs, etc.

11 Therefore, it is understood that the new Board, required to be in place for each Fund, will undertake a broad monitoring and scrutiny function for the Pension Fund, and support the County Council as the Administering Authority in the tasks set out above. It will not take on the functions currently delegated to the existing Pension Fund Board, but the County Council will need to consider what the governance relationship should be between the new Board and the existing Pension Fund Board, and whether the role, terms of reference or membership of the existing Pension Fund Board should be changed. The current understanding of officers is that no change to the existing terms of reference for the Pension Fund Board will be required. The new Board's terms of reference will reflect the overseeing and scrutiny role proposed by the draft Regulations.

12 Each Administering Authority, i.e., the County Council, has to establish their new Board by 1 April 2015. Its expenses will form part of the administration costs of the Fund.

13 The new Board will be responsible for assisting the Administering Authority with securing compliance with the Regulations, any other legislation relating to the governance and administration of the scheme, and requirements imposed by the Pension Regulator.

14 The new Board could be merged with the existing Pension Fund Board, but this would need specific agreement by the Secretary of State. In practice, the Secretary of State will need to be satisfied that there is no conflict of interest with such an arrangement. Officers regard this option as unworkable.

15 Under the draft Regulations, the new Board could either be established as if under Section 101 of the 1972 Local Government Act, or the Administering Authority could establish its own procedures which apply, e.g., on voting, paying expenses, etc. The first option is as if it the Panel was a statutory committee, governed by legislation, while the second option is more flexible for local choice. The outcome of the consultation process will assist the Government in making a choice of these two options, i.e., Section 101 Committee or flexible option.

16 The new Board must include an equal number of employer and fund member representatives, which should be no less than four (two from the employers and two from the employees). Administering Authorities should establish how the Board members are appointed, but these representatives should not be local councillors. Local councillors could be permitted as additional new Board representatives, but should not exceed the number of employer and employee representatives. Representatives must have relevant experience and capacity to represent their stakeholders and should have no conflict of interest.

Consultation

17 The Regulations are still in draft form and comments were sent in by officers by the deadline of 14 August 2014, shown as Annex 2. Any changes to the current council committee arrangements will need to be achieved by means of an amendment to the Council's Constitution and approved by full Council before 1 April 2015.

Next Steps

18 A report recommending the new constitutional arrangements which need to be in place by 1 April 2015 will be taken to full Council. This will include proposals on membership of the Scrutiny Board, Terms of Reference, delegations, frequency of meetings and decision-making powers. The Pension Fund Board will be kept appraised of progress.

19 Guidance from the Pensions Regulator and LGA is currently being drafted. It is important that this guidance is forthcoming as the Draft Regulations on Scheme Governance only provide a very high level analysis of respective roles with little detail.

CONSULTATION:

20 The Chairman of the Pension Fund Board has been consulted on the report.

RISK MANAGEMENT AND IMPLICATIONS:

21 Risk related issues are contained within the report, most notably the very short timescale before required implementation, no published guidance and no final Regulations yet published.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

22 Financial and value for money implications will be discussed in future reports once a clear guidance has been published.

DIRECTOR OF FINANCE COMMENTARY

23 The Director of Finance will ensure that all material, financial and business issues and possibility of risks will be considered when a report is presented to full Council.

LEGAL IMPLICATIONS – MONITORING OFFICER

24 Legal implications or legislative requirements associated with this initiative will be addressed in the full Council report.

EQUALITIES AND DIVERSITY

25 Equalities and diversity implications associated with this initiative will be addressed in future reports.

OTHER IMPLICATIONS

26 There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

27 The following next steps are planned:

- A report recommending the formation of a new Board to go to full Council

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman

Annexes:
Annex 1: Draft LGPS Governance Regulations
Annex 2: Response to consultation process by the Surrey Pension Fund

Sources/background papers:
None

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Department for Communities and Local Government

13

The Local Government Pension Scheme (Amendment) Regulations 2014

Draft Regulations on Scheme Governance

Consultation

This document/publication is also available on our website at www.gov.uk

Any enquiries regarding this document/publication should be sent to us at:

Department for Communities and Local Government
Eland House
Bressenden Place
London
SW1E 5DU
Telephone: 030 3444 0000

ISBN : 978-1-4098-4254-5

The Consultation Process and How to Respond

Scope of the consultation

Topic of this consultation:	The Local Government Pension Scheme (Amendment) Regulations 2014
Scope of this consultation:	This consultation seeks responses from interested parties on draft scheme governance regulations for the new Local Government Pension Scheme which came into force on 1 April 2014.
Geographical scope:	England and Wales.
Impact Assessment:	These Regulations have no impact on business or the voluntary sector.

Basic Information

To:	This consultation is aimed at all Local Government Pension Scheme interested parties.
Body responsible for the consultation:	The Secretary of State for Communities and Local Government is responsible for policy and the consultation exercise.
Duration:	8 weeks. As timing allows, account will be taken of representations made after the close of the consultation.
Compliance with the Code of Practice on Consultation:	This consultation complies with the Code and it will be for 8 weeks. The consultation is aimed at all parties with an interest in the Local Government Pension Scheme and in particular those listed on the Government's website: https://www.gov.uk/government/publications/local-government-pension-scheme-regulations-information-on-who-should-be-consulted

Background

Getting to this stage:	The Government commissioned Lord Hutton to chair the Independent Public Service Pensions Commission to review public service pensions and to make recommendations on how they can be made sustainable and affordable in the long term, and fair to both public sector workers and the taxpayer. Lord Hutton's final report was published on 10 March 2011. In that report he made clear that change is needed to "make public service pension schemes simpler and more transparent, fairer to those on low and

	moderate earnings”. The recommendations made by Lord Hutton were accepted by the Government and were carried forward into the Public Service Pensions Act 2013. The Act included a requirement for DCLG as a responsible authority to make regulations establishing a national scheme advisory board and enabling each LGPS administering authority to establish local pension boards. In June 2013, the Department published an informal discussion paper inviting comment from a wide range of interested parties on how the requirements of the 2013 Act should be taken forward into the new 2014 Scheme. The outcome of that exercise and comments from the Shadow Scheme Advisory Board has been fully taken into account in the preparation of the draft regulations. These draft regulations carry forward these requirements into the 2014 Scheme

How to respond

1. You should respond to this consultation by **15 August 2014**.

2. You can respond by email to Sandra.layne@communities.gsi.gov.uk. When responding, please ensure you have the words “LGPS Governance Regulations 2014” in the email subject line.

Alternately you can write to:

LGPS Governance Regulations 2014
Department for Communities and Local Government
Zone 5/F5 Eland House
Bressenden Place
LONDON SW1E 5DU

3. When responding, please state whether you are responding as an individual or representing the views of an organisation. If responding on behalf of an organisation, please give a summary of the people and organisations it represents and, where relevant, who else you have consulted in reaching your conclusions.

Additional copies

4. This consultation paper is available on the Department for Communities and Local Government website at: https://www.gov.uk/government/organisations/department-for-communities-and-local-government

Confidentiality and data protection

5. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

6. If you want the information that you provide to be treated as confidential, please be aware that, under the Freedom of Information Act 2000, there is a statutory code of practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, in itself, be regarded as binding on the department.

7. DCLG will process your personal data in accordance with the Data Protection Act 1998 and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties. Individual responses will not be acknowledged unless specifically requested.

Help with queries

8. Questions about the policy issues raised in the document can be sent to the address given at paragraph 2 above.

9. A copy of the consultation criteria from the Code of Practice on Consultation is at http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance. Are you satisfied that this consultation has followed these criteria? If not or you have any other observations about how we can improve the process please email: consultationcoordinator@communities.gsi.gov.uk

or write to:

DCLG Consultation Co-ordinator, Zone 8/J6, Eland House, Bressenden Place London SW1E 5DU.

Contents

Chapter 1

Introduction

1.1 This document commences a period of statutory consultation on the new governance arrangements for the 2014 Local Government Pension Scheme ("LGPS") which came into effect on 1 April 2014. Your comments are invited on the set of draft regulations at **Annex A**. and also on the separate policy issues included at Chapter 3 below.

1.2 **The closing date for responses is 15 August 2014**.

Background and context

1.3 This consultation on the Local Government Pension Scheme (Amendment) Regulations 2014 represents a key step in the process of reform that began with the commitment given in the Coalition Government's programme to review the efficiency, effectiveness and sustainability of public service pension schemes.

1.4 A key aim of the reform process is to raise the standard of management and administration of public service pension schemes and to achieve more effective representation of employer and employee interests in that process.

1.5 The Public Service Pensions Act 2013 included two main provisions to achieve this policy objective. Firstly, a requirement for responsible authorities such as DCLG to establish at national level a Scheme Advisory Board with responsibility to provide advice to the Department on the desirability of changes to the Scheme. And secondly, in cases where schemes like the Local Government Pension Scheme are subject to local administration, for scheme regulations to provide for the establishment of local pension boards to assist administering authorities with the effective and efficient management and administration of the Scheme.

Consultation responses

1.6 In view of the need to give administering authorities and other interested parties sufficient lead-in time to establish local pension boards, Ministers have agreed to a consultation period of 8 weeks.

1.7 To allow for the fullest response to proposed Scheme regulations, every attempt will be made to include any late submissions.

1.8 Your comments should therefore be sent by 15 August 2014 to LGPS Governance Regulations 2014, Department for Communities and Local Government, Zone 5/G6, Eland House, Bressenden Place, London SW1E 5DU. Electronic responses can be sent to Sandra.layne@communities.gsi.gov.uk.

Chapter 2

Proposals for consultation

2.1. The Regulations are being made under the powers conferred by the Public Service Pensions Act 2013. Under Section 3(5) of the 2013 Act, the Regulations require the consent of Treasury before being made.

Preliminary Provisions

2.2 **Regulation 1** covers the citation, commencement, interpretation and extent of the Regulations. The Regulations will apply to the Scheme in England and Wales and, for the most part, will come into operation on 1 October 2014 to allow sufficient time for the new Scheme Advisory Board and local pension boards to become operational on 1 April 2015.

2.3 **Regulation 2** amends the Principal 2013 Regulations in accordance with regulations 3 to 5.

2.4 **Regulation 3** deletes Regulation 53(4) from the Principal 2013 Regulations because that provision becomes obsolete in view of the amendments introduced by these Regulations.

2.5 **Regulation 4** amends Schedule 1 to the Principal 2013 Regulations to include definitions of "Local Government Pensions Scheme Advisory Board" and "local pension board".

2.6 **Regulation 5** inserts new regulations 105, 106,107, 108, 109, 110, 111, 112 and 113 into the Principal 2013 Regulations. These provisions are described in detail immediately below.

Main Provisions

2.7 **New Regulation 105** confers power on the Secretary of State to delegate functions under the Principal 2013 Regulations and administering authorities to delegate their functions. It also allows for any delegated function by an administering authority to be sub-delegated.

Local pension boards : establishment

2.8 **New Regulation 106** concerns the establishment of local pension boards.

2.9. **Regulation 106(1)** provides that each administering authority must establish a local pension board no later than 1 April 2015. This would not prevent a board being established before that date.

2.10 **Regulation 106(1)(a) and (b)** sets out the role of a local pension board as being to assist the administering authority in securing compliance with (i) the Principal 2013 Regulations, (ii) any other legislation, and (iii) requirements imposed by the Pensions Regulator in relation to the Scheme. The role is further extended by **Regulation 106(1)(b)** to assist the administering authority in ensuring the effective and efficient governance and administration of the Scheme. These provisions mirror those set out in section 5(2) and (3) of the Public Service Pensions Act 2013.

2.11**. Regulation 106(2)** carries forward into the Principal 2013 Regulations, section 5(7) of the Public Service Pensions Act 2013. This provides that where the scheme manager of a Scheme under section 1 of the Act is a committee of a local authority, the scheme regulations may provide for that committee also to be the board for the purposes of this section. This is discussed in more detail in Chapter 3.

To ensure that any proposal to combine the committee and local pension board into a single, dual-function body is appropriate and practicable, **Regulation 106(2)** requires such proposals to be approved by the Secretary of State. Where appropriate, the Department may seek advice from relevant interested parties, in particular, the Scheme Advisory Board and Pensions Regulator.

2.12 **Regulation 106(3)** provides that the Secretary of State may, in giving such approval, impose any such conditions that he thinks fit.

2.13 **Regulation 106(4)** enables the Secretary of State to withdraw any approval given under Regulation 106(2) if any of the conditions given under Regulation 106(3) are not met or, more generally, that there is evidence to suggest that the combined body is no longer working as intended.

2.14 **Regulation 106(5)** sets out the means by which an administering authority establishes its local pension board but the draft offers two different alternatives of the regulations as described later in Chapter 3 (Other connected policy issues). Consultees are specifically invited to indicate and comment on their preference.

2.15. **Regulation 106(6)** provides that the costs of local pension boards are to be regarded as administration costs charged to the fund.

13

Local pension boards : membership

2.16. **Regulation 107(1) –** requires each administering authority to determine the membership of the local pension board; the manner in which such members may be appointed and removed and the terms of their appointment.

2.17**. Regulation 107(2)** provides that in determining membership of their local pension board, an administering authority must include employer representatives and member representatives in equal numbers, the total of which cannot be less than four.

2.18**. Regulation 107(2(a)** prevents a councillor member of a local authority being included either as an employer or member representative, but this does not prevent an administering authority from appointing councillor members of a local authority (or any other person) to the local pension board over and above the required equal number of employer and member representatives.

2.19**. Regulation 107(2)(b)** requires an administering authority to be satisfied that employer and member representatives appointed to a local pension board have the relevant experience and the capacity to perform their respective roles. There is a risk that could act as an unhelpful barrier to people putting themselves up as pension board nominees but we believe that this pre-condition is necessary to ensure that appointees to the board have the background and capacity to undertake the duties and responsibilities required of pension board members. The Department will work closely with all relevant interested parties in preparing and publishing guidance on the experience and capacity required of local pension board nominees.

(It is important to note that Regulation 107(2)(b) and the pre-condition of "relevant experience and capacity" is not to be confused with the requirement for pension boards members to acquire "knowledge and understanding" under section 248A of the Pensions Act 2004 as introduced by paragraph 19 of Schedule 4 (Regulatory oversight) to the Public Service Pensions Act 2013.

2.20**. Regulation 107(3)** ensures that the number of employer and member representatives appointed to a local board must represent a majority of total members.

Local pension boards : conflict of interest

2.21. **Regulation 108(1)** carries forward section 5(4) of the Public Service Pensions Act 2013 and requires each administering authority to be satisfied that any person appointed to a local pension board does not have a conflict of interest as defined in section 5(5) of that Act.

2.22**. Regulation 108(2)** requires an administering authority to monitor conflict of interests over time.

2.23**. Regulations 108(3) and (4)** impose requirements on persons to provide relevant information to the administering authority on nomination as a member of a local pension board and, if appointed, during membership.

Local pension boards : guidance

2.24**. Regulation 109** requires an administering authority to have regard to guidance issued by the Secretary of State in relation to local pension boards. In formulating such guidance, the Department will work closely with all relevant interested parties, including the Scheme Advisory Board and the Pensions Regulator.

Scheme advisory board : establishment

2.25**. Regulation 110(1)** provides that a scheme advisory board is established.

2.26**. Regulation 110(2)** sets out the responsibility of the scheme advisory board to provide advice to the Secretary of State on the desirability of making changes to the Scheme in accordance with section 7(1) of the Public Service Pensions Act 2013. But note that we are not proposing to carry forward the provision in the Act that such advice is to be at the Secretary of State's request. We believe that the interaction between the Department and the scheme advisory board should be open and transparent and that scheme regulations should not prevent the scheme advisory board from initiating its own advice or recommendations to the Secretary of State.

2.27**. Regulation 110(3)** extends the scope of the scheme advisory board to include advice and assistance to administering authorities and local pension boards in relation to the effective and efficient administration and management of the Scheme and its pension funds.

2.28**. Regulation 110(4)** permits the scheme advisory board to establish its own procedures.

Scheme advisory board : membership

2.29**. Regulation 111(1)** sets out the membership requirements of the scheme advisory board. The Chair of the scheme advisory board is to be appointed by the Secretary of State and the Department will work closely with the Shadow scheme advisory board in formulating and organising the nomination and appointment process. Membership of the board must comprise at least 2 and no more than 12 persons appointed by the Chair with the approval of the Secretary of State.

2.30**. Regulation 111(2)** confers a duty on the Secretary of State to ensure that approval under Regulation 111(1)(b) is subject to consideration of how fair the Chair has been in nominating employer and scheme members to the board for approval.

2.31. **Regulation 111(3)** requires the constitution of the scheme advisory board to include details of the terms and conditions of members' appointments.

2.32. **Regulation 111(4)** permits persons who are not members of the scheme advisory board to be appointed as members of any sub-committee to the board.

2.33. **Regulation 111(5)** applies the same provision in Regulation 111(3) to members of any sub-committee to the board.

Scheme advisory board : conflict of interest

2.34. **Regulation 112** applies the provision in sections 7(4) and (5) of the Public Service Pensions Act regarding conflict of interest to nominees and members of the scheme advisory board.

Scheme advisory board : funding

2.35. **Regulation 113(1)** provides that the expenses of the scheme advisory board are to be treated as administration costs to the Scheme and recharged to administering authorities in such proportions as are determined by the board.

2.36. **Regulation 113(2)** ensures that safeguards are in place to ensure value for money. Before any monies can be levied on administering authorities by the scheme advisory board, the board's annual budget must first have been approved by the Secretary of State.

2.37. **Regulation 113(3)** requires an administering authority to pay the amount determined by the scheme advisory board under Regulation 113(2).

Chapter 3

Other connected policy issues

Combined Section 101 committee and local pension board (Regulation 106(2)).

3.1. Draft **Regulation 106(2**) enables a single, dual function body to carry out the functions of both a section 101 committee established by the administering authority to manage and administer the Scheme and those of a local pension board.

3.2. In practice, a combined body would be subject to two separate legal codes under both the Local Government Act 1972 and associated legislation, and the Public Service Pensions Act 2013. A combined body might also have difficulty in ensuring that all members had both knowledge and understanding that is currently expected of elected members and the experience and capacity required of local pension board members. There could also be difficult and different issues about conferring voting rights and compliance with local government law on the political composition of committees.

3.3. The Public Service Pensions Act 2013 does allow for this facility in scheme regulations but we are not compelled to introduce it. Comments are therefore invited on whether the Regulations should include such provision.

Establishment of local pension boards (Regulation 106(5)}

3.4. The draft regulations offer two alternatives to the way in which an administering authority could establish their local pension board.

3.5. The first version of **Regulation 106(5)** offers a simple solution by proposing that establishment of a local board should be undertaken as if it was a committee under section 101 of the Local Government Act 1972. This would automatically apply the section 101 regime to the way in which local boards are to be established. Although this option would provide administering authorities with a ready-made set of provisions to help them establish local pension boards, it is arguable that local pension boards should be established on a bespoke basis best suited to their own role and responsibilities.

3.6. The alternative version of **Regulation 106(5)** confers a wide discretion on administering authorities to establish the procedures applicable to a local pension board such as voting rights, the establishment of sub-committees, the formation of joint committees and payment of expenses. This list is not exhaustive, and could include some of the features of the section 101 regime, such as voting rights, political composition, etc. Although this option would represent more of a burden to administering authorities, it would allow greater flexibility and choice at local level in the way that local pension boards are established.

3.7. Consultees are therefore invited to state their preference for option 1, option 2, or any other proposal. Where option 2 is preferred, it would be helpful if the response could also set out those elements which should either be specifically excluded or included from the wide discretion afforded by the second version of Regulation 106(5).

Funding of the Scheme Advisory Board (Regulation 113)

3.8. It is accepted that funding the Scheme Advisory Board will be a complex and difficult matter. **Regulation 113** has been drafted on the basis of informal discussions with interested parties but we acknowledge that more work needs to be done to both ensure that the board is adequately funded to enable them to carry out their agreed work plans and that the cost of the board to each administering authority is fair and represents value for money.

3.9. Comments are therefore invited on what additional provision we need to make to Regulation 113 to achieve both objectives and regarding any other aspect of the scheme advisory board's funding.

Joint pension boards

3.10. As currently drafted, these Regulations require each administering authority to establish a local pension board. However, the extent to which administering authorities are either already sharing, or planning to share, their administration with other administrating authorities, suggests that provision ought to be made in these Regulations for a single pension board to serve more than the one administering authority.

3.11. On the other hand, it would run counter to the spirit of the primary legislation if a single board ended up serving a significant number of administering authorities. We believe therefore, that the default position must be one local pension board for each administering authority, but that exceptions where administration and management is mainly or wholly shared between two or more administering authorities should be catered for. This could be demonstrated by the management and administration being undertaken by a joint committee of the participating administering authorities.

3.12. Comments are invited on whether the Regulations need to provide for shared local pension boards and, if so, what test, if any, should be applied. For example, should provision be made for either the scheme advisory board or the Secretary of State to approve any proposal for a shared pension board?

Annual general meetings, Employer forums, etc

3.13. The staging of AGMs, employer forums, etc, is currently a recommendation in the Department's statutory guidance on governance compliance. There is evidence to suggest that a significant minority of administering authorities do neither and also that those that do, receive positive feedback from employers and scheme members alike.

3.14. Comments are invited on whether the Regulations should require administering authorities to facilitate a forum for both employers and employees on at least an annual basis.

Public Sector Equality Duty

3.15. The Equality Duty is a duty on all public bodies and others carrying out public functions to ensure that public bodies consider the needs of all individuals in their day to day work. It also encourages public bodies to ensure that their policies and services are appropriate and accessible to all and meet different people's needs.

3.16. This raises the question of whether these Regulations should extend the role of the scheme advisory board to have regard to the Equality Duty in making recommendations to the Secretary of State on the desirability of making scheme changes and extending the scrutiny/.compliance role of local pension boards to include the Equality Duty.

3.17. Comments are invited on the appropriateness and practicality of this proposal.

Knowledge and Understanding

3.18. These regulations would require members of local pension boards to have the knowledge and capacity to undertake that role. This contrasts with members of committees established by the administering authority to discharge its pension functions who, although recommended to have regard to the Knowledge and Skills Framework published by CIPFA, are under no regulatory requirement to do so. Whilst recognising that the knowledge and training needs of section 101 and local pension boards are not identical, it is open to question whether the same level of regulatory requirement ought to apply to both bodies.

3.19. Comments are invited on whether either in these Regulations or at some stage in the future, provision should be made in the Principal 2013 Regulations to require members of committees established by the administering authority to discharge its pension functions to comply with the Knowledge and Understanding Framework and other relevant training.

Annex A

STATUTORY INSTRUMENTS

2014 No. 0000

PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

The Local Government Pension Scheme (Amendment) Regulations 2014

Made - - - -	*2014*
Laid before Parliament	*2014*
Coming into force - -	*2015*

These Regulations are made in exercise of the powers conferred by sections 1 and 3 of, and Schedule 3 to, the Public Service Pensions Act 2013(**1**).

In accordance with section 21 of that Act, the Secretary of State has consulted the representatives of such persons as appeared to the Secretary of State to be likely to be affected by these Regulations.

In accordance with section 3(5) of that Act, these Regulations are made with the consent of the Treasury.

The Secretary of State makes the following Regulations:

Citation, commencement interpretation and extent

1.—(1) These Regulations may be cited as the Local Government Pension Scheme (Amendment) Regulations 2014.

(2) In these Regulations "the Principal Regulations" means the Local Government Pension Scheme Regulations 2013(**2**)

(3) These Regulations come in to force as follows—

(a) on 1st October 2014, regulations 2, 4 and 5—

(i) so far as they insert regulation 105 (delegation) into the Principal Regulations,

(**1**) 2013 c. 25
(**2**) S.I. 2013/2356.

(ii) so far as they insert regulation 106 (local pension boards: establishment) into the Principal Regulations for the purposes of the obtaining of approval from the Secretary of State under paragraph (2) of that regulation, and

(iii) so far as they insert regulations 107 (local pensions boards: membership), 108 (local pensions boards: conflicts of interest), 111 (scheme advisory board: membership) and 112 (scheme advisory board: conflict of interest) for the purposes of appointment of members of local pension boards and the Local Government Pension Scheme Advisory Board; and

(b) on 1st January 2015—

(i) regulations 2, 4 and 5 so far as not already commenced, and

(ii) the remainder of these Regulations.

(4) These Regulations extend to England and Wales.

Amendment of the Local Government Pension Scheme Regulations 2013

2. The Principal Regulations 2013 are amended in accordance with regulations 3 to 5.

3. Omit regulation 53(4) (scheme managers: establishment of pension board).

4. In Schedule 1 (interpretation) after the entry for "local government service" insert—

""Local Government Pensions Scheme Advisory Board" means a board established under regulation 110 (Scheme advisory board: establishment);

"local pension board" means a board established under regulation 106 (local pension boards: establishment);"

5. After regulation 104(**3**) insert—

"PART 3

Governance

Delegation

105.—(1) The Secretary of State may delegate any functions under these Regulations.

(2) Administering authorities may delegate any functions under these Regulations including this power to delegate.

Local pension boards: establishment

106.—(1) Each administering authority shall no later than 1st April 2015 establish a pension board ("a local pension board") responsible for assisting it—

(a) to secure compliance with—

(i) these Regulations,

(ii) any other legislation relating to the governance and administration of the Scheme, and

(iii) requirements imposed by the Pensions Regulator in relation to the Scheme; and

(b) to ensure the effective and efficient governance and administration of the Scheme.

(2) Where the Scheme manager is a committee of a local authority the local pension board may be the same committee if approval in writing has been obtained from the Secretary of State.

(3) Approval under paragraph (2) may be given subject to such conditions as the Secretary of State thinks fit.

(**3**) Regulation 104 was inserted by S.I. 2014/1146.

(4) The Secretary of State may withdraw an approval if such conditions are not met or if in the opinion of the Secretary of State it is no longer appropriate for the local pension board to be the same committee.

(5) [Where a local pension board is established by a local authority within the meaning of section 270 of the Local Government Act 1972(**4**), Part 6 of that Act applies to the board as if it were a committee established under section 101 of that Act].

(5) [An administering authority may determine the procedures applicable to a local pension board, including as to voting rights, the establishment of sub-committees, formation of joint committees and payment of expenses].

(6) The expenses of a local pension board are to be regarded as part of the costs of administration of the fund held by the administering authority.

Local pension boards: membership

107.—(1) Subject to paragraphs (2) and (3) each administering authority shall determine—

(a) the membership of the local pension board;

(b) the manner in which members of the local pension board may be appointed and removed;

(c) the terms of appointment of members of the local pension board.

(2) A local pension board must include an equal number, which is no less than 4 in total, of employer representatives and member representatives (**5**) and for these purposes—

(a) a member of a local authority is not to be appointed as an employer or member representative; and

(b) the administering authority must be satisfied that—

(i) a person to be appointed as an employer representative has relevant experience and the capacity to represent employers on the local pension board; and

(ii) a person to be appointed as a member representative has relevant experience and the capacity to represent members on the local pension board.

(3) The number of members appointed under paragraph (2) must exceed the number of members otherwise appointed to a local pension board.

Local pension boards: conflict of interest

108.—(1) Each administering authority must be satisfied that any person to be appointed as a member of a local pension board does not have a conflict of interest(**6**).

(2) An administering authority must be satisfied from time to time that none of the members of a local pension board has a conflict of interest.

(3) A person who is to be appointed as a member of a local pension board by an administering authority must provide that authority with such information as the authority reasonably requires for the purposes of paragraph (1).

(4) A person who is a member of a local pension board must provide the administering authority which made the appointment with such information as that authority reasonably requires for the purposes of paragraph (2).

Local pension boards: guidance

109. An administering authority must have regard to guidance issued by the Secretary of State in relation to local pension boards.

(**4**) 1972 c. 70.
(**5**) See section 5(6) of the Public Service Pensions Act 2013 for definitions of these terms.
(**6**) See section 5(5) of the Public Service Pensions Act 2013 for the meaning of "conflict of interest".

Scheme advisory board: establishment

110.—(1) A scheme advisory board ("the Local Government Pension Scheme Advisory Board") is established.

(2) The Local Government Pension Scheme Advisory Board is responsible for providing advice to the Secretary of State on the desirability of making changes to the Scheme.

(3) The Local Government Pension Scheme Advisory Board is also responsible for providing advice to administering authorities and local pension boards in relation to the effective and efficient administration and management of the Scheme and its pension funds.

(4) Subject to these Regulations, the Local Government Pension Scheme Advisory Board may determine its own procedures including as to voting rights, the establishment of sub-committees, formation of joint committees and the payment of remuneration and expenses.

Scheme advisory board: membership

111.—(1) The Local Government Pension Scheme Advisory Board is to consist of the following members—

(a) the Chair appointed by the Secretary of State; and

(b) at least 2, and no more than 12, persons appointed by the Chair with the approval of the Secretary of State.

(2) When deciding whether to give or withhold approval to appointments under paragraph (1)(b) the Secretary of State must have regard to the desirability of there being equal representation of persons representing the interests of Scheme employers and persons representing the interests of members.

(3) A member of the Local Government Pension Scheme Advisory Board is to hold and vacate office in accordance with the terms of that member's appointment.

(4) The Chair of the Local Government Pension Scheme Advisory Board may appoint persons who are not members of the Local Government Pension Scheme Advisory Board to be members of sub-committees of that Board.

(5) A member of a sub-committee of the Local Government Pension Scheme Advisory Board is to hold and vacate office in accordance with the terms of that member's appointment.

Scheme advisory board: conflict of interest

112.—(1) Before appointing, or approving the appointment of any person to be a member of the Local Government Pension Scheme Advisory Board, the Secretary of State must be satisfied that the person does not have a conflict of interest(**7**).

(2) The Secretary of State must be satisfied from time to time that none of the members of the Local Government Pension Scheme Advisory Board has a conflict of interest.

(3) A person who is to be appointed as a member of the Local Government Pension Scheme Advisory Board must provide the Secretary of State with such information as the Secretary of State reasonably requires for the purposes of paragraph (1).

(4) A person who is a member of the Local Government Pension Scheme Advisory Board must provide the Secretary of State with such information as the Secretary of State reasonably requires for the purposes of paragraph (2).

Scheme advisory board: funding

113.—(1) The expenses of the Local Government Pension Scheme Advisory Board are to be treated as administration costs of the Scheme and are to be defrayed by the administering authorities within the Scheme in such proportions as are determined by the Board.

(**7**) See section 7(5) of the Public Service Pensions Act 2013 for the meaning of "conflict of interest".

(2) The Local Government Pension Scheme Advisory Board must identify the amount to be paid by each administering authority towards its annual costs based on—

(a) its annual budget approved by the Secretary of State; and

(b) the number of persons for which the administering authority is the appropriate administering authority.

(3) An administering authority must pay the amount it is required to pay under this regulation at such time or times as the Local Government Pension Scheme Advisory Board may determine.”.

We consent to the making of these Regulations

Names
Date Two of the Lords Commissioners of Her Majesty's Treasury

Signed by authority of the Secretary of State for Communities and Local Government

Name
Parliamentary Under Secretary of State
Date Department for Communities and Local Government

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Local Government Pension Scheme Regulations 2013 (“the 2013 Regulations”) to make provision in respect of governance of the Scheme.

Regulation 1 commences the substantive provisions from 1st January 2015 for the purposes of making appointments to local pension boards and the Scheme Advisory Board, and brings the provisions fully into force from 1st April 2015.

Regulations 3 and 4 make minor amendments to the 2013 Regulations consequential to the substantive provisions.

Regulation 5 inserts a new Part 3 into the 2013 Regulations.

New regulation 105 permits the Secretary of State to delegate functions under the 2013 Regulations. It permits administering authorities to delegate their functions and also for any delegated function to be sub-delegated.

New regulations 106 to 109 make provision for each administering authority to establish a local pension board to assist it to comply with its legal obligations relating to the Scheme. Where a local authority discharges its pension functions through a committee, it can, with the approval of the Secretary of State appoint that existing committee to be the local pensions board. Local pensions boards must have equal representation of employer representatives and member representatives who must not be councillors of the administering authority and who must constitute the majority of members of the board.

Regulations 110 to 113 establish the Local Government Pension Scheme Advisory Board to advise the Secretary of State, administering authorities and local pension boards in relation to the Scheme. Provision is made for the appointment of members to the Board and for its funding.

Annex 2

Surrey Pension Fund: Response to the Draft Governance Regulations

Timescale
The timescale is challenging and it will be extremely difficult to implement the new reforms by 1 April 2015.

Guidance
Guidance will be extensively relied on, given the broad brush detail included in the Regulations, and will need to be published well before the implementation date in order to be of any use or help, making the 1 April 2015 deadline even more challenging.

Combining the Local Pension Board with the Pensions Committee
The combining of the Local Pension Board function with an existing Pensions Committee would be a challenging solution. The Local Pension Board should be a separate body to the statutory Section 101 committee used to make executive decisions on pension fund management. In order to have credibility, the Local Pension Board should not be the same individuals scrutinising their own decisions. The existing Pensions Committee and the Local Pension Board should be distinct entities, each with their own remit.

Section 101 or Fully Flexible
We would support maximum local discretion over the arrangements for the Local Pension Board and therefore support Option 2. The following items should be included within that discretion:

Membership profile
Voting rights
Terms of Reference and reporting arrangements
Quorum arrangements and frequency of meetings
Payments permitted to Board members including expenses
Process to appoint a chairman

We do not agree with the proposal that the Local Pension Board cannot include local authority members as the representatives of employer bodies in the Fund. This will be too restrictive. The stipulation may be to reduce the potential for any conflict of interest with the existing pensions committee, but provided the memberships of the two functions are different, this shouldn't arise.

Funding of the Scheme Advisory Board
It would be helpful to understand the range of costs to be shared out among the 89 LGPS Funds. Annual increases in the levy payable to fund the National Scheme Advisory Board should be capped to prevent it becoming more of a burden. We suggest no more than CPI indexed increases should apply.

Joint Local Pension Boards
We would be happy for the regulations to include a provision for the Local Pension Board to be shared between administering authorities. Each administering authority should decide if such an arrangement is appropriate based on their local circumstances. We do not believe it is a matter for the Secretary of State or the national scheme advisory board to determine or agree to.

13

Annual Meetings
The provision of a Fund annual meeting is established good practice as is regular contact with Fund employers. However, such provision is a matter for local decision making as to what particular arrangements are suitable for each Fund. Therefore, we do not support the proposal that the Regulations should specify that a forum is required for both employers and employees to meet the Fund on an annual basis. We do not support the regulatory requirement for employee/employer communications. Funds should be trusted to judge what arrangements are suitable locally to promote good communications between both employers and employees within the Fund. This should be determined at a local level.

Equality Duty
As stated above, our view supports as much discretion as possible at a local level over how the new arrangements will apply. We therefore consider it should be up to each Administering Authority to decide if the scrutiny/compliance role of its Local Pension Board should have an explicit regard to the equality duty. We are also not persuaded that the remit of the national scheme advisory board needs to be extended to have regard to this either.

Knowledge and Understanding
Knowledge and understanding are a requirement that the existing Pensions Committee undertake to ensure they have adequate knowledge to discharge their role. We do not feel it is a matter for Regulations to specify, or for a prescriptive national approach. Each Fund should justify and publish its approach, if necessary to the Pension Regulator, as being sufficiently robust.

Surrey Pension Fund
14 August 2014

SURREY COUNTY COUNCIL

PENSION FUND BOARD

DATE: **19 SEPTEMBER 2014**

LEAD OFFICER: **SHEILA LITTLE, DIRECTOR OF FINANCE**

SUBJECT: **LGPS REFORM: OPPORTUNITIES FOR COLLABORATION, COST SAVINGS AND EFFICIENCIES**

14

SUMMARY OF ISSUE:

On 21 June 2013, the Department for Communities and Local Government (DCLG) issued a call for evidence on the future structure of the Local Government Pension Scheme. A document was submitted on behalf of the Pension Fund Board, in consultation with the Chairman of the Pension Fund Board. On 1 May 2014, the Government published a further consultation document, which acknowledged the initiatives put in place by many administering authorities with regard to collaboration and the set up of collective investment vehicles.

RECOMMENDATIONS:

It is recommended that the Pension Fund Board:

1 Note the report.

2 Note the consultation sent by Surrey Pension Fund with views expressed by members within the Board meeting of 15 May 2014.

REASON FOR RECOMMENDATIONS:

The Pension Fund Board must be aware of all prospects for collaborative working surrounding the investment of the Pension Fund.

DETAILS:

Background

1 Following the call for evidence, the DCLG consulted on fundamental changes to the 89 Local Government pension schemes funds in England and Wales. Further consultation by the Government was announced and published on 1 May 2014.

Proposals Made in the Document

2 The proposals can be summarised as follows:

14

- To move to using collective investment vehicles (CIVs). The Hymans analysis showed potential cost savings from moving to CIVs, but these savings would take a decade to realise. Within the report, there was little by way of detail on how the CIVs will work and there will be questions about what kind of CIV, how many, which asset classes and the level of the mandatory nature (if any). The document also acknowledges that the current investment regulations will need changing. It should be noted that the London Boroughs are in the process of setting up a CIV which should be in place by 1 April 2015.

- To move to greater use of passive management for listed assets. The Hymans analysis shows the LGPS scheme as a whole has not outperformed the benchmark, so there is little risk to performance and savings could be made quickly. Again, it asks how this could be done: compulsorily or through a minimum percentage held in passive. A comply or explain approach was mooted.

Consultation Response

3 The consultation closed on 11 July 2014. Surrey's response is included as Annex 1. With over 200 submissions received, the DCLG is currently analysing the responses with support from colleagues at the Cabinet Office.

CONSULTATION:

4 The Chairman of the Pension Fund Board has been consulted on the report.

RISK MANAGEMENT AND IMPLICATIONS:

5 Risk related issues are contained within the report, most notably the lack of any definite timescale and no clear view on the legislative process to be employed.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

6 Financial and value for money implications will be discussed in future reports, once a clear direction ahead has been established.

DIRECTOR OF FINANCE COMMENTARY

7 Director of Finance has ensured that all material, financial and business issues and possibility of risks were considered and addressed in responding to this consultation. The options of collaboration and will be subject to further investigation and reports to the Board.

LEGAL IMPLICATIONS – MONITORING OFFICER

8 Legal implications or legislative requirements associated with this initiative will be addressed in future reports.

EQUALITIES AND DIVERSITY

9 Equalities and diversity implications associated with this initiative will be addressed in future reports.

OTHER IMPLICATIONS

10 There are no potential implications for council priorities and policy areas.

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WHAT HAPPENS NEXT

11 The following next steps are planned:

- Future reports to the Pension Fund Board regarding Government decisions and implementation.

Contact Officer:
Phil Triggs, Strategic Finance Manager (Pension Fund and Treasury)

Consulted:
Pension Fund Board Chairman

Annexes:
Consultation response from Surrey Pension Fund

Sources/background papers:
None

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LOCAL GOVERNMENT PENSION SCHEME: OPPORTUNITIES FOR COLLABORATION, COST SAVINGS AND EFFICIENCES

General Remarks

The Surrey Pension Fund welcomes the publication of the Government's consultation on structural reform of the Local Government Pension Scheme (LGPS). We welcome the Government's recognition that a full scale merger of funds is not the way forward: the change process would have been long and a major distraction from the generation of good investment returns and the managing of deficits. We agree wholeheartedly with the Government's aim for the LGPS to remain sustainable and affordable for employers, taxpayers and members over the long term. However, years of work at Surrey in the creation of a well governed scheme with high achieving fund managers could be undone with the new passive investment proposals. A 'one size fits all' solution isn't compatible with a high performing fund, and any saving on fees would be more than lost in reduced performance, based on Surrey's consistent above benchmark investment returns. The Hymans report has an undue focus on the total investment management fees, when the returns made net of the costs is the important aspect. The research should have focused far less on the 'input' of fee costs and far more on the 'output' of net returns achieved and how to maintain those returns.

Good governance practice and replicating that good practice from well governed funds would have been much more helpful for the future performance of the overall LGPS than the narrow and simplistic focus on costs and fees. As things stand, the Surrey Fund is asked under the existing proposals to forgo an excellent investment performance record. The proposals threaten to destabilise our strong performance by re-routing us down the path of passive asset management and away from the active management that has delivered excellent returns. Surrey has a Fund that was 72.3% funded at the 2013 valuation. A year later in 2014, this has improved to 80%, partly achieved from the Fund's out-performance in actively managed growth assets. We do not think we should have to forego the future prospect of those gains at a time when public services and the taxpayers would benefit more than ever from it.

We would urge the Minister to recognise the high achievement of a number of well governed schemes, such as Surrey's, and to ensure that there remains sufficient flexibility under any changes not to impede high performance. The Hymans evidence, that the LGPS has not generally beaten the returns available from passive management, may work in aggregate. But we do not want to be pulled down to the 'average' level of a passive Common Investment Vehicle when we have excellent and sustained returns over a protracted period. We do not want to take an unnecessarily longer journey to achieve our objective of being 100% funded. Surrey's strong investment returns permit the option to consider how to ease the pressure on employer contributions at a time when the strain on funding for public services is severe. Without the flexibility to continue with our own proven record of good management, the result could be additional employer contributions and in consequence additional cuts in services or pressures for tax rises.

With a total £178bn invested amongst 89 individual Funds, the LGPS will encompass many different approaches. It is not entirely surprising that, when taken as a whole, LGPS Funds have performed broadly in line with the market, as Hymans reported. A random sample of the market may well turn out to show the underlying market average rate. However, we would make the point that the proposals should focus more on helping the less well governed Funds as, by definition, the stronger performers are already delivering good value for money. We must keep what is working well and spread the message to the other funds.

A greater focus on returns net of fees, rather than just the costs themselves, would be helpful for the improvement of the weaker performing funds and would have more validity than the blanket proposals of a CIV and potentially the use of passive funds for all. Measures tailored to the weaker performing funds, such as use of passive funds, or a stronger procurement process,
14 would help improve their performance without restricting the performance of the high achievers.

As it stands, we are very concerned that these proposals could amount to a dilution of the high achievers to the average. This is our major concern and this arises because the Hymans study and Government proposals include all LGPS Funds as one. There is no distinction between the well governed Funds with good returns and all the others. The proposals amount to seeking a generic fund, with average returns, when we know and can demonstrate that Surrey has consistently delivered more than that. Each Fund is in a different position in terms of its funding level and will have a greater or lesser appetite for risk. A centrally imposed solution will ignore all local circumstance. The investment strategy must therefore remain a decision taken by the local councillors, and not from the centre. Government can and should assist by providing a framework for collaboration, but should not compel collaboration or dictate how funds are to be invested.

Q1. Do you agree that common investment vehicles would allow funds to achieve economies of scale and deliver savings for listed and alternative investments? Please explain and evidence your view.

No. Whilst a CIV could achieve economies of scale and provide some opportunities to lower investment management fees, what we are concerned about is the net returns achieved. For the Surrey Fund, the pooling of assets would compromise our flexibility to employ our own choice of active manager. Given the proven track record of our active growth strategies in delivering above benchmark returns over the last ten years, there are significant reservations over such a proposal.

A CIV might be helpful, but it should be done under voluntary participation. If the CIV meant we could access the same investment managers as we currently employ, and who have benefitted the Fund with their excellent performance, but for lower fees, then we would consider participation. It may be that, given our size at around £2.8bn, we already have economies of scale and the savings would be marginal. Also, for the fee reductions, it is likely the Investment Manager would wish to have much simpler reporting mechanisms, perhaps reporting just to one single entity, which would weaken the accountability to the Surrey Fund.

One of the criteria we would certainly wish to apply to any CIV is that it provides for a strongly incentivised fee for better than average return. The Surrey Fund believes that this is essential to promoting the goal of strong performance. Clearly, this could not apply to a 'passive' only CIV, providing for market average returns. Above all, we wish to retain the maximum amount of local freedom which has delivered proven results to date.

Q2. Do you agree with the proposal to keep decisions about asset allocation with the local fund authorities?

Yes. This is essential. We are pleased to note the benefits of local decision making and discretion are recognised as a part of the proposals. It is vital to maintain all local discretions. Local decision makers are best placed to take decisions in the interests of their fund. We firmly oppose any form of compulsion around using a CIV or allocating assets into a passive only management set up.

As well as decision-making on asset allocation kept in-house, there is also a powerful case for the investment of assets managed internally. Surrey will monitor the possibility of introducing internal investment management over the long term.

Q3. How many common investment vehicles should be established and which asset classes do you think should be separately represented in each of the listed asset and alternative asset common investment vehicles?

Central Government should set out the criteria of what a CIV is seeking to achieve. Based on the consultation paper, it appears to be little beyond minimising the input costs of fees that we regard as too simplistic. The use of a common investment vehicle should be on a voluntary basis and it should be left to local Administering Authorities who are interested to decide on the number of funds and the mechanics of its operation. This would set up a framework that would permit Administering Authorities to maximise collaboration, whilst retaining local control and oversight. Funds should not be compelled to participate. Those responsible and accountable in each Fund should be entrusted with deciding based on local circumstance. 14

We also have concerns over applying a CIV to alternative assets. The fund of fund approach, whilst it is more expensive in fees, adds an extra element of diversity and risk reduction. Government proposals may be seeking a reduction in fees at the cost of limiting diversity and increasing risk. Assets held within fund of funds can be held for many different reasons but they are an important extra dimension to the choices over asset allocation. They can be important stabilising assets held to counter the volatility of equities. Again, local choice should be the overriding principle. We believe that, as with listed assets, the overwhelming case is for a permissive framework of a CIV to be in place, with the decision up to each Fund.

Q4. What type of common investment vehicle do you believe would offer the most beneficial structure? What governance arrangements should be established?

While there is some detail in the Hymans report about different types of CIV, Government must set out the relative merits of the different types of CIV and the criteria being proposed to establish them, e.g., access to lower fees, any applicable stamp duty exemption, reduced procurement time and costs, etc. It is then up to the participating Administering Authorities to agree the best governance arrangement to suit their local circumstances.

Q5. In light of the evidence on the relative costs and benefits of active and passive management, including Hymans Robertson's evidence on aggregate performance, which of the options set out offers best value for taxpayers, Scheme members and employers?

NB options are:

- ***Funds could be required to move all listed assets into passive management, in order to maximise the savings achieved by the Scheme.***
- ***Alternatively, funds could be required to invest a specified percentage of their listed assets passively; or to progressively increase their passive investments.***
- ***Fund authorities could be required to manage listed assets passively on a "comply or explain" basis.***
- ***Funds could simply be expected to consider the benefits of passively managed listed assets, in the light of the evidence set out in this paper and the Hymans Robertson report.***

We support the option of Funds considering the benefits of passively managed funds with freedom and choice for Funds to operate within passive funds. Whilst a saving on investment fees overall may be obtained by compulsion, in our case, there is evidence that this would come at the expense of individual fund investment performance. Economies on investment fees offered would be, for us, a false one. Fees are strongly linked to performance in the Surrey Fund, thus ensuring a corresponding benefit as fees rise, as those costs are more than offset by enhanced investment returns. This situation only holds where a Fund can choose to actively manage its assets. Different funds will also have different pressures and time horizons.

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The Surrey Fund has strong positive cash flows and is expected to be cash flow positive for many years. We can therefore afford to take a long term view of our investments and may wish to take more of a risk with the volatility of active management. It is up to each Fund to decide based on its own circumstances.

Surrey's two best performing active equity managers were appointed ten years ago. The net investment performance figures of each manager from inception to 30 June 2014 and the overall monetary amount of the out-performance are as follows:

	Benchmark	**Net of Fees Return**	**Sterling Monetary Amount Representing the Out-Performance**
Manager 1 (Global Equities)	121.3%	190.8%	£74.1m
Manager 2 (UK Equities)	122.4%	200.1%	£53.1m

It may be the case that the weaker performing funds can benefit from being averaged up to the performance level a passive management provides. But it is not the Government's role to insist or decide this across the LGPS. Any use of a common passive management vehicle should be because it can demonstrate its merits to those pension funds who wish to participate. More work on good governance, fee structure, investment strategies, risk reduction and manager selection would have been a far more beneficial study from Hymans than the one presented.

Surrey Pension Fund
July 2014