Notice of Meeting

Surrey Pension Fund Committee

Date & time
Friday, 14 September 2018 at 10.00 am

Place
Committee Room C, County Hall, Kingston upon Thames, Surrey KT1 2DN

Contact
Sharmina Ullah
Room 122, County Hall
Tel 020 8213 2838

Chief Executive
Joanna Killian

We're on Twitter: @SCCdemocracy

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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 Sharmina Ullah on 020 8213 2838.

Elected Members
Mr Tim Evans (Chairman), Mr Ben Carasco (Vice-Chairman), Ms Ayesha Azad, Mr John Beckett (Ewell), Mr David Mansfield and Mrs Hazel Watson

Co-opted Members:
Margaret Janes (Employers), Councillor Tony Elias (Borough/District representative), Councillor Ruth Mitchell (Borough/District representative) and Philip Walker (Employees)

AGENDA

1 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

2 MINUTES OF THE PREVIOUS MEETING: 8 JUNE 2018

(Pages 1 - 20)

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

3 DECLARATIONS OF INTEREST

All Members present are required to declare, at this point in the meeting or as soon as possible thereafter

(i) Any disclosable pecuniary interests and / or

(ii) Other interests arising under the Code of Conduct in respect of any item(s) of business being considered at this meeting

NOTES:

- Members are reminded that they must not participate in any item where they have a disclosable pecuniary interest
- As well as an interest of the Member, this includes any interest, of which the Member is aware, that relates to the Member's spouse or civil partner (or any person with whom the Member is living as a spouse or civil partner)
- Members with a significant personal interest may participate in the discussion and vote on that matter unless that interest could be reasonably regarded as prejudicial.

TRAINING FROM LOCAL AUTHORITY PENSION FUND FORUM

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 (*7 September 2018)*.
2. The deadline for public questions is seven days before the meeting (*6 September 2018)*.
3. The deadline for petitions was 14 days before the meeting, and no petitions have been received.

The Committee has received 3 public questions, questions will be tabled at the meeting alongside the responses.

5 **ACTION TRACKER AND FORWARD PLAN** (Pages 21 - 24)

The Committee is asked to monitor progress of actions from previous meetings and to review the Committee's forward work programme.

6 **INVESTMENT MANAGER ISSUES, PERFORMANCE AND ASSET/LIABILITIES UPDATE** (Pages 25 - 50)

Purpose of the report: This report is a summary of all manager issues that need to be brought to attention of the Pension Fund Committee, as well as an update on investment performance and the values of assets and liabilities.

7 **PRIVATE EQUITY INVESTMENT: PERFORMANCE REVIEW** (Pages 51 - 72)

Purpose of the report: The Surrey Pension Fund has a commitment to invest 5% of the fund in private equity. This is achieved by investing in funds of funds and direct funds, managed by a number of private equity specialists.

The Pension Fund Committee reviews the private equity strategy. This report is a review of the investment performance of the private equity portfolio.

8 **CORPORATE GOVERNANCE SHARE VOTING** (Pages 73 - 88)

Purpose of the report: This report provides a summary of the Fund's share voting process in Q1 of 2018/19 (1 April 2018 to 30 June 2018). The report also includes a class action against BHP who is a firm Surrey had investment in.

9 **CASHFLOW ANALYSIS** (Pages 89 - 92)

Purpose of the report: A cash-flow analysis allows the Fund to ascertain a projection as to when benefit payments may exceed income. This information can influence both the investment and funding strategy.

10 **VALUATION REPORT 2019** (Pages 93 - 106)

Purpose of the report: This report provides an introduction to the triennial valuation including a draft project plan from the Fund actuary, Hymans Robertson.

11 **GOVERNANCE REVIEW** (Pages 107 - 110)

Purpose of the report: As part of the governance and oversight of the pension fund, a regular review and update to the governance framework, policies and procedures is essential to ensure that the Fund is compliant with latest legislation, regulations and good practice.

There have been significant developments in the LGPS over the past three years, which make a review of the governance of the Fund necessary and appropriate.

This report sets out the scope and timetable for a governance review which, if approved by the Committee, will be jointly undertaken by officers and appointed specialist advisors.

12 ANNUAL REPORT/ STATEMENT OF ACCOUNTS (Pages 111 - 318)

Purpose of the report: The Pension Fund Committee role is to approve the Annual report which contains the audited statement of accounts together with other information about the Fund's performance during 2017/18. The annual report is included in Annex 1.

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 (Annex 2).

13 LOCAL PENSION BOARD REPORT (Pages 319 - 342)

Purpose of the report: This report is a summary of administration and governance issues reviewed by the Local Pension Board at its meeting 25 July 2018 that need to be brought to the attention of the Pension Fund Committee.

14 EXCLUSION OF THE PUBLIC

Recommendation: 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 the relevant paragraphs of Part 1 of Schedule 12A of the Act.

PART TWO PRIVATE

15 NATIONAL POOLING UPDATE (Pages 343 - 352)

Purpose of the report: The Border to Coast Pension Partnership (BCPP) ambition is to establish a fully regulated asset management company that is ready to accept the transition of assets, as required by government. The working timeline is expected to commence in transitioning Surrey Pension Fund assets from quarter four in 2018.

16 PUBLICITY OF PART 2 ITEMS

To consider whether the item considered under Part 2 of the agenda should be made available to the Press and public.

17 DATE OF NEXT MEETING

The next meeting of the Surrey Pension Fund Committee will be on 16 November 2018.

Joanna Killian
Chief Executive
Published: Thursday 6 September 2018

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MINUTES of the meeting of the **SURREY PENSION FUND COMMITTEE** held at 10.00 am on 8 June 2018 at Members Conference Room, County Hall, Kingston upon Thames, Surrey KT1 2DN.

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

Elected Members:

* Mr Tim Evans (Chairman)
* Mr Ben Carasco (Vice-Chairman)
* Ms Ayesha Azad
* Mr John Beckett
* Mr David Mansfield
* Mrs Hazel Watson

Ex officio Members:

Mr David Hodge CBE, Leader of the Council
Mr Peter Martin, Chairman of the Council

Co-opted Members:

* Margaret Janes, Employers
* Philip Walker, Employees
* District Councillor Tony Elias

26/18 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS [Item 1]

There were no apologies received.

27/18 MINUTES OF THE PREVIOUS MEETING 26 MARCH 2018 [Item 2]

The Minutes were approved as an accurate record of the previous meeting.

28/18 DECLARATIONS OF INTEREST [Item 3]

There were none.

29/18 QUESTIONS AND PETITIONS [Item 4]

1. Members of the public noted the response to questions submitted which are attached to the minutes as **Annex 1**. The questioners asked the following supplementary questions in response:

    a. *Cllr Jonathan Essex, on behalf of Sarah Finch:* Please can the Committee request the LAPFF to confirm what transition plans exist for oil and gas investments to a 1.5° warming scenario and provide evidence that this approach has delivered a reduction in carbon exposure to date.

b. *Question By Sally Elias:* It was noted that other comparable funds and organisations were looking at disinvestment in fossil fuels. Does the Surrey Pension Fund invest in Suncor with its tar sands interests and what does it take to convince the Committee to take your funds out of such an environmentally damaging business?

c. *Question by Vicki Elcoate:* I understand that Surrey CC Pension fund has over £45m invested in BP. Are Pension Fund members aware that BP holds nearly a 20% stake in Russian state oil company Rosneft and sits on its board? This is despite the Russian oil giant having one of the world's worst records on safety and spills. It also no longer seems very sound in terms of investment to have your pension fund associated with the Russian regime. What does it take to convince the Board that the fossil fuel business involves dirty money and it's time to get out?

d. *Question by Janet Baker on behalf of Pat Horitz:*

On the question of fiduciary responsibility, would the SPF committee bear in mind that the increasing support for moving investments out of fossil fuels and into Socially Responsible Investments and that investment in SRIs is bringing healthy returns capable of outperforming conventional investments?

e. *Question by Stephen McDonald:* I referred firstly to an extract from a LAPFF report produced in conjunction with Carbon Tracker which states in its' introduction, "most oil companies seem to plan their business on the assumption that the action on climate change needed to deliver a 2deg C scenario will not emerge in the foreseeable future"

I added, "the SPF know this only too well as the Shell website reveals some 21 new fossil fuel extraction projects supported by c. £ 60 million of Surrey Pension Fund investments"

My question was, "If we assume that the Pension Fund Trustees supported by a range of different Pension professionals are aware of the outcomes of their investment decisions, could the committee tell me what is the environmental outcome of the £ 130 million currently invested in the fossil fuel industry?"

It would make the point that an environmental outcome would be expressed in environmental terms; temperature, flooding, extreme weather events, sea level rise, ecosystem breakdown etc.

This question was not answered in section 4 of the meeting (questions and petitions) and was referred forward to the carbon asset exposure review section. Nor was it answered in

this section.

It was noted that a response to these supplementary questions would be provided in writing after the meeting and attached to the minutes as **Annex 2**.

30/18 FORWARD PLAN AND ACTION TRACKING [Item 5]

Declarations of interest:

None

Witnesses:

Neil Mason, Head of Pensions
Richard Plummer, Democratic Services Officer

Key points raised during the discussion:

1. Members noted and approved the forward plan and action tracker.

31/18 PENSION FUND BUSINESS PLAN 2017/18: OUTTURN REPORT [Item 6]

Declarations of interest:

None

Witnesses:

Neil Mason, Head of Pensions

Key points raised during the discussion:

1. Members noted the report and provided their congratulations to the pensions team for their achievements and progress on the Business Plan objectives.

Resolved:

That the Committee:

1. Noted the achievements and progress made with regard to the Business Plan objectives shown in Annex 1 in respect of the 2017/18 financial year.

32/18 CARBON ASSET EXPOSURE REVIEW [Item 7]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Neil McIndoe, Trucost
Yohan Hill, Trucost

Key points raised during the discussion:

1. Officers introduced the report and a presentation with representatives from Trucost was given to provide the committee a breakdown of the carbon asset exposure of the fund.

2. The representatives from Trucost explained that they had undertaken similar benchmarking work with 20 other Local Government Pension Schemes (LGPS) to ascertain the risk of climate change and carbon related assets. It was noted that all data used was within two years of the current date to ensure relevance.

3. Members questioned how Trucost calculated the carbon footprint of organisations in which the Fund invests. Trucost representatives explained that emission rates disclosed by companies were used in calculations, but noted that in cases where data were not available, rates were modelled using well established methodology.

4. Members asked whether the carbon footprint of the final product of oil and gas companies was included as part of the footprint. Trucost representatives noted that this was not included but that the use of the end product was included in other company footprints.

5. It was noted that oil, gas and materials companies in which the Surrey Pension Fund invests a significant carbon apportionment in the Fund's investments.

6. Members queried whether the information presented by Trucost regarding carbon footprint impact could be analysed alongside the performance of investments. Officers noted that this comparison would be included as part of future Investment Manager Reports to the Committee to allow analysis and to determine the appropriateness of the investments.

7. Members questioned benchmarks relating to investment in high carbon footprint industries and whether there was a potential for increasing the thresholds for benchmarks to reduce investments in high carbon footprint assets. Advisors noted that the Fund could employ different benchmarks to encourage this that the service could employ.

Resolved:

That the Pension Fund Committee:

1. Noted the report

33/18 EQUITY STRATEGY REVIEW [Item 8]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Steve Mitchell, Mercer
Anthony Fletcher, Allenbridge

Key points raised during the discussion:

1. Advisors noted that the Committee was required to review the balance between Global and UK equities, the allocation to RAFI and consider investments in low carbon assets and any potential changes to the balance between active and passive investments.

2. Advisors suggested that the balance between active and passive investments should remain unchanged. It was noted that the weighting between active and passive was similar in Surrey to other comparable LGPS's.

3. Advisors and officers explained that the transfer of assets to the Border to Coast Pensions Partnership (BCPP) made an equity strategy review timely and that it was important for the Fund to consider long term strategy before transfer.

4. It was noted that UK equities were heavily weighted towards oil and gas companies and that stock concentration was significantly higher in UK equities than in global equities. Advisors noted that there was a proposal to reduce UK equities to 20% of the allocation. It was also suggested that the allocation would be actively managed by the BCPP. Advisors noted that there was an agreement that UK equities should be actively managed to maximise returns.

5. Advisors highlighted that MSCI Low Carbon Target Index was the preferred low carbon index.

6. Advisors suggested that Trucost could undertake a peer analysis of comparable LGPS funds to ascertain their investment in low carbon assets and gain an indication on where the Surrey fund is in comparison with these.

7. Members noted that the Fund could work to guide the BCPP towards investment in low carbon assets by highlighting the issue as a key priority for the fund.

8. Members questioned advisors on equity protection and whether the next steps were appropriate. Officers noted that the triggers were in place and advisors suggested that protection be proceeded to stage three. It was stressed that there was a continued strong rationale for equity protection.

Resolved:

That the Pension Fund Committee:

1. Approved the reduction in UK equities in the portfolio from the current 46% to 20%, all in the active portion of the portfolio.

2. Retained the current balance in the equity portfolio of 38% passive and 62% active.

3. Approved the balance within the passive portfolio to be 16% global RAFI, 16% MSCI Global Low Carbon Target Index and 6% emerging markets.

4. Approved further work for officers, Mercer and the Independent Advisor to consider the appropriate balance of the active global/regional element of the equity portfolio and negotiate with BCPP to enable this asset mix to be realised through the BCPP global or regional sub fund offerings.

5. Noted the progress on the downside equity protection strategy.

34/18 INVESTMENT MANAGER ISSUES AND PERFORMANCE AND ASSET/LIABILITIES UPDATE [Item 9]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Steve Mitchell, Mercer
Anthony Fletcher, Allenbridge
Sheila Little, Head of Finance

Key points raised in the discussion:

1. Advisors noted that there were concerns with the performance of Aviva and that the stated objective of 4% performance levels was unlikely to be accomplished. Aviva to be put on watch for the foreseeable future.

2. Officers explained that they required power of attorney from the committee to act in the repatriation of Taiwanese Dollars (NTD) and such power required the authorisation of the Pension Fund Committee.

3. Members questioned whether the service would review other overseas positions. Officers noted that the Fund team was discussing this issue with the custodian and that an update would be brought back to the Committee when this was concluded.

Resolved:

That the Pension Fund Committee:

1. Noted the report.

2. Authorised the Power of Attorney for Deloitte (Taiwan) to act on the Surrey Fund's behalf as a tax agent in Taiwan and where appropriate in facilitating the repatriation of funds.

35/18 INVESTMENT STRATEGY REVIEW AND STATEMENT [Item 10]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Steve Mitchell, Mercer
Anthony Fletcher, Allenbridge
Sheila Little, Head of Finance

Key points raised in the discussion:

1. Members made note of the Investment Strategy Statement and made no additional comments. It was noted prior to the meeting that there were no changes to the statement since the last review.

Resolved:

That the Pension Fund Committee:

1. Noted the latest Investment Strategy Statement.

36/18 CASHFLOW ANALYSIS [Item 11]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Steve Mitchell, Mercer
Anthony Fletcher, Allenbridge
Sheila Little, Head of Finance

Key points raised in the discussion:

1. Members questioned the Quarter 3/4 total contributions and why they had significantly increased. Officers explained that the income management team had performed a reconciliation of contribution balances whereby they allocated cash to appropriate months had not been undertaken in the previous quarters. It was also suggested that an additional reason for the high increase was as a result of some employers paying the deficit contribution at the year-end.

2. Officers noted that they would bring quarterly reviews to the Committee to aid in the review of trends.

Resolved:

That the Pension Fund Committee:

1. Noted the cash-flow position for quarters three and four.

37/18 PENSION FUND INTERNALLY MANAGED CASH STRATEGY [Item 12]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Steve Mitchell, Mercer
Anthony Fletcher, Allenbridge
Sheila Little, Head of Finance

Key points raised in the discussion:

1. Officers highlighted the report, noting that unutilised cash could be better used by fund managers to yield greater return. It was proposed that the fund set up a collar for future investments of around £20 million. Officers noted that they would seek advice as to where to invest any cash that was outside of the £20 million collar.

Resolved:

That the Pension Fund Committee:

1. Approved the Pension Fund Internally Managed Cash Strategy

2. Will review the strategy on quarterly basis.

38/18 LOCAL PENSION BOARD REPORT [Item 13]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Graham Ellwood, Vice-Chair Surrey Local Pension Board

Key points raised in the discussion:

1. The Vice-Chairman of the Board explained that the Board had noted that the administration performance had improved in the last quarter.

2. The Vice-Chairman of the Board noted with concern the administration and monitoring of members in danger of breaching the annual or

lifetime allowances and stressed that the Board would be working to address this in future. Officers noted that this was becoming a national issue and that, while it was the individual's responsibility to resolve, that appropriate information should be provided to help resolve the issue.

3. The Vice-Chairman of the Board noted that the Board would be working with officers on 50/50 schemes to work on how to better publicise these schemes to members of the fund as an option.

4. Members questioned whether the Board had identified whether there were any substantial gaps in the CIPFA benchmarking report. Officers noted that this report undertook administrative benchmarking and that few other funds participated in this, limiting the level of results.

5. Officers explained that there were recommended changes to the risk register which were highlighted in the Board report, which would be implemented by the service.

Resolved:

That the Pension Fund Committee:

1. Approved the recommendations from the Local Pension Board in regard to the Administration Performance Report.

2. Approved the recommendations from the Local Pension Board in regard to the Risk Registers.

39/18 CORPORATE GOVERNANCE SHARE VOTING [Item 14]

Declarations of interest:

None

Witnesses:
Neil Mason, Head of Pensions
Steve Mitchell, Mercer
Anthony Fletcher, Allenbridge
Sheila Little, Head of Finance

Key points raised in the discussion:

1. Officers and advisors introduced the report, noting that there were no significant updates from the previous report presented to the Committee. There were no additional comments by Members.

Resolved:

That the Pension Fund Committee:

1. Noted the report.

40/18 EXCLUSION OF THE PUBLIC [Item 15]

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 the relevant paragraphs of Part 1 of Schedule 12A of the Act.

PART TWO – IN PRIVATE

41/18 NATIONAL POOLING UPDATE [Item 16]

Declarations of interest:

None

Witnesses:
John Harrison, Border to Coast Partnership

Key points raised during the discussion:

1. A discussion was held between representatives of the Border to Coast Partnership and the Committee regarding the future transition of the Surrey Pension Fund portfolio to the BCPP and the conditions that were required relating to this transfer.

Resolved:

That the Committee:

1. Noted the report.

2. Approved in principle, the transition of the UK equity portion of the Surrey Pension Fund portfolio to the Border to Coast Pensions Partnership (BCPP) national pool when it has been established, assuming that the “necessary conditions” of governance have been satisfied.

3. Approved the delegation of authority to the Director of Finance (Section 151 officer), in consultation with the Chairman of the Pension Fund Committee, to transition the UK equity portion of the Surrey Pension Fund portfolio to the BCPP, assuming that the “necessary conditions” of governance have been satisfied.

42/18 PUBLICITY OF PART 2 ITEMS [Item 17]

The Committee concluded that the items referred to in the Part Two annex should not be made available to the public at this time.

43/18 DATE OF NEXT MEETING [Item 18]

The date of the meeting was NOTED.

Meeting ended at: 1.37 pm

Chairman

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1. **Question Submitted by Sarah Finch – 07/05/2018**

   The Local Authority Pension Fund Forum, of which the SPF is a member, has previously stated that the best way to influence the reduction in fossil fuel extraction is by engagement with those companies who operate in this business. I am concerned that the evidence does not support this view.

   RESPONSE:
   For companies in all sectors, the Local Authority Pension Fund Forum (LAPFF) continues to press for alignment of business models with a 1.5 to 2°C scenario, and to push for an orderly low carbon transition, with an initial time horizon of 2020.

   The LAPFF recognises the issue of stranded assets and continued fossil fuel extraction as a collective investment risk for all asset owners and as an engagement and policy priority.

   For oil and gas companies, an important engagement and voting focus is the restriction of capital expenditure (capex) on high cost resource extraction and promotion of the return of any additional cash generated to shareholders.

   For companies with coal operations, no new resources should be exploited. Collaborative engagement with UK-listed integrated miners, Rio Tinto, Anglo-American and Glencore continues, following the strategic resilience resolutions passed at 2016 AGMs, for which a number of member funds were co-filers.

   Monitoring of progress and outcomes includes LAPFF's participation in the Transition Pathway Initiative, which aids understanding of where companies are placed in the transition to a low carbon economy and their competence to manage this transition.

   LAPFF supports the recommendations of the Financial Stability Board's (FSB) Task Force on Climate Disclosure (TFCD) report and considers all market participants should be encouraged to aim for full implementation. The LAPFF has long promoted mandatory climate risk reporting. The mechanism for this is already in place under the Companies Act requirements for companies to report financially material risks in their annual report. LAPFF has also suggested that in positioning themselves for the required low carbon future, companies should disclose a transition plan.

   Recently the LAPFF has partnered with the '50-50' initiative to engage with companies on climate risk and encourage climate resilience planning.

   In conclusion, as shown above, we believe that engagement continues to be an effective and appropriate approach to reducing carbon exposure.

2. **Question Submitted by Barry Staff – 02/05/2018**

   Do those members of the committee who were democratically elected through local elections feel that they have a moral and ethical responsibility to their electorate to stop investing in fossil fuels, the use of which is the overwhelming cause of devastating global heating?

   RESPONSE:

   The 2016 Investment Regulations sets out the following key elements that must guide an administering authority's responsible investment policy:-

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- Schemes should make the pursuit of a financial return their predominant concern;
- Schemes should consider any factors that are financially material to the performance of their investments, including social, environmental and corporate governance factors;
- They may also take purely non-financial considerations into account provided that doing so would not involves significant risk of financial detriment to the fund and where they have good reason to think that scheme members would support their decision.

The Surrey Pension Fund is proactive in its approach to the monitoring of climate change related assets.

At its meeting on 10 November 2017, the Pension Fund Committee considered the recommendation of the Surrey Local Pension Board to establish the Pension Fund's exposure to climate change and carbon risk through the commissioning of a carbon audit of the Fund's portfolios.

As a result of this Local Board recommendation a carbon footprint audit has been carried out, the results of which will be presented at the meeting of 8 June 2018.A summary of the results of this audit show that the Surrey Pension Fund equity portfolio has a lower carbon footprint than its benchmark.

Further to this the committee will continue to consider further mitigating its carbon footprint, while remaining consistent with its statutory obligations.

3. **Question Submitted by Sally Elias – 09/05/2018**

Why will the SPF committee not follow the logical and ethical examples of other investment funds in the UK and around the world, who are increasingly divesting from fossil fuels?

RESPONSE:

Refer to the answer given to Barry Staff

4. **Question Submitted by Vicky Elcote – 21/05/2018**

I would like to know why the committee continues to invest very large sums of pension funds (£ 130 million as reported at the meeting of 09 Feb) in fossil fuel companies in searching for further deposits, despite the fact that the majority of known reserves will be stranded and left in the ground if the increase in global temperatures is to be limited to 2 degrees Celsius above pre-industrial levels, let alone limited to1 ½ degrees above them, as was agreed in the UN climate talks in Paris in December 2015.

RESPONSE:

Refer to the answer given to Barry Staff

5. **Question Submitted by Stephen McDonald – 24/05/2018**

Please could the Committee explain to me how they justify continued pension fund investment investment into fossil fuels, particularly as we know that 1) There is no

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legal barrier to divestment and 2) it is well known and understood that fossil fuel investments are not required in order to provide strong returns for pension members

RESPONSE:

Refer to the answer given to Barry Staff

6. **Question Submitted by Pat Horitz – 25/05/2018**

What is the committee's future investment strategy in relation to fossil fuel companies, bearing in mind the major contribution fossil fuels are making towards the highly damaging increase in global temperatures, and the responsibility each one of us has for reducing the impact as far as we can?

RESPONSE:

Refer to the answer given to Barry Staff

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Supplementary questions submitted on 8 June 2018

1. *Cllr Jonathan Essex submitted by on behalf of Sarah Finch:* Please can the Committee request the LAPFF confirm what transition plans exist for oil and gas investments to a 1.5C warming scenario and provide evidence that this approach has delivered a reduction in carbon exposure to date.

   RESPONSE from the LAPFF:

   "To date, few oil and gas companies have evidenced specific transition plans for a 1.5° warming scenario, the emphasis has been on first getting companies to present scenarios setting out their analysis, then pushing for them to stress test these. These are measures that a large body of institutional shareholders are willing to support.

   As an example, the shareholder resolutions at the 2015 AGMs of BP and Shell, co-filed by many LAPFF funds, asked the companies to set out the asset portfolio resilience to the International Energy Agency's (IEA's) scenarios including the '450 Scenario'. This was supported by nearly all shareholders. Engagement is now focussed on the IEA sustainable development scenario, issued in November 2017 which reduces CO_2 emissions in line with the objectives of the Paris agreement.

   The Forum considers that in positioning themselves for the required low carbon future, oil and gas companies should disclose a transition plan. This is promoted through engagement and voting recommendations to members. As an example, LAPFF issued voting alerts to member funds for the 2016, 2017 and 2018 Chevron AGMs supporting shareholder resolutions on the company adapting its business model and disclosing a strategic business transition plan to shareholders. However, fewer institutional shareholders are willing to support such resolutions and the most recent resolution only garnered 8% support.

   There is evidence for reduction in carbon exposure at a number of companies, but it is not clear that this can be directly linked to specific transition plans. However, statements by companies have indicated they are aware of the challenge and are taking certain steps, for example in November 2017, Shell issued an 'ambition' to cut the net carbon footprint of its energy products by around half by 2050. BP has a focus on nearer term targets, looking to keep its methane intensity at 0.2% capped at 0.3%. The issue of controlling methane emissions had been raised previously in engagement with the company, as of course the switch to gas from other non-renewable fuels is only climatically beneficial if leakages are sufficiently small.

   LAPFF is a member of the Climate Action 100+ initiative. One of the three goals of this initiative is to engage with companies to reduce emissions across the value chain.

   To enable member funds to tackle carbon risk exposure, LAPFF has issued a 'Climate Change Investment Policy Framework' to help guide their policy approach to current and future investment risks and opportunities that result from the impacts of climate change."

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2. *Question submitted by Sally Elias:* It was noted that other comparable funds and organisations were looking at disinvestment in fossil fuels. Does the Surrey Pension Fund invest in Suncor with its tar sands interests and what does it take to convince the Committee to take your funds out of such an environmentally damaging business?

   RESPONSE:

   The Surrey Pension Fund currently invests c£6.5m in Suncor through its global portfolio with the Newton Global Equity Fund.

   Consistent with our ESG policy, the Fund believes that the best way to influence companies is through engagement; therefore the Surrey Pension Fund will not divest from companies principally on social, ethical or environmental reasons.

3. *Question submitted by Vicki Elcoate:* I understand that Surrey CC Pension fund has over £45m invested in BP. Are Pension Fund members aware that BP holds nearly a 20% stake in Russian state oil company Rosneft and sits on its board? This is despite the Russian oil giant having one of the world's worst records on safety and spills. It also no longer seems very sound in terms of investment to have your pension fund associated with the Russian regime. What does it take to convince the Board that the fossil fuel business involves dirty money and it's time to get out?

   RESPONSE:

   The Surrey Pension Fund's investment strategy is incorporated in its Investment Strategy Statement within the regulatory and legal context. This includes our ESG policy and the adoption of the Responsible Investment Policy (RIP) of Border to Coast Pensions Partnership (BCPP). The RIP of BCPP explicitly states the following approach:

   "The best way to influence companies is through engagement; therefore BCPP will not divest from companies principally on social, ethical or environmental reasons. As responsible investors, the approach taken will be to influence companies' governance standards, environmental, human rights and other policies by constructive shareholder engagement and the use of voting rights. The services of specialist providers may be used when necessary to identify issues of concern."

   In establishing these policies, both the Surrey Pension Fund Committee and BCPP have regard to the views of the Local Authority Pension Fund Forum and it remains our belief that divestment alone is a blunt tool that deprives investors of leverage to influence companies.

4. *Question submitted by Janet Baker on behalf of Pat Horitz:*On the question of fiduciary responsibility, would the SPF committee bear in mind that the increasing support for moving investments out of fossil fuels and into Socially Responsible Investments and that investment in SRIs is bringing healthy returns capable of outperforming conventional investments?

   RESPONSE:

   The Committee, with guidance from its investment consultant and independent advisor, is committed to investigate all viable investment options.

Under current consideration is a new investment to funds with a focus on sustainable or renewable energy.

5. *Question submitted by Stephen McDonald:* I referred firstly to an extract from a LAPFF report produced in conjunction with Carbon Tracker which states in its' introduction, "most oil companies seem to plan their business on the assumption that the action on climate change needed to deliver a 2deg C scenario will not emerge in the foreseeable future"

   I added, "the SPF know this only too well as the Shell website reveals some 21 new fossil fuel extraction projects supported by c. £ 60 million of Surrey Pension Fund investments"

   My question was, "If we assume that the Pension Fund Trustees supported by a range of different Pension professionals are aware of the outcomes of their investment decisions, could the committee tell me what is the environmental outcome of the £ 130 million currently invested in the fossil fuel industry?"

   It would make the point that an environmental outcome would be expressed in environmental terms; temperature, flooding, extreme weather events, sea level rise, ecosystem breakdown etc.

   This question was not answered in section 4 of the meeting (questions and petitions) and was referred forward to the carbon asset exposure review section. Nor was in answered in this section.

   RESPONSE:

   The Surrey Pension Fund does not believe it is possible to give a reliable and quantifiable answer within the terms of this question with specific reference to the Surrey Pension Fund's holdings.

   Environmental outcomes are not associated with a specific level of investment in one sector. These outcomes are linked to other sectors, including the transport and energy utility sectors as well as other high emitting industries such as steel and cement.

   However, you will be aware that a wider scoped carbon footprint audit was recently carried out and the Surrey Pension Fund continues to actively manage this risk through its portfolio.

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Surrey Pension Fund Committee – ACTION TRACKING

ACTIONS

Number	Meeting Date	Item	Recommendation / Action	Action by whom	Action by when	Action update
P2/18	09/02/2018	Risk Registers: Pension Fund And Administration	That a regular update be provided to the committee on a quarterly basis including a breakdown of key risks and a detailed list of scenario plans	Head of Pensions	September 2018	**This has been added to the forward plan**
P4/18	08/06/2018	Pension Fund Internally Managed Cash Strategy	The Committee review the Cash Strategy on a quarterly basis.	Head of Pensions	September 2018	**This has been added to the forward plan**

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Surrey Pension Fund Committee Forward Plan

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Date	Standing items	New items
14 September 2018	• National pooling update • Investment Manager Issues • Local board update (to include): - *Administration update* - *Governance update* - *Pension fund and administration risk registers* - *Share voting* • Cash-flow analysis • Voting and class action update	• Valuation Introductory Report • Private equity report • Annual report • Governance review Training to be provided by the LAPFF
16 November 2018	• National pooling update • Investment Manager Issues • Local board update (to include): - *Administration update* - *Governance update* - *Pension fund and administration risk registers* - *Share voting* • Cash-flow analysis • Voting and class action update	• Training, including self-assessment • Valuation update • Responsible Investment Policy Update • CEM performance analysis report • Governance review • Investment strategy review update (global mandate) • Investment strategy statement update RIP training to be provided by BCPP and Environment Agency. Actuarial training to be provided by Hymans
8 February 2019	• National pooling update	

Surrey Pension Fund Committee Forward Plan

	• Investment Manager Issues • Local board update (to include): - *Administration update* - *Governance update* - *Pension fund and administration risk registers* - *Share voting* • Cash-flow analysis • Voting and class action update	
7 June 2019	• National pooling update • Investment Manager Issues • Local board update (to include): - *Administration update* - *Governance update* - *Pension fund and administration risk registers* - *Share voting* • Cash-flow analysis • Voting and class action update	

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **PRIVATE EQUITY INVESTMENT: PERFORMANCE REVIEW**

SUMMARY OF ISSUE:

The Surrey Pension Fund has a commitment to invest 5% of the fund in private equity. This is achieved by investing in funds of funds and direct funds, managed by a number of private equity specialists.

The Pension Fund Committee reviews the private equity strategy. This report is a review of the investment performance of the private equity portfolio.

RECOMMENDATIONS:

It is recommended that:

1 The Committee note the Fund's Private Equity holdings, respective funds investment performance and review from the Funds investment consultant and independent investment adviser.

2 The Fund continue to commit to drawdowns of the existing private equity schemes, and consider new opportunities to the Pension Fund Committee for approval as and when they arise.

3 Approve the recommendation of the Fund's investment consultant, Mercer, to invest a further £30-40m in new private equity fund with its defined characteristics.

4 Approve for officers to work with Mercer and the independent advisor to research the market for appropriate private equity providers with these defined characteristics and bring a further recommendation to the pension fund committee.

REASON FOR RECOMMENDATIONS:

A solid framework of review is required in order to benefit from this long term asset category.

DETAILS:

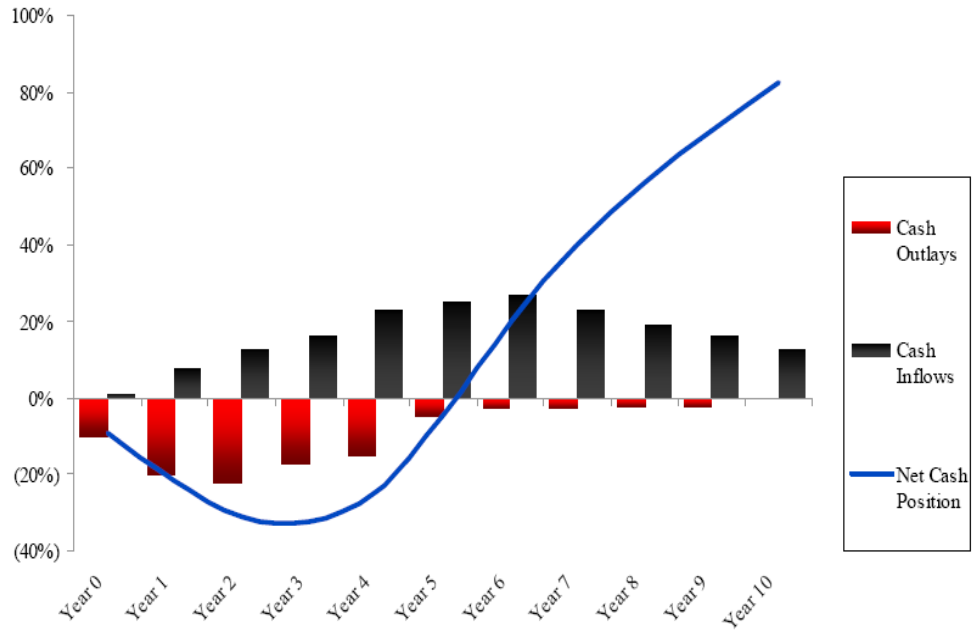
Background

1 Private equity investments are equity investments in private companies.

2 It is a long term investment to provide capital to privately traded companies to fund growth or liquidity to certain shareholders.

3 The typical lifetime of a private equity fund in the region of ten years plus from an investment (drawdown) phase to the final distribution phase, with the returns weighted to the second half of the fund life.

4 Returns in the early years tend to be negative as capital is paid out to make investments, cover associated transaction costs and pay management fees, leading to the J-Curve effect (see graph below):



Current Position

5 The detailed position on commitments and cash invested as at 31 March 2018 is shown in Annex 1 and is summarised as follows:

	Value (£m)	% of Fund
Total Commitment	444	11.0%
Investment drawn (paid in capital)	300	7.4%
Commitment Outstanding	144	3.6%

	Value (£m)	% of Fund
Distributions Received	175	4.3%
Fair Value of Remaining Investments	245	6.1%
Distributions + Remaining Investments	420	10.4%

Where relevant valuations converted to £ equivalent as at 31 March 2018

6 Based on investment assets of £4,030m as at 31 March 2018, 9.5% of the Fund is committed to private equity investments. The actual level of investment (based on the Fair Value of the remaining investments) is 6.1% of the Fund versus the asset allocation target of 5.0% but this will gradually fall back in line with the allocation target, when future distributions are received from existing holdings.

7 The Fund's independent advisor has produced a summary of the Fund's existing private equity holdings and an analysis of the benefits. This is shown as Annex 2.

Performance Measurement

8 An updated Public Market Equivalent (PME) calculation for each scheme's asset value to 31 March 2018 is shown in Annex 3.

9 As at 31 March 2018, the calculated internal rate of return (IRR) for the private equity cash flows portfolio of partnerships currently active is 7.7% versus a benchmark from the MSCI World Index of 12.4%, an underperformance of 4.7%. The current target performance return against the benchmark is +5%.

New private equity investment

10 In order to ensure that the Fund remains consistent to its target asset allocation of 5% to private equity it should make regular investments. This is to ensure that a time / vintage diversification is achieved and that the Fund is positioned to take advantage of opportunities in a structured way.

11 In addition, as the Fund is currently in the process of receiving distributions from its existing private equity holdings, the value of the private equity portfolio will erode over time and fall below the target allocation of 5%.

12 The Fund's investment consultant, Mercer, have produced a report (included as Annex 4) which recommends a theme of private equity for new investment, within the context of its existing holdings.

13 The recommendation defines the following characteristics as being desirable:

- Global
- A preference for infrastructure
- A focus on sustainable or renewable energy
- Consider complementarity with strategies being implemented by Border to Coast partner funds

CONSULTATION:

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

RISK MANAGEMENT AND IMPLICATIONS:

15 Risk related issues are contained within the report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

16 Financial and value for money implications are contained within the report.

DIRECTOR OF FINANCE COMMENTARY

17 The Acting Section 151 Officer is satisfied that all material, financial and business issues and possibility of risks have been considered, and that private equity has been a good performing asset class for the pension fund.

LEGAL IMPLICATIONS – MONITORING OFFICER

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

EQUALITIES AND DIVERSITY

19 The review of the Fund's private equity programme will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

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

WHAT HAPPENS NEXT

21 The following next steps are planned:

- Officers to work with Mercer and the independent advisor to research the market for appropriate private equity providers with these defined characteristics and bring a further recommendation to the pension fund committee
- Continued monitoring of private equity fund partnerships and a performance review report to be brought to the committee on an annual basis

Contact Officer:
Neil Mason, Head of Pensions

Consulted:
Pension Fund Committee Chairman

Annexes:
Annex 1: Detailed position on commitments and cash invested at 31 March 2018
Annex 2: Summary report from the Fund's Independent Advisor
Annex 3: Public Market Equivalent (PME) calculation for each scheme's asset values to 31 March 2018
Annex 4: Mercer recommendation report

Sources/background papers:
Private equity manager reports

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 versus Paid In Capital	IRR
Sterling Funds			£	£	£	£	£	£		
HG Capital	HG 5	2006	7,752	105	7,857	10,727	891	11,618	1.7	11.50%
HG Capital	HG 6	2009	9,392	608	10,000	11,574	5,267	16,841	1.9	11.80%
HG Capital	HG7	2013	14,158	842	15,000	5,353	15,926	21,279	1.5	16.40%
Capital Dynamics	LGPS Collective 2016/2017	2016	2,000	6,000	8,000	120	2,010	2,130	1	7.30%
Capital Dynamics	LGPS Collective 2017/2018	2017	560	7,440	8,000	0	576	576	1	3.70%
Living Bridge	LIVING BRIDGE 4 LP	2013	1452	683	2,135	607	1425	2,032	1.9	18.00%
Living Bridge	LIVINGBRIDGE ENTERPRISE 1 LP	2013	6,801	3,199	10,000	2,843	6,675	9,518	1.4	17.00%
Darwin Property Management	Darwin Property Fund	2013	60,000	0	60,000		73,508	73,508		
Euro Funds			€	€	€	€	€	€		
SL Capital	ESP 2006	2006	13,745	1255	15,000	16,004	3,096	19,100	1.4	5.70%
SL Capital	ESP 2008	2008	13,922	1078	15,000	10,349	9,803	20,152	1.4	9.60%
SL Capital	ESP II	2004	9,323	677	10,000	15,175	229	15,404	1.7	12.40%
SL Capital	ESF I	2011	11,654	5846	17,500	1082	12,930	14,012	1.2	6.10%
Dollar Funds			$	$	$	$	$	$		
BlackRock	Vesey Street I	2001	4,750	250	5,000	8,338	109	8,447	1.8	13.21%
BlackRock	Vesey Street II	2003	4,675	325	5,000	8,118	389	8,507	1.7	10.40%
BlackRock	Vesey Street III	2005	15,400	2,100	17,500	19,469	2,057	21,526	1.4	4.66%
Goldman Sachs	GS PEP 2000 LP	2000	9,311	189	9,500	16,398	318	16,716	1.7	13.90%
Goldman Sachs	GS PEP 2004 LP	2004	9,808	192	10,000	14,836	793	15,629	1.5	7.40%
Goldman Sachs	GS PEP 2005 LP	2006	16,136	864	17,000	16,702	4,673	21,375	1.3	3.90%
Goldman Sachs	GS PEP X LP	2008	14,926	3074	18,000	16,942	9,302	26,244	1.6	11.10%
Goldman Sachs	GS PEP XI LP	2011	31,602	8,398	40,000	20,364	33,716	54,080	1.5	18.10%
Goldman Sachs	GS Vintage VI	2013	12,418	7,582	20,000	11,248	10,030	21,278	1.4	14.40%
Goldman Sachs	GS Vintage VII	2016	20,794	29,206	50,000	4,872	20,006	24,878	1.2	TBC
Goldman Sachs	WS EUROPEAN INFRASTRUCTURE LP	2017	4,600	15,400	20,000	0	4,449	4449	1.0	TBC
Pantheon	Pantheon Global Infrastructure	2017	11,200	48,800	60,000	0	11,300	11,300	1.0	TBC
Capital Dynamics	Clean Energy	2012	24,225	675	24,900	1,662	23,063	24,725	1	0.49%
SL Capital	SOF I Feeder	2014	16,077	3,923	20,000	8,312	13,084	21,396	1.3	13.60%
SL Capital	SOF II Feeder	2014	11,750	8,250	20,000	1,435	16,155	17,590	1.4	25.90%
SL Capital	SOF III Feeder	2017	10,290	34,710	45,000	0	13,004	13,004	1.2	>100%
TOTAL (GBP)			**300,535**	**143,658**	**444,193**	**174,901**	**245,168**	**420,069**		

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Review of Private Equity and Infrastructure Investments

PREPARED FOR:

Surrey County Council Pension Fund

14TH SEPTEMBER 2018

Attendees

Tim Evans, Neil Mason (Surrey) and Anthony Fletcher (MJ Hudson Allenbridge)

Date of meeting 5th July 2018

Background

The Surrey Pension Fund has a long history of investing in Private Equity Funds and has more recently begun to invest in Infrastructure Funds. The Fund began making investments in 1999, to date the funds have all been closed-end and has a number of funds that have been or are very close to be fully realised, ie they have completed their life cycle, the committed capital has been drawn, invested, the investments sold and the capital returned to Surrey, either in the form of a capital or income gain.

Unlike publicly quoted equities, which are listed and traded openly on a Stock Exchange, where the price is known in real-time and logged at the end of the day's trading. Private Equity prices are arrived at by "price discovery", this means that at a particular point in time, there is some uncertainty over the price. This price uncertainty is often referred to as the "illiquidity premium", an extra return that is demanded by investors to compensate for the fact that assets cannot be sold quickly and easily as publically listed equity. In the past this "premium" or extra return has varied, but over the long term it has on a net of fees basis been greater than 1% above the return of listed equity markets.

Investment in Private Markets a broader term for Private Equity, Private Debt and Infrastructure can be achieved by investing in a fund of funds, direct funds, co-investing and direct investing. This way some of the risks of this type of investment can be mitigated by diversifying not just at the investee company level but also by the style of manager. Funds can be open ended or closed-end occasionally they are listed on a stock exchange, most often they will be Closed-end and Unlisted. While the fund of funds approach is potentially the most expensive, it does have lower governance requirements, higher diversification and investor access, than most of the other approaches.

The key to success of investment in Private Markets asset is "manager skill", the quality of the research, the ability of the manager to identify good quality companies, to invest not just money but also to provide consulting and / or hands on experience in management, usually the manager will have seat on the Board of the investee company and will be actively engaged in driving forward the strategy and value creation. It is also important that the manager has a stake in the investee companies, investing alongside management and the investors, to ensure the alignment of interests. Other important keys to success include diversifying factors such as Geography, Sector and Vintage.

Most funds are Primary offering closed-end funds, this means the investors can be invested for over 10 to 12 years, once the investor has committed funds they are obliged by contract to deliver the capital when called. Many closed-end funds have a finite life, by which time all the committed capital must be returned to investors, sometimes there is an extension period to enable the sale of assets at a better price or to mitigate general macro-economic conditions.

Listed in the table below are the past and current Private Equity and Infrastructure investments in the Surrey Pension fund listed by Fund Manager and then by Vintage (year of creation).

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Private Equity Fund Manager and Fund Name	Vintage	Fund Status in life cycle	Surrey Commitment	% of commitment drawn	Gross IRR	Net IRR [2]
Aberdeen Standard Investments						
European Strategic Partners II	2002	Fully Realised	E10m	93	17.2%	12.4%
European Strategic Partners 2006	2006	Distributing	E15m	92	7.8%	5.7%
European Strategic Partners 2008	2008	Distributing	E15m	93	13.4%	9.6%
European Smaller Funds I	2012	Value Creation	E17.5m	67	9.8%	5.4%
Secondarieis Opportunities Fund I	2014	Value Creation	US$20m	92	15.5%	13.5%
Secondarieis Opportunities Fund II	2014	Investing	US$20m	82	27.5%	24.5%
Secondarieis Opportunities Fund III	2017	Investing	US$45m	23	n/a	n/a
BlackRock						
DivPEP I	2000	Distributing	US$5m	96	18.9%	13.2%
DivPEP II	2002	Distributing	US$5m	94	14.6%	10.4%
DivPEP III	2005	Distributing	US$17.5m	88	6.9%	4.7%
Capital Dynamics						
LGPS Collective PE Vehicle	2016	Investing	£8m	25	n/a	n/a
LGPS Collective PE Vehicle	2017	Investing	£8m	7	n/a	n/a
Darwin Alternatives						
Darwin Leisure Development Fund	2013	Value Creation	£20m			13.3%
Darwin Leisure Development Fund	2017	Investing	£40m			9.8%
Goldman Sachs						
Private Equity Partners 2000	2000	Distributing	US$9.5m	107		13.9%
Private Equity Partners 2004	2004	Distributing	US$10m	105		7.4%
Private Equity Partners 2005	2005	Distributing	US$17m	100		3.8%
Private Equity Partners X	2008	Distributing	US$18m	91		11.2%
Private Equity Partners XI	2011	Value Creation	US$40m	90		17.6%
Vintage VI Secondaries Fund	2013	Investing	US$20m	79		14.9%
Vintage VII Secondaries Fund	2016	Investing	US$50m	29		n/a
HgCapital						
HgCapital Partners 5	2006	Distributing	£10m	98	16.1%	11.5%
HgCapital Partners 6	2006	Distributing	£10m	94	17.2%	11.8%
HgCapital Partners 7	2013	Value Creation	£15m	94	23.5%	16.4%
Livingbridge						
ISIS II	1999	Fully Realised	£12m		22.0%	17.0%
ISIS III	2003	Fully Realised	£14m		33.0%	24.0%
Livingbridge 4 LP	2007	Fully Realised [3]	£15m		29.0%	18.0%
Livingbridge Enterprise 1 LP	2013	Value Creation	£10m	66	17.0%	12.0%
Infrastructure Fund Manager and Fund Name						
Goldman Sachs						
West Street Infrastructure Partners III	2017	Investing	US$20m	23	n/a	n/a
Pantheon						
Pantheon Global Infrastructure III	2018	Investing	£45m	20	n/a	n/a
Estimated average Net IRR						**12%**

Notes

2) Net Returns are stated after fees and carried interest (where applicable)

3) The fund is fully realised, other than holding £1.4m in escrow following the sale of Autologic.

Performance

From the table above, a simple average of the 22 (out of 29) funds fully or majority invested, shows an estimated return of over 12% pa. While this number is somewhat mis-leading the Net Internal Rate of Return (IRR) for each fund varies between 3.8 and 24.5%, with many showing strong double-digit IRR's. This estimate is somewhat higher than the return available from the publicly listed equity markets over a similar period.

Funds invested with a vintage prior to the Global Financial Crisis (GFC) have consistently achieved IRR's of over 10% with the range 10.4 to 24%. Those funds with a vintage just before and during the GFC have more varied IRR's in a range of 3.8 to 18% and an average just under 10% and those funds of a vintage post the GFC that have been fully, or majority invested have achieved an average return over 10% in a range of 5.4 to 24.5%. There are number of funds that have only recently had capital committed to them, these are marked n/a because there is no meaningful data on performance at this stage.

Where I was able, I have included the gross IRR's to show how expensive some of the fund managers are, but as I mentioned above manager skill and alignment of interests are the keys to success in this asset class. It is also worthy of note that most managers have deployed over 90% of committed capital over the life cycle of the funds.

Adviser View

The reports received from the various managers and my analysis, support the investment thesis that investing in Private Equity does generate higher returns than listed equities to compensate for the lack of liquidity. The same thesis is yet to be proven, but with time investment in infrastructure can also be expected to provide higher returns, more linked to income than growth, if at higher costs, than publicly listed assets for the Surrey Pension Fund. Possibly and more importantly because of the different nature of the private market assets and the investment approaches adopted by the managers, the Surrey Pension Fund enjoys significant risk diversification benefits from its current investments and should probably consider increasing its allocation.

The Surrey Strategic benchmark's asset allocation is already well diversified and contains an allocation to Private Equity, but there is no dedicated allocation to other Private Markets such as Private debt or Infrastructure. These investments are less liquid (more difficult to buy and sell) and require high levels of due diligence to ensure only the best opportunities are acquired. The manager selection process is resource intensive, can be slow and once the manager is selected, deployment of committed cash can take a long time.

Despite this, Private Market assets exhibit many desirable attributes for pension funds whose long term liabilities have call for a balanced portfolio of long term assets whose performance is dependent on diverse sources of risk and return compared to more traditional tradable asset classes such as bonds and listed equities. For instance Private Debt can access higher yielding assets with floating rate yields, thereby reducing the interest rate sensitivity of the Fund and Infrastructure investment can provide a cheaper way to access long term inflation linked cash flows than through index linked gilts.

Private Equity is a very different asset class to listed equity because of the level of active engagement by the manager driving forward the value creation and development of the investee company rather than the hands off approach used when investing in listed equity where the management is trusted to run the business.

Currently the Strategic benchmark has a 5% allocation to Private Equity which I believe from a diversification, liquidity, risk and reward point of view is reasonable. However I believe that the Fund should consider investing in other Private Market asset classes and have a dedicated allocation to Infrastructure and Private Debt. As mentioned above these alternative asset classes have many of the attributes suitable for pension funds in that their returns are more highly linked to long term higher yielding contractual cash flows and provide diversified sources of income to traditional bond markets. While the manager selection process is resource intensive, Surrey will have these resources provided to it by its partnership with the BCPP Pool.

Further investment in the Private Equity and Infrastructure asset classes is merited, but because of the nature of the cash flows to and from the asset class and the growth of the Surrey Pension Fund, the level of investment will need to be monitored by the Pensions team, to ensure that the neutral weight is at least maintained so as to capture of the returns available. Until the Pensions and Investments Committee have a clear view of what Private Market funds the Border to Coast Pension Partnership has to offer and the timing of the delivery of this capability, the PIC will need to continue to make allocations directly to these alternative investment strategies. As mentioned above there is probably merit in having a dedicated allocation to Infrastructure and Private Debt.

Anthony Fletcher
Independent Investment Adviser
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Table 1 Private equity cashflow analysis - Net of all fees and expenses

Financial Year	Drawdowns (Purchase) £000	Distributions (Sales) £000	Total (net of Purchase/Sales) £000
1999/2000	-161	0	-161
2000/2001	-1,174	6	-1,168
2001/2002	-1,141	16	-1,125
2002/2003	-3,822	170	-3,652
2003/2004	-7,608	1,851	-5,757
2004/2005	-5,792	6,858	1,066
2005/2006	-16,147	5,589	-10,558
2006/2007	-17,172	8,853	-8,319
2007/2008	-9,881	4,598	-5,283
2008/2009	-6,696	2,098	-4,598
2009/2010	-13,880	11,351	-2,529
2010/2011	-15,468	21,401	5,933
2011/2012	-17,365	13,137	-4,228
2012/2013	-19,290	22,785	3,495
2013/2014	-15,633	10,986	-4,647
2014/2015	-32,730	40,558	7,828
2015/2016	-25,921	25,310	-611
2016/2017	-19,465	17,209	-2256
2017/2018	-42,236	30,779	-11,457
Grand Total	**-271,582**	**223,555**	**-48,027**
Calculated Internal Rate of Return (IRR)*		**7.7%**	**12.4%**

* The IRR is a discount rate applied to the total cash flows in Table 1 as well as the final assessed value in table 2 to ensure that the net present value is zero. These calculations are performed for each of the assessed values using the same cash in and out to get a comparison between private equity performance and public market performance.

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **CORPORATE GOVERNANCE SHARE VOTING**

SUMMARY OF ISSUE:

This report provides a summary of the Fund's share voting process in Q1 of 2018/19 (1 April 2018 to 30 June 2018). The report also includes a class action against BHP who is a firm Surrey had investment in.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1 Note the report.

REASON FOR RECOMMENDATIONS:

The Pension Fund Committee must be aware of the voting actions pertaining to the segregated portfolios of shares held within the pension fund.

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).

3 Annex 1 contains a list of terms and abbreviations used in the report and Annex 2 shows the Fund's latest approved responsible investment and stewardship (and share voting) policy.

Meetings Voted: Q1 2018/19

4 Table 1: Meetings Voted below shows that 99 meetings were voted in total, comprising entirely AGMs.

Table 1: Meetings Voted

Region	AGM	EGM	GM	Court	SGM	Total
UK and Ireland	56	-	3	-	-	59
Asia and Oceania	2	-	-	-	-	2
North America	23	-	-	-	-	23
Europe	9	1	-	-	-	10
Japan	4	-	-	-	-	4
Africa	1	-	-	-	-	1
Total	95	1	3	0	0	99

Resolutions

5 Table 2: Resolutions Voted shows the total number of resolutions voted by region, broken down by meeting type. During Q1, 1,781 resolutions were voted, with the bulk of these in UK and Ireland.

Table 2: Resolutions Voted

Region	AGM	EGM	GM	Court	SGM	Total
UK & Ireland	1,205	-	4	-	-	1,209
North America	326	-	-	-	-	326
Asia & Oceania	23	-	-	-	-	23
Europe	150	4	-	-	-	154
Japan	54	-	-	-	-	54
Africa	15	-	-	-	-	15
Total	1,773	4	4	-	-	1,781

6 The table shows the majority of the meetings were held in May, reflecting the relatively condensed AGM season for UK and North American companies.

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

Event	Apr	May	Jun	Total
AGM	23	61	11	95
EGM	-	-	1	1
GM	-	2	1	3
Court	-	-	-	-
SGM	-	-	-	-
Total	23	63	13	99

Votes Against Management

7 The data in Table 4 (Votes Against Management By Resolution Category) show some important perspective on the type of voting decisions being made. As a part of the research analysis of meetings, each resolution is categorised according to the governance considerations to which they relate.

8 Table 4 shows the total number of resolutions which Surrey was entitled to vote along with the number of contentious resolutions voted during the quarter. Surrey voted against management on 15.7% of the resolutions for which votes were cast during Q1.

9 Remuneration and Board resolutions accounted for the majority of all resolutions to be voted on with 76 voted against, 74 resolutions sought remuneration report approvals with the remaining two resolutions related to overall remuneration policy.
Surrey voted against Remuneration resolutions in 51.0% of cases.

10 60.2% of Shareholder Rights-related resolutions were voted against, 49 out of 50 were resolutions to approve 14-day notice periods for ordinary general meetings (other than AGMs).

Table 4: Votes Against Management By Resolution Category

Resolution Category	Total Resolutions	Voted Against Management	% votes Against Management
Board	915	50	5.5%
Capital	357	59	16.5%
Remuneration	149	76	51%
Audit & Reporting	227	12	5.3%
Shareholder Rights	83	50	60%
Sustainability	42	32	76.2%
Corporate Actions	7	-	0%
Other	1	1	100%
Total	1,781	280	15.7%

Shareholder Proposed Resolutions

11 Thirty resolutions voted during the period were proposed by shareholders. 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. However, the flipside danger is the possibility of lack of shareholder support from other shareholders.

12 Two shareholder resolutions passed in Q1; the management-supported proposal to amend the Articles of Association in relation to the election procedure on directors representing employees at Orange and the proposal at Gilead Sciences to amend the bylaws to provide that shareholders may act by written consent.

13 A significant proportion of shareholder resolutions received more than 25% shareholder support in the quarter, relating mainly to shareholder rights requests or requests to amend governance practices.

Remuneration

14 Votes against remuneration resolutions in Q1 reflected the principles advocated in Surrey's policy. 31 distinct resolutions informed Surrey's remuneration voting and the chief concerns as measured by the number of resolutions associated with remuneration issues were:

- **Bonus Caps:** The upper bonus cap for any of the executive directors exceeds an acceptable multiple of salary. This was a factor in 44 of the remuneration resolutions opposed by the fund;
- **Alignment:** where there is misalignment between the incentive scheme performance measures and key performance indicators used by the company. This was a factor in 43 of remuneration resolutions opposed by the fund;
- **Remuneration Committee Composition:** The composition of the remuneration committee was of concern in 12 remuneration resolutions opposed by the fund
- **Assessment:** In 19 remuneration resolutions opposed by the fund, the company had received a low Manifest Remuneration Assessment Grade;
- **Severance Provisions:** Contract provisions for executives provided for potentially excessive severance payments. This was a factor in 13 remuneration resolutions opposed by the fund;
- **LTIP Vesting:** The minimum performance period and/or vesting period was considered too short. This was a factor in 12 of the remuneration resolutions opposed by the fund;

15 All remaining concerns featured in less than 10 remuneration resolutions opposed during Q1. These concerns included: a lack of disclosure of the performance targets under the annual bonus; all awards not being subject to performance conditions; executive pensions accruing at a preferential rate compared to ordinary employees; a bonus payment awarded despite a loss being recorded; awards could partially vest for below median performance; and various disclosure concerns.

Table 5: Remuneration

Resolution Category	Total Resolutions	Voted Against Management
Remuneration – Amount (Total, Collective)	1	0
Remuneration – Amount (Total, Individual)	11	0
Remuneration – Report	79	75
Remuneration - Policy (Long-term incentives)	14	0
Remuneration – Non-executive	6	0
Remuneration - Policy (Overall)	29	1
Remuneration - Policy (All-employee Share plans)	4	0
Remuneration - Policy (Contracts)	2	0
Remuneration – other	3	0
Total	149	76

Monitoring and Review

16 The share voting policy is kept under constant review.

Class Actions

17 Surrey county council has recently entered into a class action against BHP Billiton Limited (BHP) and will be represented by Phi Finney Mcdonald.

Claim Overview

18 The class action relates to the collapse of the Fundão tailings dam at the Germano mine in Minas Gerais, Brazil, on 5 November 2015. The dam released between 32 and 62 million cubic metres of waste (the largest tailings dam rupture ever recorded), killing 19 people and creating a catastrophic and enduring impact on the surrounding communities and the environment.

19 The Germano mine was operated by Samarco Mineração SA (Samarco), a joint venture of BHP and Vale SA (Vale). BHP's stock prices declined significantly in the days following the disaster.

20 The claim alleges that, from at least 21 October 2013, BHP knew that there was a material risk that the dam would collapse, and of the likely consequences of such a collapse. On that basis, the claim will allege that BHP breached its continuous disclosure obligations and engaged in misleading or deceptive conduct by failing to disclose this risk to the market

(the Claims). These Claims may be amended over time, particularly after receipt of discovery.

Funding Agreement

21 Under the proposed agreements, Surrey would not have any obligation to pay any legal fees and expenses of the Phi Finney McDonald law firm that will be representing plaintiffs. The firm's fees and expenses will be paid by a litigation funder, G&E KTMC Funding.

22 If the litigation is successful, the funder would receive a payment of 18%, plus certain other expenses.

23 Governed by the laws of Victoria state, Australia, where the case will be tried.

24 Disputes will be dealt with by arbitration in New York. Surrey are responsible for its own costs in any dispute should it escalate.

25 The Funder will lead the case on our behalf.

26 In the event of a conflict of interest between Surrey and the Funder, the lawyers will act for Surrey.

CONSULTATION:

27 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:

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

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

29 There are no financial and value for money implications.

DIRECTOR OF FINANCE COMMENTARY

30 The Acting Section 151 Officer is satisfied that the share voting policy offers an effective framework for the sound share voting of the pension fund, subject to reviews of the policy being presented on a regular basis.

LEGAL IMPLICATIONS – MONITORING OFFICER

31 There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

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

OTHER IMPLICATIONS

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

WHAT HAPPENS NEXT

34 The following next steps are planned:

- Share voting policy be kept under review

Contact Officer:
Neil Mason, Head of Pensions

Consulted:
Pension Fund Committee Chairman

Annexes:
Annex 1: List of abbreviations
Annex 2: Latest approved Responsible Investment and Stewardship Policy

Sources/background papers:
None

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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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Annex 2

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 Stewardship Policy annually. The Fund's officers will carry out this review and propose any changes to the Pension Fund Board 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.

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 and financial reporting 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, 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 and when the incumbent audit firm was appointed.

- **Approval of Financial Statements**

Where there is a qualified audit statement; where there is uncertainty about the future viability of the business; where there is a restatement 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.

- **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 a suitable alternative resolution, where available, such as 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.

Committees should be composed of individuals with adequate professional understanding of the matters to be resolved. This is particularly the case for the audit and risk committee. The fund may choose to abstain where there is insufficient evidence of appropriate competencies.

- **Separation of Chairman & Chief Executive Officer (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 and 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**

Evidence of reward for failure has lead to shareholder concerns over the length of notice periods for directors which have been used in the past to inform severance pay levels. Where the terms of executive pay policy allow overly generous severance pay on early termination of an executive contract, the fund may choose to register concern via an abstention vote.

Director notice periods are significantly important. Where an executive director's notice period exceeds twelve 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, for example, audit or HR.

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 and 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.

- **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 equitable 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.

- **Controlling Shareholder**

Where a controlling shareholder is present on the share register, it is important that minority investors understand fully the nature of the rights held by that shareholder. Minority investors expect a formal relationship agreement to be in place and for this agreement to be fully disclosed to all shareholders.

4.5 Mergers and Acquisitions (M&A)

Support will be given to mergers and acquisitions that enhance shareholder returns in the longer term and encourage 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 recognises that some legitimate business related expenditure, such as marketing or sponsorship, may be construed as political under the terms of current legislation in some markets. Where authority for political expenditure fails to distinguish the amounts involved, or the period covered, or the amounts or period are considered excessive, the fund will not support the authority.

In addition 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 stewardship activities.

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.

The Board will provide an annual report on how the Surrey Pension Fund satisfies its UK Stewardship Code obligations requirements.

SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **CASHFLOW ANALYSIS**

SUMMARY OF ISSUE:

A cash-flow analysis allows the Fund to ascertain a projection as to when benefit payments may exceed income. This information can influence both the investment and funding strategy.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Note the cash-flow position for quarters four and one.

REASON FOR RECOMMENDATIONS:

The Pension Fund Committee must approve and review all working documents produced for the Pension Fund.

DETAILS:

Cash-flows for quarters four (2017/18) - one (2018/19) (1 January 2018 – 30 June 2018)

1. In simple terms, Pensions Funds have a positive cash-flow when their contribution inflows exceed pension benefits paid.

2. Contributions are derived from employers and employees. Pension benefits are derived from pensions and lump sum benefits paid to retired members and benefits paid to employees on leaving the Fund.

3. The half-yearly (quarters four-one) cash-flow for the Surrey Pension Fund shows positive cash flow of £4,197,716 as follows:

Quarter	Total contributions received	Total pension benefits paid	Net cash-flow

Four (1 Jan 2018 – 31 Mar 2018)	£48,069,984	£38,909,282	£9,160,702
One (1 Apr 2018 – 30 Jun 2018)	£34,266,600	£39,320,471	(£5,053,871)
		Closing cash-flow	**£4,106,831**

4. The quarter one contributions is in line with the historic trend where the contribution inflow are significantly lower than those in the Q4. As this is the start of a new financial year, the employers are generally slow in paying. However, all of the contributions are received before the end of the year, and thus larger contributions in Q4, which overall eliminates any negative cash-flows in the prior quarters.

5. An indication of the current membership trends is shown by movements in membership over quarters four-one, compared to the position at the 2016 valuation (as taken from statistics provided by the pension administration team):

Period	Active members	Deferred members	Pension members	Total members
2016 valuation (31 Mar 2016)	33,404	33,200	23,243	89,847
Quarter four 2017/18 (1 Jan 2018 – 31 Mar 2018)	34,557	36,119	25,043	95,719
Quarter one 2018/19 (1 Apr 2018 – 30 Jun 2018)	35,321	36,406	25,345	97,072

CONSULTATION:

6. The Chairman of the Pension Fund has been consulted and offered full support for the proposals.

RISK MANAGEMENT AND IMPLICATIONS:

7. The Fund will keep the cash-flow position under review and ensure the investment strategy remains consistent and appropriate.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

8. There are no financial and value for money implications.

DIRECTOR OF FINANCE COMMENTARY

9. The Acting Section 151 Officer is satisfied that all material, financial and business issues and possibility of risks have been considered.

LEGAL IMPLICATIONS – MONITORING OFFICER

10. There are no legal implications or legislative requirements

EQUALITIES AND DIVERSITY

11. Cash-flow analysis does 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:

    - A cash-flow analysis update to be provided to the Committee twice annually. The next report being produced for the 16 November 2018 meeting.

Contact Officer:
Neil Mason, Head of Pensions

Consulted:
Pension Fund Committee Chairman.

Annexes:

Sources/background papers:
None

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **2019 VALUATION REPORT**

SUMMARY OF ISSUE:

This report provides an introduction to the 2019 triennial valuation including a draft project plan from the Fund actuary, Hymans Robertson.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1 Note the report and two annexes from Hymans Robertson.

2 Authorise officers to continue work with Hymans Robertson on tailored employer investment strategies and bring further updates to the Committee.

REASON FOR RECOMMENDATIONS:

The Pension Fund Committee must be aware of and informed of all elements of in respect of the triennial valuation as this informs employer contribution rates and the investment strategy of the Fund.

DETAILS:

Background

1 The Fund actuary, Hymans Robertson, carries out a triennial valuation of the Fund's assets and liabilities. The primary and secondary contribution rates for all employers in the Fund and the accompanying investment strategy are derived from this valuation.

2 The next triennial valuation is on 31 March 2019 (effective 1 April 2020).

3 The project timeline for the next valuation runs for approximately one year from June 2018 to June 2019. Hymans have produced a draft project plan, included as Annex 1.

4 Officers will work with Hymans to refine this plan and report regularly on progress towards the valuation to the Board.

Tailored Investment Strategies

5 The Fund comprises over 250 participating employers with a range of differing characteristics. These include Surrey County, Borough and District councils, Surrey Police, education establishments and admitted bodies.

6 In the 2016 triennial valuation these employers were categorised in to four groups commensurate with the security they offered the Fund. These categories each had a contribution methodology consistent with risk they presented the Fund.

7 Although categorised in to four there is currently a single investment strategy across all employers in the Fund.

8 Tailoring both funding and investment strategies to different groups of employers would help improve overall risk management of the Fund in the following ways:

- by reducing the risk of adverse outcomes for employers;
- allowing the fund to monitor and engage with employers with default risk and ensure their funding strategy is appropriate;
- mitigating the risk of complaints against the Fund (and the associated reputational damage).
-

9 Hymans Robertson have provided have produced a report, shown as Annex 2, which identifies the following risk metrics by which employers may be grouped to derive their investment strategies:

- Maturity: liability profile
- Funding level
- Net cash-flow position
- Maturity: declining payroll
- Time horizon

10 The Fund introduced the Hymans Robertson Employer Asset Tracker (HEAT) since the 2016 valuation. The HEAT system tracks and reports the asset position for each individual employer in that Fund. HEAT can also be used to track the asset position of a pool or group of employers; to do this it sums the assets attributed to each employer in the pool or group. HEAT allows for the more effective facilitation of tailored investment strategies. The methodology of HEAT is also shown in the Hymans report (Annex 2).

CONSULTATION:

11 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:

12 Default by scheme employers can represent a material risk to the Pension Fund. This report seeks to identify and mitigate this risk.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

13 There are no financial and value for money implications.

DIRECTOR OF FINANCE COMMENTARY

14 The Acting Section 151 Officer is satisfied that work towards planning for the 2019 valuation is necessary and appropriate.

LEGAL IMPLICATIONS – MONITORING OFFICER

14 There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

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

OTHER IMPLICATIONS

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

WHAT HAPPENS NEXT

17 The following next steps are planned:

- Undertaking the analysis of the risk metrics; and
- Review the analysis and the need for the multiple strategies in the Fund
- Bring a future paper and recommendations to the Pension Fund Committee

Contact Officer:
Neil Mason, Head of Pensions

Consulted:
Pension Fund Committee Chairman

Annexes:
Annex 1: Pre-valuation project plan
Annex 2: Hymans paper on exploring tailored employer investment

Sources/background papers:
None

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Surrey pre valuation project plan: DRAFT project overview as at June 2018
HEAT -HYMANS EMPLOYER ASSET TRACKER

HYMANS ROBERTSON

KEY
- Deliverable
- Reporting / Engagement
- Decision making
- Fund's Process
- Hymans' Process
- Milestone markers

Project management/engagement

Project planning

- Monthly catch up call

Engagement

- Local Pensions Board meeting (25 July) Present project plan
- Project reporting to stakeholders
- Committee Meeting (14 Sept) Paper on individual investment strategies
- Project reporting to stakeholders
- Committee Meeting (16 Nov)
- AGM (Nov)
- Project reporting to stakeholders
- Project reporting to stakeholders
- Committee Meeting (Feb) Assumption sign off
- Project reporting to stakeholders
- Project reporting to stakeholders
- Committee Meeting (TBC)

HEAT Implementation

Data Provision

- Manual for data requirements passed to Fund's internal team
- Fund pulls together 1st month of data
- Hymans' review of initial dataset
- Fund refines data as per review
- Initial dataset complete
- Fund provides remaining data for 23 months of cash flows from April 2016 – March 2018
- Ongoing data clarification between Hymans and the Fund
  Updates on new employers
- Data for months since March 2018 provided by Fund
- Ongoing data clarification between Hymans and the Fund
- Monthly data provision
- Monthly data provision
- Monthly data provision
- Monthly data provision

HEAT system

- Hymans' test initial dataset with HEAT
- Hymans' enters initial dataset into HEAT
- Initial HEAT dataset complete
- Hymans' enters remaining datasets into HEAT
- Core Phase 1 datasets complete
- Hymans' enters final datasets into HEAT
- Phase 1 HEAT implemented
- Entry into HEAT
- Entry into HEAT
- Entry into HEAT
- Entry into HEAT

Monthly data process

- Fund apply monthly data provision template internally with support from Hymans
- Internal development of monthly process for delivering data
- Monthly process for delivering data agreed
- BAU monthly process in place
- Monitor monthly process and refine if needed
- BAU monthly process complete

Individual employer investment strategies

HEAT Phase 2

- Hymans' draft paper on strawman of what individual strategies will look like
- Sign off initial paper for taking to Committee
- Committee decision on Phase 2 GO / NO GO from 1 April 2019
- Hymans' training for applying multiple strategies for HEAT
- Fund considerations for Phase 2:
  - Strategy design
  - Asset implementation
  - Admin (reporting, policies, procedures etc)
- Design of and implementation of strategies
  Analysis of assets
- Draft and finalise recommendation
- Training for Committee

Employers

Categorisation

- Meeting covenant advisor
- Review employer database and current status of each employer
- Draft of expanded categorisation
  Consideration of metrics to be gathered for each employer
  Initial high level categorisation set out
- AGM – set the scene
- Draft actions / options for employers to allow them to change their category
- Employer meetings to kick off expanded categorisation and multiple investment strategies

Valuation process

Timeline

- Initial correspondence released with timetable for year
- Assumption modelling
- Setting Council contribution rates
- Finalise Council contribution rates
- Finalise assets for valuation

Administration team

Pre valuation work

- Provide complete list of employer codes and names to Hymans
- Provide data for any outstanding new employers to date
- Data cleansing on Data Portal
  Data as at 31 March 2018 to capture two years of cleansing
- Provide data for any outstanding new employers to valuation date
- Final Employer database

June '18 | Jul '18 | Aug '18 | Sept '18 | Oct '18 | Nov '18 | Dec '18 | Jan '19 | Feb '19 | Mar '19 | Apr '19 | May '19 | June '19

PHASE 1: IMPLEMENTATION DATE

PHASE 2: IMPLEMENTATION DATE

2019

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Exploring employer investment strategies

Addressee and purpose

This paper is addressed to Surrey County Council in its capacity as Administering Authority to the Surrey Pension Fund ("the Fund"). The purpose of this paper is to discuss the need for the Fund to consider implementing tailored investment strategies, complementing the categorised employer funding strategies already in place, to help employers achieve better funding outcomes. This paper has been prepared by Hymans Robertson LLP in our capacity as actuaries to the Fund.

Background

The Fund is made up of many participating individual employers (c. 200) who have a diverse range of funding profiles. For example, one employer may be well funded and consist purely of active members whereas another may have no active members and be poorly funded.

In the past few years the Fund has adopted a more flexible approach to funding and contribution strategy. The introduction of the individual employer categorisation means that the funding strategy now recognises the diversity between employers. However, at present, the Fund operates a single investment strategy which applies to every employer.

Tailoring both funding and investment strategies to different groups of employers would help improve risk management, reduce the risk of adverse outcomes for employers and reduce the risk of complaints against the Administering Authority (and the associated reputational damage).

Bearing the above in mind, and as part of the 2019 valuation, the Fund should investigate whether this 'one size fits all' approach to the investment strategy is still appropriate or whether multiple investment strategies could be implemented for different groups of employers.

This paper sets out:

1 What we mean by 'multiple of investment strategies'

2 The benefits to the Fund in operating multiple investment strategies

3 Why employers in the Fund have differing objectives and why they may be best served by alternative investment strategies

4 Analysis that can be carried out to investigate the need for multiple strategies

5 The next steps to consider

What do we mean by 'multiple of investment strategies'

The Fund currently operates a single investment strategy which applies to every employer. The high level strategy can be simplified as assets invested 80% in growth and 20% in defensive holdings. Growth assets are high return seeking assets such as equities which, by nature, come with relatively high volatility of returns. Defensive assets are lower risk assets such as government bonds, in contrast, provide lower but more certain returns.

By offering multiple investment strategies to employers, the Fund would instead offer investment mixes for the allocations to growth and lower risk assets. An example of the strategies could be:

- Strategy 1 - Main Fund: 60% growth / 40% lower risk

  This strategy may be suitable for long term, reasonably well funded, secure employers.

- Strategy 2 – Reduced Risk: 40% growth / 60% lower risk

  This strategy may be suitable for employers with no guarantor or targeting full funding on a gilts basis i.e. a flightpath to cessation.

- Strategy 3 – Recovery: 80% growth / 20% lower risk

  This strategy may be suitable for poorly funded employers.

The above are purely illustrative but the selection of suitable strategies would be a key stage in the implementation process to ensure that they deliver the best outcomes for the Fund employers.

Benefits to the Fund

The introduction of multiple investment strategies provides the following benefits for the Fund.

- Better funding outcomes for employers which therefore reduces the overall risk to the Fund
- Increased flexibility for setting employers funding plans
- Meets increasing needs of employers and provides them with a better service, particularly where they have bespoke objectives such as targeting exit on a gilts cessation basis
- Keep pace with other funds in the LGPS (as at start of 2018, 5 funds have implemented this solution with more considering it alongside planning for the 2019 formal valuation)
- Realise full benefit of the HEAT tool (see the Appendix for a recap on how the mechanics of the HEAT tool)

The ultimate aim of the Fund is to ensure all member's benefits can be paid in future. By introducing multiple investments strategies the Fund can ensure that each employer has the best possible funding outcome, tailored to their own circumstance which can only stand to benefit the overall Fund aim.

Employers objectives

In the past, the Fund primarily consisted of long term, secure employers such as Councils and other scheduled bodies. However, in recent years the diversity in the participating employers in the Fund has increased dramatically. The Fund now has councils, colleges, contractors, academies and charities, all with different objectives for their LGPS participation.

In order to assess whether the differing objectives of these employers would be best served by multiple investment strategies, the Fund should consider undertaking some analysis which aims to group similar employers based on risk metrics and funding objectives. This analysis builds on that undertaken for the purposes of the categorisation for setting employer contribution rates. From this analysis a rationalisation of whether these groups require multiple investment strategies can follow.

The risk metrics we believe should be considered as part of the analysis are set out below, together with some reasoning as to why each may indicate a need for an alternative strategy.

Maturity: liability profile

Mature employers are more likely to require investment income to meet their benefit outgo whereas less mature employers will benefit from reinvesting any investment income. Mature employers will also be funding any deficits with a small (in comparison to the deficit) payroll which can cause problems. These problems could be mitigated by considering multiple investment strategies.

There are a few measures of maturity which could be used, including:

1. Liability profile (percentage of past service liabilities that are in respect of pre-retirement members);
2. Gearing ratio (liabilities divided by payroll); and
3. Mean duration of liabilities (typically rolling 20 years plus for long term, secure employers that remain open to new entrants and possibly say 10-12 years and shrinking for employers with a high average age who are closed to new entrants – these different categories of employer have a different investment time horizon).

The degree of maturity alone will not drive a decision to switch to a lower risk investment strategy. For example, a poorly funded, mature employer may not be able afford to take less risk because of the level of contributions that would be required. For affordability reasons, such an employer may need to stick with the riskier main fund growth strategy and bear the associated volatility, in the hope of repairing its deficit.

Funding level

The funding position of an employer is a measure of the relative amount of assets held to pay the liabilities. If an employer is poorly funded it may benefit from a more aggressive investment strategy with the aim that higher asset returns will return them to a well funded position. Conversely, if an employer is well funded i.e. over 100% they may prefer a less risky investment strategy which doesn't expose them to potential large investment losses particularly if their remaining period of participation in the Fund is short – in other words they may seek to limit the downside risk.

Net cashflow position

Net cashflow position is the measure of contribution income over benefit outgo. As employers mature the contribution income will fall whilst benefit outgo rises. At some point the net cashflow position will become negative i.e. more benefits are paid out than contributions received. At this point the employer will start using their assets to pay benefits which may have implications for their future funding and investment strategy i.e. it may need to yield relatively more income in order to have cash to pay benefits as they fall due rather than be a forced seller of assets.

Maturity: declining payroll

For closed employers, the employer payroll will gradually fall over time as members leave through retirement or withdrawal. As the payroll falls the contribution income will decrease and benefit outgo will rise. Analysing the point at which the payroll will have fallen by say 50% gives an indication of how quickly the employer is maturing.

The rate at which an employer is expected to mature may indicate a need to change their investment strategy either to increase or decrease their level of investment risk depending on the results of the other risk metrics.

Time horizon

Some employers have clearly defined future time horizons for their participation in the Fund (e.g. contractors with fixed term contracts). Other employers have a finite period of future participation (e.g admission bodies who are closed to new entrants and who may be required to pay a termination payment on a gilts valuation positiont at the point the last active leaves). We can therefore quantify or estimate the outstanding period of time to the end of the admission agreement, a factor that should be taken into account in the combination of metrics which might trigger a change to a lower risk investment strategy. This is particularly pertinent when an employer has ceased and has made a cessation payment on a gilts basis. Currently this is invested in the main fund and running the volatility inherent in that rather than being invested.

Results of the analysis

There are combinations of metrics outlined above that may be strong indicators that an alternative investment strategy would be suitable. An example would be a combination of strong **funding level** and short **time horizon**.

For instance, an admission body that is a) well funded (say 120-140% funded on an ongoing basis); and b) has a short outstanding period of participation in the Fund (say 3 years or less) would likely benefit from switching to a lower risk investment strategy.

The analysis would include commentary on where any combinations of metrics indicates an alternative strategy would be more suitable.

Next steps

The next step in the process would be for Administering Authority to consider:

1. Undertaking the analysis of the risk metrics as outlined above; and
2. Reviewing the analysis and the need for the multiple strategies in the Fund.

If the need for multiple strategies is confirmed and the decision made to implement this following the 2019 valuation then there would be work carried out in conjunction with Mercer, in their capacity as the Fund's investment advisor. The work would involve identifying the number of alternative investment strategies and the strategic asset allocation of each.

Reliances and limitations

The advice in this paper is intended for the Fund to make a decision on whether to investigate the possible use of multiple investment strategies for employers.

This document should not be released or otherwise disclosed to any third party without our prior consent, in which case it should be released in its entirety. Hymans Robertson LLP accepts no liability to any other party unless we have expressly accepted such liability in writing.

Gemma Sefton FFA

For and on behalf of Hymans Robertson LLP

4 September 2018

Appendix

Recap on the HEAT system for allocating assets

Hymans Robertson Employer Asset Tracker (HEAT) is a system developed by Hymans Robertson that tracks the assets held by each employer in a multi-employer LGPS fund. The system can also be used to facilitate the implementation of multiple investment strategies within the fund.

The high level operation of the system is:

- The LGPS fund provides data to Hymans Robertson
- Hymans Robertson enters the data into HEAT
- HEAT calculates up to date employer asset values
- Hymans Robertson users can generate reports from HEAT which can be passed on to the LGPS fund.

The HEAT system uses a simplified cashflow approach to track employer asset shares.

Each implementation of the system is for one LGPS Fund and will track and report the asset position for each individual employer in that Fund. The system can also be used to track the asset position of a pool or group of employers; to do this it sums the assets attributed to each employer in the pool or group.

The system can be used to operate a single investment strategy or multiple investment strategies. Where a single investment strategy is operated initially, the system can be easily manipulated at a future date to introduce additional investment strategies. We have outlined below how the system operates for each of the single strategy and multiple strategy cases.

Overview of the HEAT process – single investment strategy

HEAT works on calculating investment returns for 'Sub Funds' on a monthly basis. Where there is only a single investment strategy being operated, there will be only one Sub Fund.

The Sub Fund is the sum of the assets across all investment managers ('invested assets') together with the Fund's uninvested cash (i.e. that sitting within the Fund's bank account(s)).

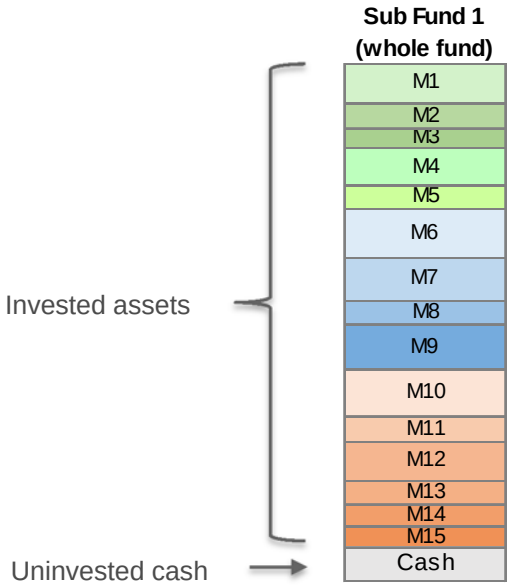
All Employers in the Fund are invested 100% in the Sub Fund, such that the sum of all of the employers' assets at any given month end equals the total value of the Sub Fund (and therefore the total value of the Fund).

At month ends, Employers are credited with investment returns (positive or negative) on the assets they notionally hold within the Sub Fund. Investment returns are derived from the change in the value of the Sub Fund over the month (after taking account for any inward or outward flow of assets in the month).

Employer cashflows are added to and subtracted from the Employer's asset holdings in the Sub Fund.

An example of a HEAT solution with a single investment strategy is shown in Figure A.

Figure A



Investment strategy	% in SF1	Employers
A	100%	1 - 40

Overview of the HEAT process – multiple investment strategies

HEAT calculates investment returns for notional 'Sub Funds' on a monthly basis. Where there are multiple investment strategies being operated, more than one Sub Fund will be required.

A Sub Fund is the sum of the assets across a collection of investment managers. Typically, the investment managers would serve a related purpose (e.g. growth assets). In addition to investment managers, each Sub Fund contains a notional, tracked portion of the Fund's uninvested cash (i.e. that sitting within the Fund's bank account(s)).

Employers are assigned to an investment strategy which is defined in terms of percentage holdings in each Sub Fund. For the avoidance of doubt, determining the investment strategy is not part of the HEAT scope of work.

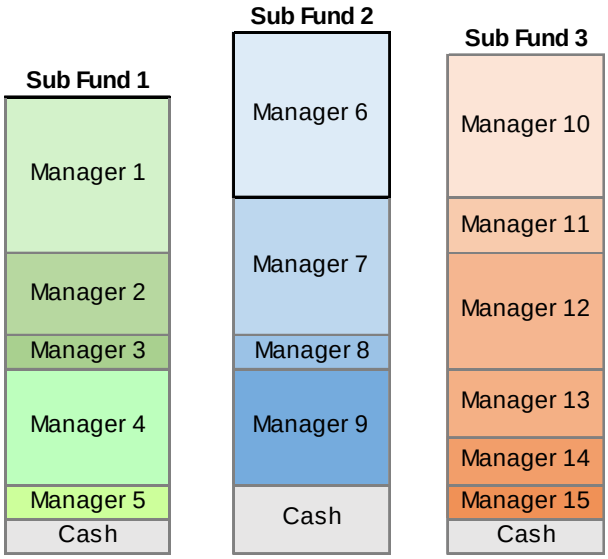
Employers are notionally allocated assets in each Sub Fund in accordance with their investment strategy. The sum of an employer's asset holdings across all Sub Funds is the Employer's total asset value.

At month ends, Employers are credited with investment returns (positive or negative) on the assets they notionally hold within each Sub Fund. Investment returns are derived from the change in the value of the Sub Fund's underlying assets (after taking account for any inward or outward flow of assets in the month).

Employer cashflows are added to and subtracted from the Employer's asset holdings in each Sub Fund in the proportions specified by the Employer's investment strategy.

An example of a HEAT solution with multiple investment strategies is shown in Figure B.

Figure B



Investment strategy	% in SF1	% in SF2	% in SF3	Employers
A	50%	50%		1 - 20
B		25%	75%	21 - 40

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SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **GOVERNANCE REVIEW**

SUMMARY OF ISSUE:

As part of the governance and oversight of the pension fund, a regular review and update to the governance framework, policies and procedures is essential to ensure that the Fund is compliant with latest legislation, regulations and good practice.

There have been significant developments in the LGPS over the past three years, which make a review of the governance of the Fund necessary and appropriate.

This report sets out the scope and timetable for a governance review which, if approved by the Committee, will be jointly undertaken by officers and appointed specialist advisors.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Approve officers to undertake a governance review and procure specialist governance advisors to assist with this review.

REASON FOR RECOMMENDATIONS:

The LGPS Regulations require each administering authority to publish a statement setting out the authority's policy on pension fund governance, including issues concerning the representation and participation of key stakeholders on pension committees/boards.

Regulation 55 of the Local Government Pension Scheme Regulations 2013 requires administering authorities to prepare a written governance compliance statement. Governance is defined as the leadership, direction and control of organisations to ensure they achieve their aims and objectives.

In public service organisations particularly, these processes need to be clear and open to scrutiny

The Pension Fund Committee must approve the governance compliance of the Pension Fund.

BACKGROUND:

1. Since 2015 there have been several major changes within the LGPS, including the following:

    - The introduction of the Pensions Regulator as regulator for the scheme;
    - The formation of local pension boards for each LGPS scheme;
    - The creation of a national Scheme Advisory Board which pays a significant role in the guidance and stewardship of the scheme;
    - The progress made under Government guidance in the formation of national asset pools leading to the Fund becoming a partner in the Border to Coast Pension Partnership (BCPP).

2. Taking the above major changes which in a way affect the LGPS - presents Funds with a new set of governance challenges. It is therefore necessary and appropriate to carry out a review of the Fund's existing way of thinking about their strategy and management going forward.

3. These changes make a review of the governance of the Fund necessary and appropriate.

DETAILS:

4. The proposed scope of the governance review has three sections, Overview, Background and Review.

5. **Overview**: Examine the existing governance framework, identify the main risks associated with the governance of the Fund and suggest possible improvements. In particular to comment on:
    - The extent to which the Committee takes proper advice on those matters which require specialist input;
    - The relationship between the Pensions Fund Committee and the Local Board;
    - The role of BCPP;
    - Compliance with the regulatory framework.

6. **Background**: The following Fund policies and other documents will be considered in the review:
    - Terms of reference of the Pension Fund Committee and Local Pension Board;
    - Investment Strategy Statement;
    - Policy on Discretions;
    - Governance policy/Governance compliance statement;
    - Communication Policy;
    - Process for reporting breaches of legislation;
    - Funding Strategy Statement;
    - Training Policy;
    - Conflict of Interest Policy;
    - Administration Strategy;
    - Service specification between the Fund and administration team;
    - ESG/Responsible investment policy.

7. **Review:** The review will include the following:

    - Direction – mission statement and supporting objectives
        - Legislative and regulatory compliance
        - Strategies and Policies
    - Delivery – How does the Fund meet its aims?
        - Annual business plan
        - Performance Monitoring
        - Risk Management
    - Decisions – Does the Fund have effective decision making?
        - Governance Structure
        - Behaviour
        - Pensions Skills and Knowledge
        - Governance structure: are all appropriate areas included, is ownership clear, appropriate and compliant with delegations of authority
        - Timeliness and quality control
        - In-house competency and use of expert advisors
    - The review should include an assessment of current Pensions Fund Committee and Local Pension Board meetings.

8. A report outlining the conclusions after interaction with officers, should be available for delivery to the Pension Fund Committee.

9. It is proposed to use the National LGPS Framework to procure a specialist governance consultant to provide specialist advice for this review. The cost of this advice is estimated at £25k-£30k.

10. The procurement process is estimated to take approximately one month from approval. Draft review findings would then be expected for the November 2018 Pension Fund Committee, with a final review available for the February 2019 Pension Fund Committee meeting.

CONSULTATION:

11. The Chairman of the Pension Fund has been consulted and offered full support for the proposals.

RISK MANAGEMENT AND IMPLICATIONS:

12. A regular review of governance is a suitable method of identifying and monitoring risk.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

13. The estimated cost to the pension fund of £25k-£30k in procuring a governance review are appropriate in the context of the risk management inherent in this activity.

DIRECTOR OF FINANCE COMMENTARY

14. The Acting Section 151 Officer has been consulted and is satisfied at the necessity of this review.

LEGAL IMPLICATIONS – MONITORING OFFICER

15. There are no legal implications or legislative requirements

EQUALITIES AND DIVERSITY

16. A review of governance does not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

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

WHAT HAPPENS NEXT

18. The following next steps are planned:

- Procure a governance advisor to assist with the governance review.

Contact Officer:
Neil Mason (Head of Pensions)

Consulted:
Pension Fund Committee Chairman.

Annexes:

Sources/background papers:
None

SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **ANNUAL REPORT/ STATEMENT OF ACCOUNTS**

SUMMARY OF ISSUE:

The Pension Fund Committee role is to approve the Annual report which contains the audited statement of accounts together with other information about the Fund's performance during 2017/18. The annual report is included in Annex 1.

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 (Annex 2).

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Note and approve the Annual Report for publication subject to audit approval.

2. Note the content of the 'External Audit Findings for Surrey Pension Fund' Report as set out in Annex 2, which reviewed the Pension Fund Statement of Accounts 2017/18

3. Note the Letter of Representation with regard to the Surrey Pension Fund Statement of Accounts as set out in Annex 3.

REASON FOR RECOMMENDATIONS:

Under the Local Government Pension Scheme (Administration) Regulations 2008, administering authorities of LGPS funds are required to prepare a pension fund annual report.

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

DETAILS:

1. The Surrey Pension Fund Statement of Accounts was presented to the Audit and Governance Committee at its meeting on 26 July 2018.

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 2017/18 draft financial statements and related notes to the accounts.

3. A copy of the financial statements and notes to the accounts included as part of the Pension Fund Annual Report 2017/18 in Annex 1.

4. The External Audit Findings for the Surrey Pension Fund is presented at Annex 2 and sets out a summary of the work carried out, the conclusion reached and recommendations made. The Pension Fund Committee 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 Acting Section 151 Officer is included at Annex 3.

6. The Audit and Governance Committee approved the report and associated attachments at the 26 July 2018 meeting.

CONSULTATION:

7. The Chairman of the Pension Fund has been consulted and offered full support for the proposals.

RISK MANAGEMENT AND IMPLICATIONS:

8. There are risk related provisions detailed within the Hymans report.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

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

DIRECTOR OF FINANCE COMMENTARY

10. The Acting Section 151 Officer 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

EQUALITIES AND DIVERSITY

12. The approval of the financial statements does 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 2017/18

Contact Officer:
Neil Mason (Head of Pensions)

Consulted:
Pension Fund Committee Chairman.

Annexes:
1. Surrey Pension Accounts 2017/18
2. External Audit Findings Report
3. Interim Section 151 Officer Letter of Representation

Sources/background papers:
None

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Surrey Pension Fund

Annual Report 2017/18

SURREY PENSION FUND

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Contents Page

Chairman's Introduction

2017/18 has been a very busy and successful year for Surrey Pension Fund with strong investment performance and growth in the number of employers in the Fund. The value of the Fund has increased from £3.9bn to £4.1 bn and the funding level from 93.8% to 95.1%. The number of employers in the fund is now over 230 and we service 100,000 members.

Investment pooling within the LGPS

The Surrey Pension Fund also made significant progress towards pooling the Fund's assets with other LGPS funds in order to improve returns, reduce costs and increase resilience across the funds. The Surrey Pension Fund has chosen to become part of the Border to Coast Pensions Partnership (BCPP), alongside 11 other partner LGPS funds. The BCPP is the largest LGPS pool, with assets valued at £43 billion, supporting over 900,000 scheme members and 2,200 employers.

Changes in the Investment Strategy

The transition to BCPP has provided the right time to reconsider the investment strategy of the Fund. This has led to a change in asset allocation, with additional allocation to global market funds at the expense of the UK holdings.

Investing Responsibly

The Fund has taken an increasingly active role in ensuring it invests with due attention to our environmental, social and governance (ESG) responsibilities. This has seen us agree an obligation to the BCPP Responsible Investment Policy and also directly led to the audit of the carbon footprint of the Fund and changes in our asset allocation to invest in low carbon alternatives. We believe that our ESG

objectives are best served by engagement and this is borne out with our relationship with BCPP and our membership of the national Local Authority Pension Fund Forum.

Funding Strategy

The triennial valuation was undertaken during 2016, with the changes to some of the funding assumptions. The valuation also saw the introduction of risk assessed employer contribution rates, based on strength of employer covenant. The introduction of this risk management strategy has seen the Fund assure additional security of over £2m, and gained industry recognition in being awarded Risk Management Strategy of the Year in the 2017 Local Authority Pension Fund Awards.

Changes in Management

Phil Triggs our previous Strategic Manager of Pension Fund & Treasury left Surrey in November 2017 and is succeeded by Neil Mason. We also had three new members joining the vibrant new Pension Fund team.

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Membership of the Pension Fund Committee

The current membership of the Pension Fund Committee is as follows:

	**Tim Evans: Chairman** Party: Conservative Borough and District: Spelthorne E:tim.evans@surreycc.gov.uk T:01932 785138
	**Ben Carasco: Vice Chairman** Party: Conservatives Borough and District: Woking E: ben.carasco@surreycc.gov.uk T: 07733 307525
	**Ayesha Azad** Party: Conservative Borough and District: Woking E: a.azad@surreycc.gov.uk T: 01483 757646

	**John Beckett** Party: Residents Association Borough and District: Epsom and Ewell E: john.beckett@surreycc.gov.uk T: 020 8393 8208
	**David Mansfield** Party: Residents Association Borough and District: Surrey Heath E:david.mansfield@surreycc.gov.uk T: 01483 799328
	**Hazel Watson** Party: Liberal Democrats Borough and District: Mole Valley E: h.watson@surreycc.gov.uk T: 01306 880120
	**Peter Stanyard** Party: Independent Borough and District: Mole Valley E: pgstanyard@gmail.com T: 07785 243988

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	**Tony Elias** Party: Conservative Borough and District: Tandridge E:Cllr.tony.elias@tandridgedc.gov.uk T: 01883742685
	**Margaret Janes** Head of Pensions University of Surrey
	Philip Walker Employee & Pensioners Representative

Membership of the Local Pension Board

	**Nick Harrison: Chairman** Party: Residents' Association and Independent Borough and District: Reigate and Banstead E: nicholas.harrison@surreycc.gov.uk T: 01737 215405
	**Graham Ellwood: Vice Chairman** Party: Conservative Borough and District: Guildford E: graham.ellwood@surreycc.gov.uk T: 07899 846626
	**Paul Bundy** Head of Finance Surrey Police E: Paul.Bundy@surrey.pnn.police.uk
	**Tina Hood** Surrey LGPS Members **E:** tina.hood@surreycc.gov.uk

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	Paresh Rajani Surrey LGPS Members
	David Stewart Surrey LGPS Members
	**Claire Williams-Morris** Guildford Borough Council
	**Trevor Willington** Surrey LGPS Members)

Officer Contact Details

	**Sheila Little** Director of Finance E: sheila.little@surreycc.gov.uk T: 020 8541 7012
	**Neil Mason** Head of Pensions E: neil.mason@surreycc.gov.uk T: 020 8213 2739
	**Steve Turner** Professional Advisor - Mercer E: steve.j.turner@mercer.com T: 01483 777035
	**Anthony Fletcher** Professional Advisor - Independent E: Anthony.Fletcher@MJHudson.com T:
	**Barry McKay** Fund Actuary T: 0141 566 7757 E: barry.mckay@hymans.co.uk

Fund Managers

Baillie Gifford
CBRE Global Investors
Franklin Templeton Investments
Legal and General Investment Management
Majedie Asset Management
Marathon Asset Management
Newton Investment Management
UBS Global Asset Management
Western Asset Management
Darwin Property Investment Management
Aviva Investors
Ruffer

Global Custodian

Northern Trust

Private Equity Advisors

BlackRock
Capital Dynamics
Goldman Sachs Asset Management
Hg Capital
Livingbridge Equity Partners
Standard Life Capital Partners
Pantheon Global Infrastructure

AVC Provider

Prudential Assurance Company
Equitable Life Assurance Society

Auditors

Grant Thornton UK LLP

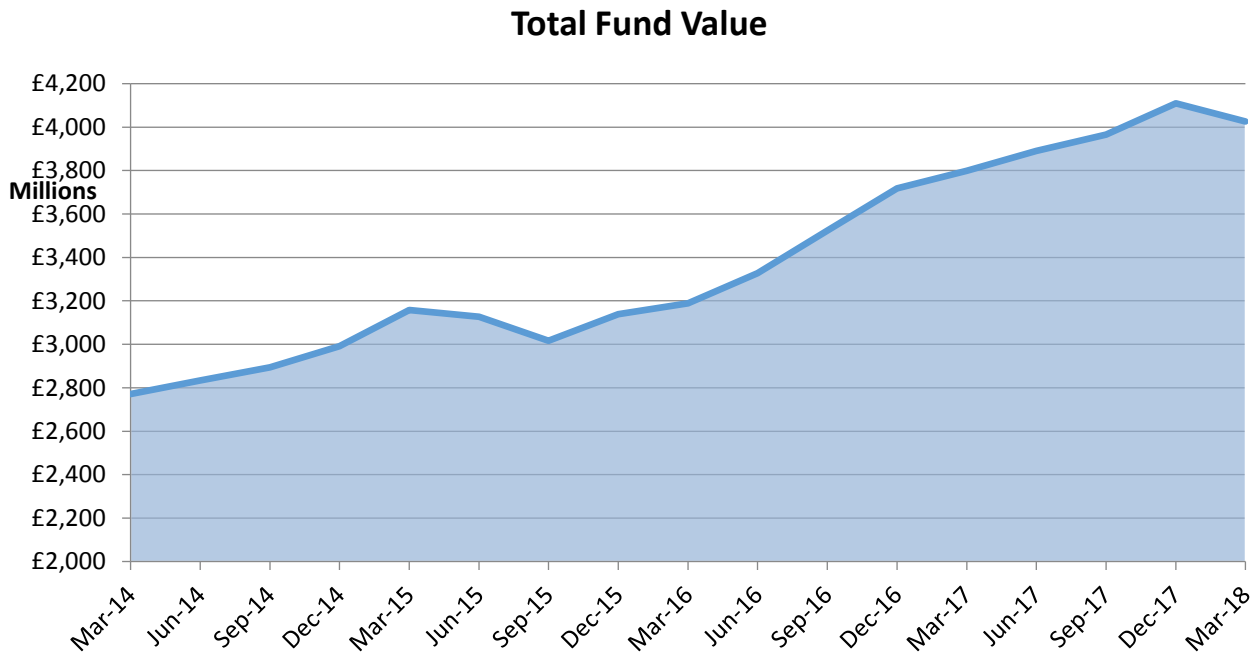
Bankers

HSBC

Overview

	2014/15 £000	2015/16 £000	2016/17 £000	2017/18 £000
Contributions and transfers in	181,104	192,419	199,650	191,164
Less benefits and expenses paid	-130,758	-139,213	-157,645	-167,521
Net additions	**50,346**	**53,206**	**42,005**	**23,643**
Net investment income*	39,504	45,592	61,238	64,719
Change in market value	299,210	-68,655	541,953	98,662
Net return on investments	**338,714**	**-28,063**	**603,191**	**163,381**
Net increase in Fund	386,020	30,143	645,196	187,024
Fund value at 31 March	3,193,520	3,223,663	3,868,859	4,055,883

*Net of Investment and governance expenses and tax withheld expenses



Summary Membership Details

31 Mar 2017		31 Mar 2018
34,298	Employees in the fund	35,802
24,025	Pensioners	25,135
41,573	Deferred pensioners	45,079

LGPS Scheme Details

On 1 April 2014, the new Local Government Pension Scheme (LGPS) came into effect, replacing the final salary scheme with a career average revalued earnings (CARE) scheme for future benefit accrual.

The new Scheme:

- has a normal pension age equal to state pension age (minimum age 65)
- gives a pension for each year at a rate of 1/49th of pensionable pay received in that year
- provides increased flexibility for members wishing to retire early
- allows members to pay reduced contributions as an alternative to opting out (though benefits build up at a slower rate)
- provides for previous years' CARE benefits to be inflation proofed in line with the Consumer Prices Index while the member is still paying in
- requires members to have at least 2 years' membership to qualify for pension benefits

Key LGPS Facts England and Wales

- Made up of 90 regional funds
- Around 5.3 million members
- Total fund assets are £217 billion
- Total expenditure on benefits is over £9.4 billion p.a.

Key LGPS Facts SCC

- Made up of 230 employers
- Around 100,000 members
- Total fund assets are £4.1 billion
- Total expenditure on benefits is over £137 million p.a.

The following pay ranges and employee contribution rates will apply from April 2018 as follows:

Actual Pensionable Pay	Contribution Rate
Up to £14,100	5.5%
£14,101 to £22,000	5.8%
£22,001 to £35,700	6.5%
£35,701 to £45,200	6.8%
£45,201 to £63,100	8.5%
£63,101 to £89,400	9.9%
£89,401 to £105,200	10.5%
£105,201 to £157,800	11.4%
£157,801 or more	12.5%

The regulations for the pre-April 2014 and post-April 2014 scheme are shown below:

Pre-2014: www.lgpsregs.org/timelineregs/Default.html

Post-2014: http://www.lgpsregs.org/schemeregs/lgpsregs2013/timeline.php

More information on the LGPS can be found on pages 109 to 112.

The Fund is financed by contributions from employees and employers, together with income earned from investments. The surplus of contributions and investment income over benefits currently being paid is invested.

The pay bands above increase each April in line with increases in the Consumer Prices Index (CPI).

Employers' contribution rates are set following each Actuarial Valuation. A valuation of the Fund's financial position must be made every three years when the Actuary certifies the employers' rates payable until the results of the next valuation are known.

Under the Regulations employer contributions are determined in two parts.

- A common rate based on the existing and prospective liabilities of the Fund having regard to the circumstances common to all the participating employers and to the desirability of maintaining as nearly constant a rate as possible
- Individual adjustments arising from circumstances peculiar to an individual employer.

Pensions paid to retired employees, and benefits with a deferred payment date, are subject to mandatory increases under pensions increase legislation. The cost of inflation-proofing benefits is funded through the employers' contribution rate.

Pension Fund Governance

Pensions Committee:

Responsibility and governance for the Pension Fund, including investment strategy, fund administration, liability management corporate governance is delegated to the Surrey Pension Fund Committee, 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 Committee is advised by a representative of the Fund's professional investment consultant, an independent advisor, the Director of Finance and the Head of Pensions. The Pension Fund Committee meets on a quarterly basis.

Local Board:

The governance arrangements of the Local Government Pension Scheme are changing. From 1 April 2015 the Surrey Pension Fund Committee will be assisted in its management of the Surrey Pension Fund by a Local Pension Board made up from representatives of members and employers of the scheme.

The role of the local Pension Board, as defined by Regulation 106 of the Local Government Pension Scheme Regulations 2013 is to assist the County Council as Administering Authority:

(a) to secure compliance with:

I. the scheme regulations;
II. any other legislation relating to the governance and administration of the LGPS Scheme and any connected scheme;
III. any requirements imposed by the Pensions Regulator in relation to the LGPS Scheme.

(b) to ensure the effective and efficient governance and administration of the LGPS Scheme.

The Local Pension Board will ensure it effectively and efficiently complies with the Code of Practice on the governance and administration of public service pension schemes issued by the Pension Regulator.

The Local Pension Board will also help ensure that the Surrey Pension Fund is managed and administered effectively and efficiently and complies with the Code of Practice on the governance and administration of public service pension schemes issued by the Pension Regulator. The Local Pension Board has power to do anything that is calculated to

facilitate or is conducive or incidental to the discharge of any of its functions but should always act within its terms of reference.
The Local Board is made up of representatives of the employers and members within the Surrey Fund and that the representation between employees and employers should be equal. The terms of reference of the board outlines the constitution of members as follows:

Employer representatives
- 2 x Surrey County Councilors
- 2 x Other employer representatives

Member representatives
- 1 x GMB nominated representative
- 1 x Unison nominated representative
- 2 x Other member representatives

The first meeting of the Local Pension Board was the 27 July 2017, the Board papers and minutes of meetings, as well as those for the Pension Fund Committee, are available on the Surrey County Council website.

The annual report of the Local Pension board is overleaf.

Local Pension Board Annual Report

This is the third annual report of the Surrey Local Pension Board. We have used 2017/18 to continue to build on the good practice developed since our establishment in 2015.

The Board is a requirement of the Local Government Pension Scheme Regulations 2013. Its primary functions are to assist Surrey County Council in:

- its compliance with the LGPS Regulations, other relevant legislation and requirements imposed by the Pensions Regulator; and
- the effective and efficient governance and administration of the scheme.

The Board has exercised oversight of the activities of the Pension Fund Committee in relation to the results of the triennial valuation, changes to investment strategy and the implementation of the local government pension pools through the Surrey Fund's membership of the Border to Coast Pension Pool.

The Board has closely tracked the administrative performance of the Fund and its impact on member and employer experience, through quarterly KPI's and reports on projects, systems changes and broader changes in pension's legislation and best practice guidance.

The Board has oversight of the Fund's risk management practices and risk registers.

The Pension Fund Committee requested that the Board reviewed the Fund's approach to Environmental, Social and Governance (ESG) compliance, as part of its development of an Investment Strategy Statement. As result, the Board and Committee agreed an approach which evidenced how responsible and sustainable investment informs our collective fiduciary responsibilities. The Board reviewed the policies of peers in Autumn 2017, in order to identify areas of good practice, and made a series of recommendations which are being used by the Pension Fund Committee to develop its investment strategy.

In order to streamline the practices of the Local Pensions Board and the Pension Fund Committee, we have agreed a revised protocol whereby the Board meets some weeks before the Committee, and takes the lead in reviewing administrative performance and projects, and the risk register, and reporting issues of concern to the Committee. The Board also reviews the activities of the Committee at each meeting, making comments back as required.

Following the County Council elections in May 2017, the members of the Board were re-appointed, with the exception of John Orrick, who served as the Vice-Chairman of the Board and stood down as a councillor. His input and assistance was invaluable, and the Board has

benefited greatly from his experience. We welcomed Graham Ellwood, who joined us as an employer representative (Surrey County Council) and Vice-Chairman.

The meetings of the Surrey Local Pension Board are held in public. We would always welcome anyone with an interest to attend and see how the Board operates. We are also open to suggestions from both employers and members about how it can best support them.

You can find out more by writing to the Board's supporting officer, Sharmina Ullah at sharmina.ullah@surreycc.gov.uk or phoning 0208 213 2838.

Nick Harrison

Chairman of the Surrey Local Pension Board
July 2018

To secure compliance with the Regulations, any other legislation relating to the governance and administration of the Scheme, and requirements imposed by the Pensions Regulator in relation to the Scheme.	How the Board does this
a) Review regular compliance monitoring reports which shall include reports to and decisions made under the Regulations by the Committee.	The Board and Committee receive regular updates regarding their respective activities. The Board and Committee are committed to working together.
b) Review management, administrative and governance processes and procedures in order to ensure they remain compliant with the Regulations, relevant legislation and in particular the Code of Practice.	The Board has oversight of Pension Fund policies and processes. The Board reviews Key Performance Indicators (KPIs) for pension administration on a quarterly basis.
c) Review the compliance of scheme employers with their duties under the Regulations and relevant legislation.	The Board reviewed employer pension discretions in July 2016, and has continued to monitor compliance over the past year.
d) Assist with the development of and continually review such documentation as is required by the Regulations including Governance Compliance Statement, Funding Strategy Statement and Statement of Investment Principles.	This was reviewed as part of the Fund Annual Report on 12 October 2017, with specific policies also reviewed periodically in 2017/18 meetings. The Board will review these on an annual basis as part of the Fund Annual Report and as part of its Forward Plan.
e) Assist with the development of and continually review scheme member and employer communications as required by the Regulations and relevant legislation.	The Board was provided with an outline of the current communications channels for members and employers as part of a training session in October 2015. This is an item for fuller consideration 2018/19.
f) Monitor complaints and performance on the administration and governance of the scheme.	The Board reviews complaints on a quarterly basis.
g) Assist with the application of the Internal Dispute Resolution Process.	The Board receives a quarterly update on the number of Internal Dispute Resolution Process cases and monitors any key themes emerging from these.

h) Review the complete and proper exercise of Pensions Ombudsman cases.	N/A – No current or outstanding Ombudsman cases to consider.
i) Review the implementation of revised policies and procedures following changes to the Scheme.	N/A – No changes. The Board is fully conversant on current proposed changes to the LGPS regulations through regular bulletins.
j) Review the arrangements for the training of Board members and those elected members and officers with delegated responsibilities for the management and administration of the Scheme.	The Board will review its own training needs on an annual basis. A knowledge and understanding log is included in the Board's annual report. All Board members are required to complete the Pension Regulator Public Sector toolkit in order to comply with the Board's Attendance, Knowledge and Understanding policy.
k) Review the complete and proper exercise of employer and administering authority discretions.	The Board reviewed these discretions on 7 July 2017.
l) Review the outcome of internal and external audit reports.	The Board complies with Surrey County Council's agreed process for internal audit reports being considered by scrutiny boards. This means all relevant audit reports are circulated to the Chairman, and any report with one or more high priority recommendation will be considered for discussion at the Board. The results of any external audit are shared with the Board.
m) Review draft accounts and scheme annual report.	The Board received both the draft accounts and fund annual report on 12 October 2017.
n) Review the compliance of particular cases, projects or process on request of the Committee.	N/A
o) Any other area within the core function (i.e. assisting the Administering Authority) the Board deems appropriate.	N/A

27 July 2017

- Committee update: 27 July 2017
- Administration Internal
- Key Performance Indicators: Quarter Four
- Customer Complaints report: Quarter One
- Review of Internal Dispute Resolution Cases 2016/17
- Data Quality Assurance
- Risk Register
- Scheme Advisory Board Survey
- Pension Administration Strategy Scoping Document
- Administration Risk Register
- Service Specification Scoping Document
- GMP Reconciliation

12 October 2017

- Committee Update: Investment Strategy Statement Report
- Environmental, Social and Governance Compliance
- Administration Audit Progress Report
- Key Performance Indicators: Quarter One
- Annual Benefit Statement 2017
- New Performance Metrics
- New Service Specification between the Pension Fund and the Pension Administration Function
- Draft Administration Strategy
- Administration Risk Register
- Review OF Internal Dispute Resolution Cases in 2017/18: Quarter One
- Breaches Log
- GMP Reconciliation Update
- Local Pension Board Annual Report 2016/17
- Annual Accounts 2016/17

18 January 2018

- Reorganisation of the Surrey Pension Fund Team
- Summary of the Pension Fund Committee meeting(s): 10 November 2017 and 29 November 2017
- Administration Performance Report: 1 October 2017 to 31 December 2017
- Administration Update: 1 October 2017 to 31 December 2017

- Review of Internal Dispute Resolution Cases in 2017/18: Quarter One
- Risk Registers 2017/18: Quarter Three
- Administration Strategy Update

23 April 2018

- Summary of Pension Fund Committee Meeting(s): 9 February 2018 and 26 March 2018
- Administration Update: 1 January 2018 to 31 March 2018
- Administration Performance Report: 1 January 2018 to 31 March 2018
- Risk Registers 2017/18: Quarter Four
- Review of Internal Dispute Resolution Cases in 2017/18: Quarter Four
- Transition Plan
- Annual Service Review and Continuous Improvement Report
- Training Bulletin: Quarter Four

Members of the Local Pension Board

Name	Representing	Appointed	Appointment ended
(NH) Nick Harrison (Chairman)	Scheme employers	17 July 2015	N/A
(GE) Graham Ellwood (Vice Chairman)	Scheme employers	14 June 2017	N/A
(PB) Paul Bundy	Scheme employers	17 July 2015	N/A
(TH) Tina Hood	Scheme members	29 January 2016	N/A
(PR) Paresh Rajani	Scheme members	3 May 2016	N/A
(DS) David Stewart	Scheme members	17 July 2015	N/A
(CW) Claire Williams-Morris	Scheme employers	17 July 2015	N/A
(TW) Trevor Willington	Scheme members	17 July 2015	N/A

Meeting attendance

Meeting date	In attendance	Apologies
27 July 2017	NH, GE, DS, PR, CW, TW	PB, TH
12 October 2017	NH, GE, DS, PR, CW, TW	PB, TH
18 January 2018	NH, GE PB, TH, PR, CW TW	DS
23 April 2018	NH, GE, PB, TH, PR, DS, TW, CW	

Compulsory training

Training	Attained
The Pensions Regulator Public Sector Toolkit	NH, PB, PR, DS, CW TW
Local Government Association Fundamentals 1	NH, PB, TH, PR, DS, CW TW
Local Government Association Fundamentals 2	NH, PB, TH, PR, DS, CW TW
Local Government Association Fundamentals 3	NH, PB, TH, PR, DS, CW TW

Additional training

Training	In attendance
ESG Training	PR,DS,NH,PB,CW,TH
Pension Committee Induction	PR,DW,TW,NH,PB,TH

Publications distributed to all Local Pension Board members

Local Government Pension Secretariat bulletins	157-169

Board expenditure

Chairman and Vice-Chairman Allowances	£5,500.00
LGA Training	£1,440.00
Total:	£6,940.00

The Public Service Pensions Act 2013, Section 5(4) requires that any member of a Pension Board must not have a "conflict of interest", which is defined in Section 5(5) as a "financial or other interest which is likely to prejudice the person's exercise of functions as a member of the board, but does not include a financial or other interest arising merely by virtue of membership of the scheme or any connected scheme."

A conflict of interest exists where there is a divergence between the individual interests of a person and their responsibility towards the Local Pension Board, such that it might be reasonably questioned whether the actions or decisions of that person are influenced by their own interests.

A conflict of interest would prejudice an individual's ability to perform their duties and responsibilities towards the Local Pension Board in an objective way.
An example of a potential conflict of interest could be:

A Local Pension Board member may be required to review a decision which may be, or appear to be, in opposition to another interest or responsibility; e.g(s):

- a review of a decision which involves the use of departmental resource in the function of the Local Pension Board, whilst at the same time being tasked with reducing this departmental resource by virtue of their employment;

- a Local Pension Board member could also be employed or have an interest in either privately or as part of the Council in a service area of the Council for which the Local Pension Board has cause to review;

- an independent member of the Local Pension Board may have a conflict of interest if they are also advising the Scheme Manager.

Name	LGPS Member/ Employer Representative	Date of Appointment / Termination (if applicable)	Relevant employment or positions held	In receipt of a LGPS pension ?	Stated Conflict with Employment ?	Additional note	Other Conflicts of Interest
Nick Harrison	Employer	17/07/2015	Elected Member of Surrey County Council; Trustee director of a company pension scheme, DB Pension Fund Trustee Ltd.	No	No	Deutsche Bank itself has no role in relation to the Surrey Pension Fund and no role more generally in providing banking, investment or other services to Surrey County Council.	N/A
Graham Ellwood	Employer	14/06/2017	Elected Member of Surrey County Council; RI of Wilton Wealth Management Ltd	No	No	N/A	N/A
Paul Bundy	Employer	17/07/2015	Head of Finance, Surrey Police	No	Yes	Employed by an employer of the fund. If a conflict was to arise, this would be mitigated by the Board member removing himself from the discussion.	N/A
Tina Hood	Member	29/01/2016	GMB Branch Secretary Surrey County Branch County Hall	Yes	No	N/A	N/A

Claire Morris	Employer	17/07/2015	Head of Financial Services and Deputy Chief Financial Officer, Guildford Borough Council	No	Yes	Employed by an employer of the fund. If a conflict was to arise, this would be mitigated by the Board member removing herself from the discussion.	N/A
Paresh Rajani	Member	03/05/2016	Electrical Services Engineer, Neighbourhood & Housing Management Services, Guildford Borough Council; Unison representative	No	No	Employer not involved in financial business.	N/A
David Stewart	Member	17/07/2015	Shared Performance and Reward Manager (LBHF and RBKC), Shared Human Resources London Borough of Hammersmith & Fulham/Royal Borough of Kensington & Chelsea	Yes	No	Employer's pension services are administered by Orbis - this is actively managed by being recorded at every meeting, and any likelihood of conflict arising would be mitigated by the member removing himself from the discussion.	N/A
Trevor Willington	Member	17/07/2015	Governor, North East Surrey College of Technology	Yes	No	Employer not involved in financial business.	N/A

Knowledge and Skills Policy

The administrators of the Surrey Pension Fund are committed to the implementation of the Code of Practice on public sector pensions finance knowledge and skills. The Pension Fund Committee has agreed the following knowledge and skills policy statement.

1. The Pension Fund Committee recognises the importance of ensuring that all staff and members charged with the financial administration and decision-making with regard to the pension scheme are fully equipped with the knowledge and skills to discharge the responsibilities allocated to them.

2. It therefore seeks to utilise individuals who are both capable and experienced and it will provide/arrange training for staff and members of the Committee to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills

.

The members of the Committee are to partake in the CIPFA Knowledge and Skills Framework in order to identify areas where further training is required.

12 Communication Policy Statement

1 Communication Objectives

- To accurately communicate the provisions and requirements of the Local Government Pension Scheme (LGPS) to all stakeholders.
- To identify and meet all regulatory requirements regarding provision of information.
- To promote appropriately membership of the LGPS Scheme to employees of participating employers.
- To communicate clearly to all stakeholders their own responsibility for communication and information flows in relation to the Scheme, and work with these other parties to improve efficiency of communications.
- To ensure communications are made in a timely manner.
- To use a variety of means for communication, depending on the purpose and content of the communication, and recognising that different styles and methods will suit different stakeholders.

2 Stakeholders

The various stakeholders for the purpose of this communication policy are identified below:

- Active members
- Prospective members
- Deferred members
- Pensioners
- Employers

3 Website

The Pension Fund has an established website:

surreypensionfund.org

Method of Communication	Media	Frequency of issue	Method of Distribution	Audience Group (Active, Prospective, Deferred, Pensioner, Employer or All)
Scheme overview and joiner form	Paper based and on website	On commencing employment and by request	Via employer	Active and prospective
Scheme booklet and joiner pack	Paper based and on website	On joining the scheme and by request	Home address or via employer	Active and prospective
Factsheets	Paper based and on website	On request	Post to home address or email	Active and deferred
Newsletters	Paper based and on website	After material scheme changes	Via employer	Active and Pensioner
Annual benefit statements	Paper based	Annually	Post to employer or home address	Active and Deferred
Pension clinics/roadshows and drop-in events	Face to face	As requested by employer and employee	Via employer	Active and prospective
Pre-retirement courses	Face to face	As requested by employer	Via employer	Active
Briefing reports	Paper based and electronic	Ad hoc	Email or hard copy	Employers
Formal dispute resolution procedure	Paper based or electronic	As and when a dispute arises	Email or hard copy	All
Investment updates	Website	Quarterly	On request	Employers
Annual report and accounts	Paper based, electronic or website	Annually	Email or hard copy	All
Annual general meeting	Face to face	Annually	Email invitation	Employers
Actuarial valuation report	Electronic or website	Triennial	Email	All

Surrey Pension Fund Administration Strategy

1. Legislative Framework

1.1 This strategy statement has been prepared by Surrey County Council as the administering authority to the Surrey Pension Fund in accordance with Regulation 59 of the Local Government Pension Scheme) Regulations 2013.

2. Review

2.1 This strategy will be kept under review and will be revised, after consultation with scheme employers, following any material changes in legislation or policies that relate to the strategy.

3. Purpose

3.1 The purpose of the strategy is to establish levels of performance and procedures for liaison and communication for both the administering authority (AA) and the employers participating in the fund with a view to maintaining good working relationships, transparency and efficient administration.

4. Employer Duties & Responsibilities

4.1 The employer should nominate a person or persons to liaise with the AA on pension administration matters.

4.2 The employer should ensure that any information passed on behalf of the employer to the AA or any requests for information made on behalf of the employer to the AA are undertaken by a duly authorised officer of the employer.

4.3 The employer should notify the AA in respect of the following changes in a scheme member's status and within the required timescale by completing the appropriate pension form or secure on-line submission:

- New Joiner
  Within one month of joining

- Change in member's details e.g. hours, maternity etc
  Within one month of the change

- Retirements
  Two months prior to the date of retirement. It is however recognised that there will be occasions where this time limit cannot be met, for example, because the member has

retired with little or no notice or details of pensionable pay cannot be provided until the member has left employment.

- Death in Service
  Within five working days of the member's death

- Leavers
  Within one month of the member leaving

- TUPE transfer of scheme member
  At least two months before the transfer date. This is to allow adequate time for pension protection to be put in place as appropriate.

4.4 The employer must determine the pension contribution rate at which its employees should contribute to the scheme from 1 April each year and, where there is a change to the member's pensionable pay during the year, from that date. Where an employee holds more than one post, the employer must determine the rate applicable for each post.

4.5 The employer will ensure that member and employer pension contributions are deducted at the correct rate, including contributions due on leave of absence with reduced or no pay, maternity leave and any additional contributions the member has requested to pay.

4.6 The employer will ensure that pension contributions are paid to the AA within seven days of the end of each month.

4.7 The employer will ensure that additional voluntary contributions are paid to the relevant provider within seven days of being deducted from the member's pay.

4.8 The employer must, no later than 30 April each year, provide the AA with year-end information to 31 March in an approved format in respect of each post the member holds.

4.9 The employer is responsible for exercising the discretionary powers given to employers by the LGPS regulations. The employer is also responsible for publishing its policy in respect of these discretions to its employees and forwarding a copy to the AA.

4.10 The AA is not required to verify the accuracy of any information provided by the employer for the purpose of calculating benefits under the provisions of the Local Government Pension Scheme. Therefore, employers should ensure that all information provided is accurate.

4.11 Any over-payment resulting from inaccurate information supplied by the employer may be recovered from the employer if it cannot be recovered from the scheme member.

4.12 In the event of the AA being fined by The Pensions Regulator, this fine may be passed on to the relevant employer where that employer's action or inaction resulted in the fine.

4.13 The employer must nominate a person to hear complaints made under Stage 1 of the Internal Disputes Resolution Procedure and should provide this person's name, job title, and office address. When an amendment to these details is made, a notification of the change should be sent to the AA immediately.

4.14 The employer must obtain the approval of the AA as to its choice of registered medical practitioner for the purposes of awarding ill health retirement under the Scheme regulations.

4.15 The employer must pay to the AA any cost identified by the AA as a result of the employing authority's decision to release any pension benefits prior to a member's normal retirement age. Such payments should be made within 30 days from the date of receipt of an invoice issued by the AA or such longer period as agreed by the AA.

4.16 The employer must also pay to the AA any charge identified by the AA as a result of the employing authority's decision to award any additional benefits to a scheme member in accordance with its statement of policy regarding the exercise of certain discretionary functions. Such payments should be made within 30 days from the date of receipt of an invoice issued by the AA or such longer period as agreed by the AA.

5. Administering Authority Duties & Responsibilities

New Joiners

5.1 *Confirmation letter of scheme admittance to all members*.
Within 20 days

5.2 *Transfers from previous pension schemes.*
Within 20 days

Existing Active Members

5.3 *Annual Benefit Statement*
By 30 September providing year end data has been received from the employer

5.4 *Benefit estimates to employers*
Within ten days of receipt of request

5.5 *Retirements*
Within ten days of retirement

5.6 *Death in Service*
Death Benefits and dependants' pensions
Within five days

Early Leavers

5.7 *Deferred Benefit statement*

Within one month of leaving

5.8 *Refunds*
Within ten days

5.9 *Transfer to new pension scheme*
Within 20 days

Deferred Benefit Members

5.10 *Annual Benefit Statement*
By 30 June

5.11 *Benefits put into payment*
Within ten days

5.12 *Death Benefits and dependants' pensions*
Within five days

Pensioner Members

5.13 *Changes in personal details*
Payroll record updated before next payroll run

5.14 *Death benefits and dependants' pensions*
Within five days

*The timescales for completing the tasks above are measured from the date the AA is in receipt of all the relevant information required to complete the task is expressed in "working days"

Communication

5.15 The AA will provide employers with the necessary forms and documents for it to carry-out its pension administration responsibilities. These forms to be available in paper and electronic format, where appropriate
.

5.16 The AA will provide a guide to the Local Government Pension Scheme for scheme members for employer to issue.

5.17 The AA will provide a joiner pack to new scheme members.

5.18 The AA will issue a newsletter for active scheme members at least once a year

5.19 The AA will issue regular employer newsletters and provide training at County Hall for employers to comply with their pension administration responsibilities.

5.20 The AA will enable scheme members and employers to visit Pension Services during normal working hours from 8.30am to 5.30pm.

5.21 The AA will maintain a Pension Fund Website which will include:

- General information on the LGPS
- Copies of all the publications of the pension fund including newsletters, scheme guides, strategy statements, annual reports and accounts.
- Standard forms to be used by employers when providing information to the pensions team

5.22 The AA will arrange a Pension Fund Annual General meeting for employers and produce an annual report.

Data Quality and Security

5.23 The AA will ensure that the data held on the systems used to administer the scheme will be secure and regularly backed up to an off-site location. The AA will apply year end data quality control and review processes.

6. Unsatisfactory Performance by an Employer

6.1 Where an employer materially or consistently fails to operate in accordance with the standards laid down in this strategy, which results in additional administration costs being incurred by the AA, the AA may issue a written notice to the employer requiring that these extra costs are met by the employer. Steps to recover additional administration costs would normally only be pursued after support and training had been offered by the AA to address the underperformance.

Investment Report

12

Annual Investment Report

This report has been prepared by Anthony Fletcher "Independent Investment Advisor" to Surrey County Council Pension Fund (the Fund). At the request of the Pension and Investment Committee the purpose of the report is to fulfil the following aims: -

- Provide a review of the economic and market background over the 12 months to 31st March 2018.
- Provide an overview of market returns by asset class over the last 12 months.
- Provide an overview of the Fund's performance versus the Fund specific benchmark for the last 12 months.
- An overview of the outlook for markets and how this may impact the performance of the Fund.

1. Economic Background

In the year to 31st March 2018 the global economy continued to enjoy stronger and more globally synchronised growth and relatively subdued inflation. The US grew at a rate of 2.8% year over year; Europe (2.4%) and Japan (1.1%) saw their strongest growth rates of recent years. In aggregate growth rates in the emerging economies were higher than in the developed economies, with China achieving 6.7% growth over the period. The UK was a notable exception to the generalised improvement seeing growth decline from 2% to 1.6% and inflation increase over the period, as the lingering effects of the weakness of Sterling and low real wage growth worked their way through the data. The price of Brent Crude oil rose from $54 to $69 during the year, stimulated by production curbs imposed by OPEC and Russia, as well as by stronger economic activity globally. While the annual growth numbers are strong, as can be seen in Chart 1 below the initial estimates of quarterly growth in the first quarter of 2018 have dropped off somewhat, and as can be seen in Chart 2, inflation rates are higher than they were 12 months ago, but outside the UK they remain below central bank target rates.

Chart 1: - Quarterly GDP growth rates.

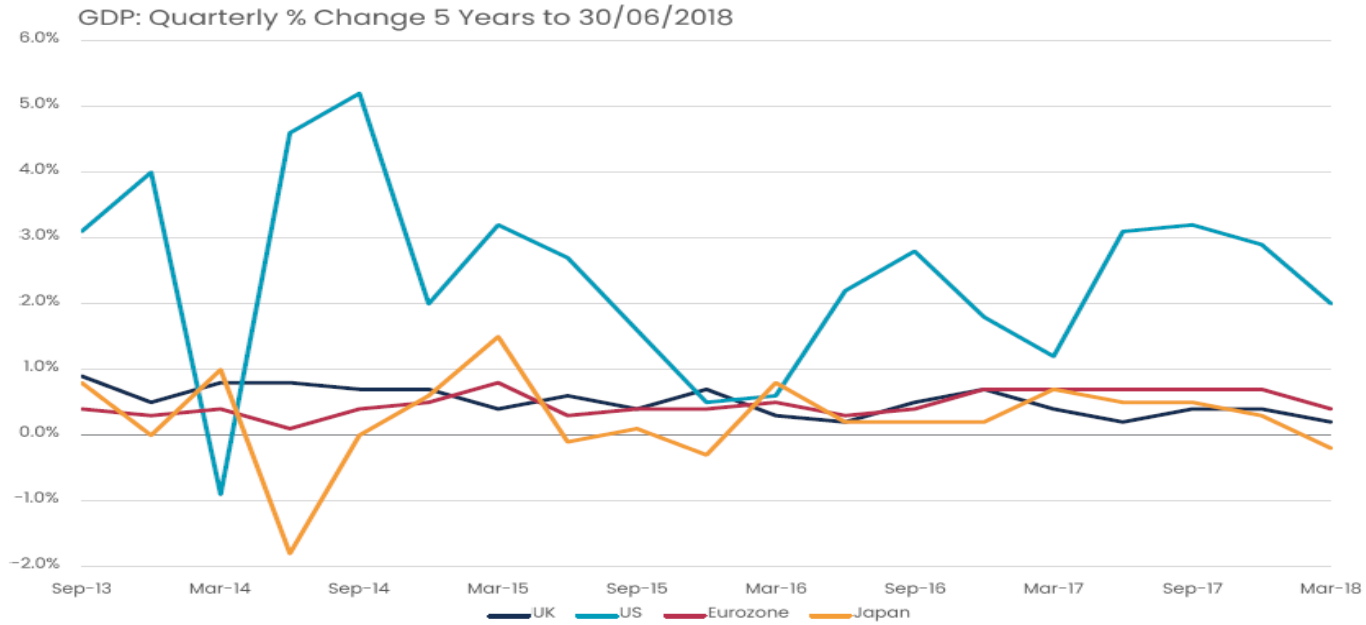
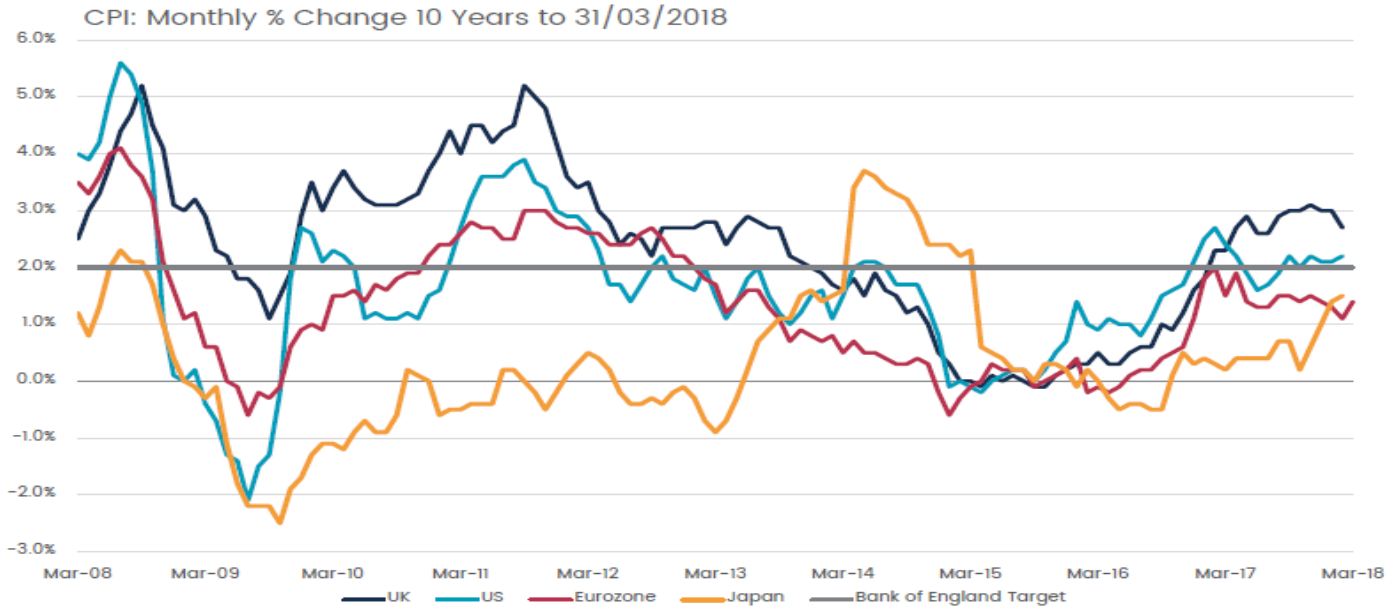


Chart 2: - Inflation remains at or below the central bank target rate of 2%.



Source: - Charts 1 and 2 Bloomberg

As a result of the economic improvement, the period of special monetary measures (QE) embarked on by the world's central banks after the Financial Crisis of 2007/08 is beginning to wind down. The US Federal Reserve increased it Fed funds rate by 1% from 0.75 to 1.75% during the year and announced that it would start to reduce its balance sheet by not re-investing the proceeds of maturing bonds. The Bank of England (BoE), meanwhile, raised the UK base rate by 0.25% in November, taking back the emergency cut it made following the BREXIT referendum. While the European Central Bank (ECB) and the Bank of Japan (BoJ) left rates unchanged, the European Central Bank halved its monthly purchases of bonds to €30bn from January 2018 and the Bank of Japan continues with its programme of bond-buying, targeting a 0.1% yield on 10 year government bonds.

After the political surprises and concerns about the rise of populism in Europe at the start of the year (March 2017), the impact on economies and markets of the political events over the last 12 months has been subdued. In Europe there were concerns over French and German elections, but in the end in France Emmanuel Macron was elected President at the head of a new centrist party, while several months after the German elections the CDU/CSU renewed its coalition with the SDP, allowing Angela Merkel to remain as Chancellor. However, In June, the snap UK election called by the Prime Minister resulted in a loss of the Conservatives' overall majority, and they entered into a pact with the DUP to ensure they still had a working majority in Parliament. Negotiations on the terms of Britain's exit from the EU are continuing, amid disagreements within the Conservative party about many of the detailed arrangements. And following the collapse of the government in Italy over constitutional reform, a new Italian general election in March 2018 has produced an uncertain outcome after the big gains registered by the Five Star Movement and the ring-wing Lega (formerly the Northern League) parties.

The United States Congress approved the Tax Bill in December, sharply cutting the Corporation Tax rate and also reducing the top rate of Income Tax. President Trump announced the imposition of tariffs on imports of steel and aluminium from certain countries, and has threatened to put tariffs

on a range of Chinese goods, to which China has responded with its own list of items to be penalised if the US tariffs come into force. Russia has been the subject of diplomatic responses and further sanctions from the West following the alleged poisoning of two Russians in England.

2. Market Returns

After the strong returns from markets in the year to 31st March 2017, the markets produced much lower returns in the period to the end of March 2018, see Table 1. To some extent the lower returns were a consequence of a recovery in Sterling but the 1st quarter of 2018 saw the first negative quarterly returns for global equity markets since the 1st quarter of 2016.

Table 1, below shows the total investment return in pound Sterling for the major asset classes, using FTSE indices except where noted; for the 3 and 12 months to the end of March 2018.

% Total return dividends reinvested

Market returns

	Period end 31st March 2018	
	3 months	**12 months**
FTSE All-Share	-6.9	1.3
MSCI ACWI – Global Equities	-4.2	3.1
FTSE Regional Indices		
North America	-4.5	1.3
Europe ex UK	-4.4	4.3
Japan	-2.6	7.5
Pacific Basin	-4.5	6.0
Emerging Equity Markets	-2.2	8.8
UK Gilts - Conventional All Stocks	0.3	0.5
UK Gilts - Index Linked All Stocks	0.1	0.5
UK Corporate bonds*	-1.4	1.4
Overseas Bonds**	0.3	1.6
Property IPD quarterly	2.9	10.9
Cash 7 day LIBID	0.09	0.21

* Merrill Lynch £ Corporate Bond; **Citigroup WGBI ex UK hedged

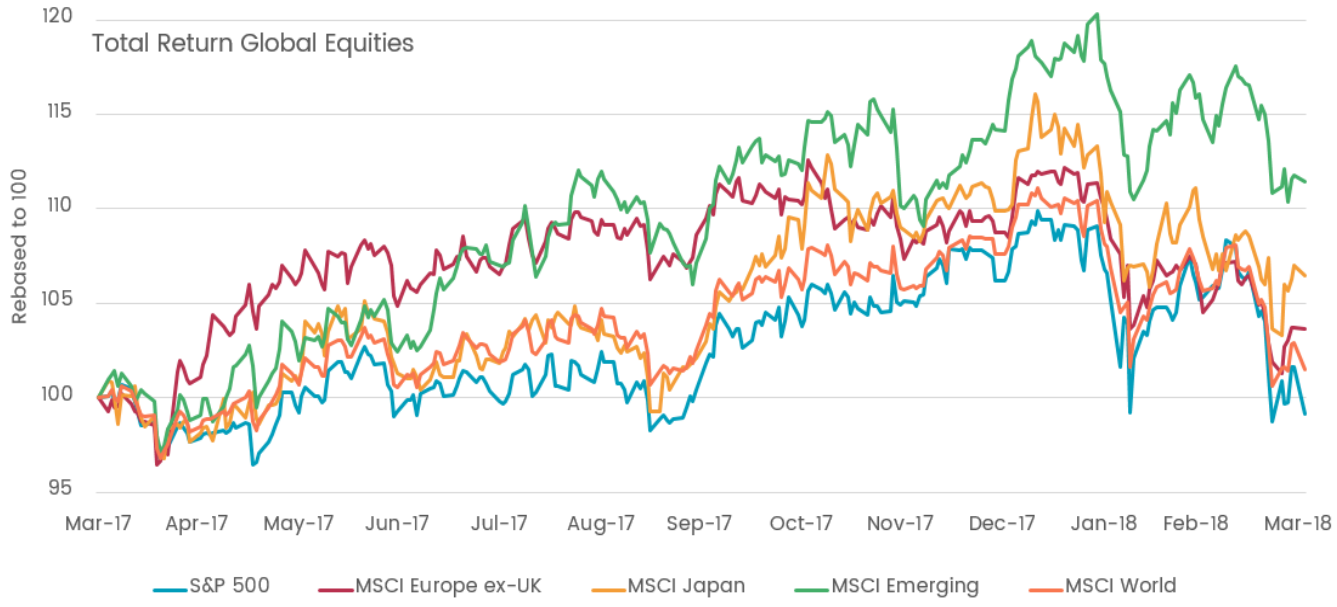
From Chart 3 below, we can see that global equity markets in Sterling terms moved gently higher throughout during the year. The strength shown from October – January was swiftly cancelled out by sharp falls in early February when investors became concerned about a possible rise in inflation in the US. After the exceptionally strong preceding year, Global Equities gave a total return of just

3.1% (in £) in the year to March 2018. Within this figure, Emerging Markets (+8.8%), Japan (+7.5%) and Asia Pacific ex-Japan (+6.0%) were the strongest regions, while North America and the FTSE all Share (+1.3%) see Chart 4, were laggards.

In the year to March 2018, the pound gained 12% against a generally weak US dollar, and 7% against the Japanese yen, but lost 4% against the euro. The yield on 10-year US Treasury bonds rose from 2.4% to 2.75% during the year, in response to the rate increases by the Federal Reserve and signs of rising inflation, while yields on UK and German government bonds were little changed for the year as a whole. Index-Linked Gilts were also flat, gaining just 0.5% during the year.

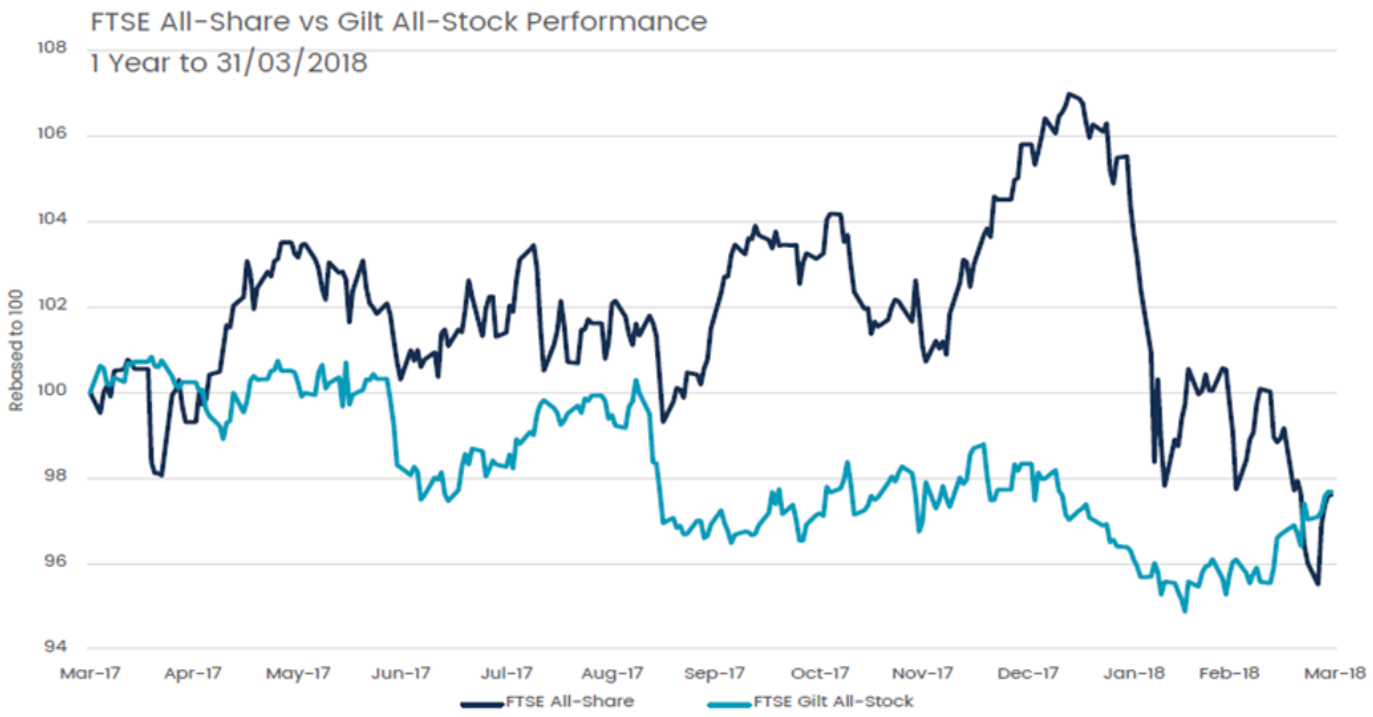
UK Commercial Property recorded a solid total of 10.9%, comprising a return of 21.6% from Industrial Property, 8.6% from Offices and 7.1% from Retail.

Chart 3: - Total return of overseas equity markets in Sterling terms, last 12 months.



Source: - Bloomberg

Chart 4: - UK bond and equity markets since 31st March 2017



Source: - Bloomberg

3. Fund Performance and Manager

At the end March 2018, the Surrey Pension Fund was valued at £4,025.6 million, this represents a total increase in value of £156.7 million, since 31st March 2017. The Fund achieved a total net investment return of 3.9% for the year, outperforming the benchmark return of 3.6%.

All managers produced lower total returns than last year and returns were also more mixed reflective of their individual style biases. Drilling down into performance versus benchmark and target over the 12 months for UK equity UBS outperformed benchmark and target and Majedie had a very difficult year. The combined returns from global equity were also lower than benchmark and target. Western, the active bond manager performed broadly in-line with their benchmark and target. Returns from the portfolio of DGF funds were also mixed, but these funds have been chosen specifically for their style diversification and contrasting investment approaches. The strongest absolute return was achieved by CBRE the property manager demonstrating the value of this asset class as a source of diversified returns. It was pleasing to see that all of Surrey's equity managers produced smaller negative returns than the markets in 1q18.

I believe it is more valuable to look at the returns over a longer time horizon and using the data provided by Northern Trust, over the last 3 years, the Fund has delivered an investment return of 7.3% pa compared to its benchmark return of 6.8% pa.

The Surrey Pension Fund has made no material changes in asset allocation strategy during the year.

4. Economic outlook

The strong synchronised global expansion which began in 2016 appears to be showing some signs of slowing in 2018, and inflation has picked up in most regions, although economic data remains positive. In the US and Eurozone, declines in manufacturing and purchasing managers' indices suggest potentially slower (although still positive) growth to come. However as Chart 5a shows the current consensus estimates for growth in 2018, compared to last year's remain positive.

Chart 5a: - Real GDP expectations 2017 and 2018;

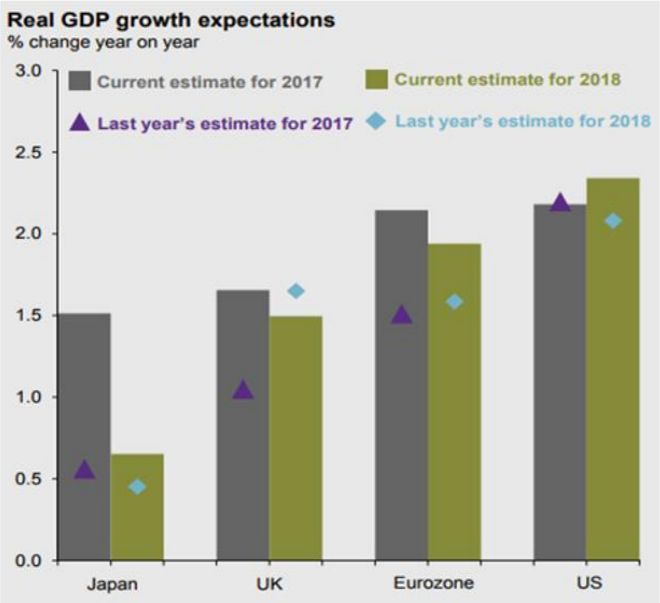
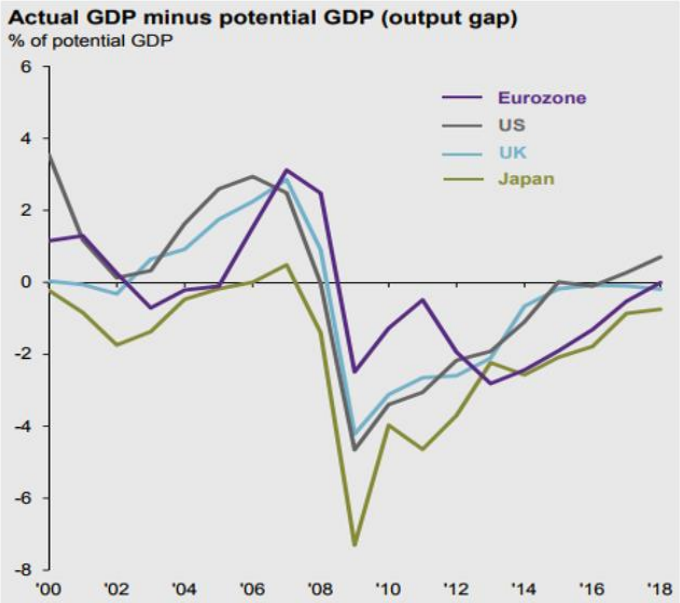


Chart 5b: - Output Gaps



Source: - JPM Asset Management

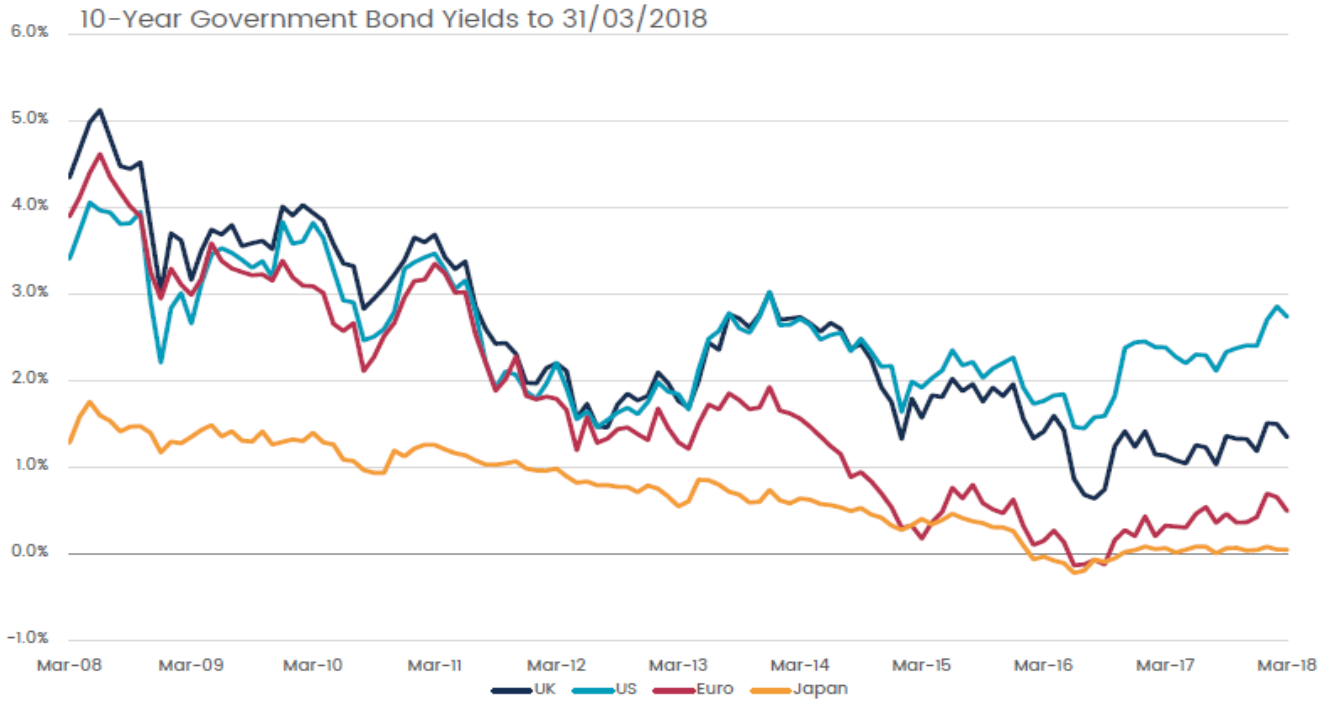
In terms of Inflation (see chart 2), US inflation has ticked up causing some concern that the US Fed may become more activist. However the rise in oil prices may dampen expectations as the increase has taken back about half the value of the income tax cut. As predicted by the Bank of England, UK inflation has started to fall as the weakness of sterling washes through the data. Outside of the US stronger activity has not translated into higher inflation, because the other economies have yet to exceed their respective "output gaps" (chart 5b above). The geo-political backdrop remains as uncertain as ever, with Russia's relations with the West, and the consequences of the Syrian conflict, now being supplemented as clouds on the horizon by potential trade wars involving the United States.

5. The outlook for markets

The markets expect global bond yields to continue to rise, led by the US, the Fed is likely to raise rates 2 or 3 times over the next 12 months and through their Quantitative Tightening programme, they will no longer be recycling coupons and principle repaid on their holdings of government bonds purchased during QE. Therefore it remains appropriate to focus on US government yields as the main driver of higher global government bond yields, see chart 6 below. Balanced against this the ECB and the Bank of Japan are keeping overnight interest rates negative, the ECB continues to buy bonds for QE (albeit at a lower rate) and in Japan 10 year yields pegged at 0.1%

as part of their QE programme. The resulting capital flow into the US Government bond markets may actually be keeping global government bond yields artificially low.

Chart 6: - Government bond yields, look set to continue to rise to more normal levels led by the US.



Source: - Bloomberg

The recent volatility and price correction in all equity markets, has bought 12 month market returns down to around 3%, but average returns are still above 8% pa for the last 10 years. This high level of average long term returns is unlikely to be sustained into the future and forecasters are expecting medium to long term average equity market returns to be around 4% for developed markets, but maybe as high as 7% for developing markets. The other factor supporting equity markets has been the uncharacteristically low volatility over the last 5 years, this is another market feature that is unlikely to persist. Lower aggregate returns and higher uncertainty are strong arguments for active rather than passive investment, it is also an argument for diversification. In terms of the macro-economic factors, investors should focus their asset allocation on markets where the secular as well as the cyclical factors still have upside potential and secondly on active asset managers with a proven ability to add value in all market conditions. It is still likely that equity markets can go higher, but returns have been high and valuations especially in the US have become extremely stretched, see chart 7. The total return from equities over the next 12 months is likely to be lower and more volatile than the 8% average we have become accustomed to.

Chart 7: - Global Equity returns, last 10 years.

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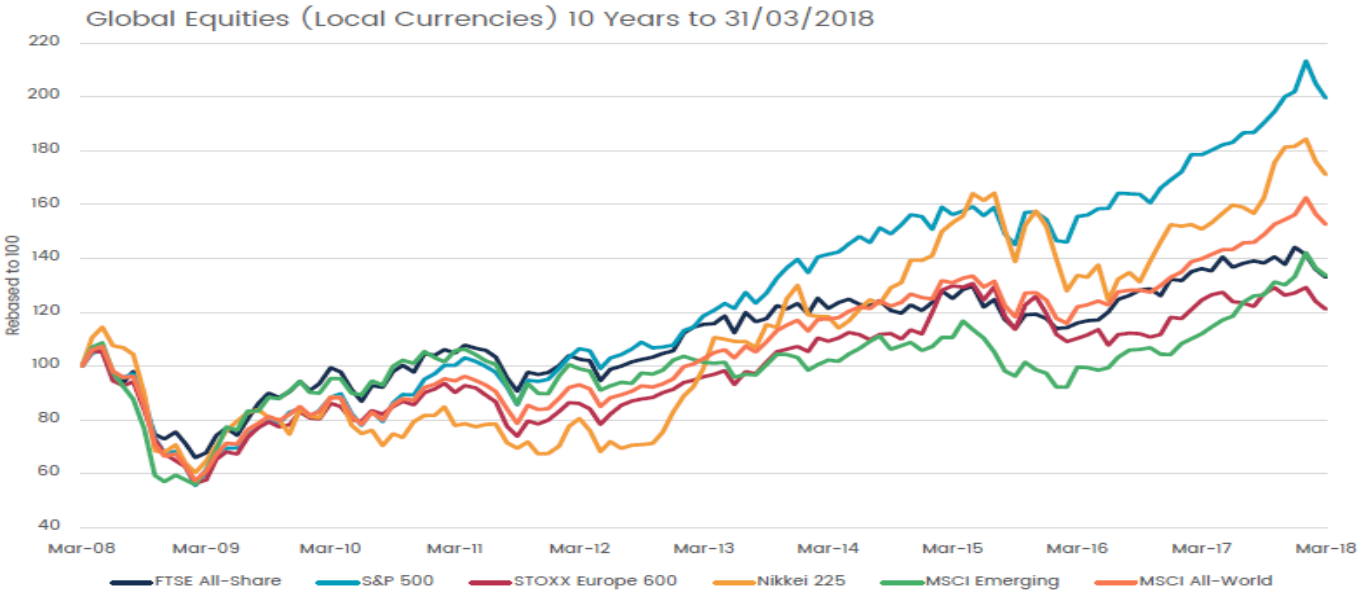

Source: - Bloomberg

After a prolonged period of unusually strong investment returns and unusually low market volatility, it is prudent to expect a rather less benign environment in the coming years. The investment strategy for the Surrey Pension Fund reflects the need to generate good long-term returns while smoothing short-term volatility through diversification in asset classes, geography, managers and investment styles. The bias remains on growth through a well-diversified portfolio of quoted and unquoted equities, bonds, property and actively managed Diversified Growth Funds (or DGFs).

Investment Arrangements

At Surrey the overall direction of the Fund's investment is the responsibility of the Pension Fund Committee. The Committee comprises

- 5 county council members
- 3 employer representatives
- 1 employee representatives
- 2 professional investment advisors

The Fund is managed on both an active and passive basis.

There are a number of external investment managers, who have been appointed to undertake day-to-day decisions on the allocation of investment between types of asset and choices of individual stocks within approved classes. They are required to take a long-term view, balancing risk against return and are remunerated on scales related to the value of funds under management and in certain cases for performance over and above benchmark return. Regular meetings are held with external managers to assess performance.

In addition the Fund has investments in private equity funds managed by Blackrock, Goldman Sachs, Hg Capital, Living Bridge Equity Partners, Capital Dynamics, Standard Life Capital Partners and Pantheon Access.

At 31 March 2018 the market value of assets under management was £3.8m, excluding the private equity portfolio, internally managed cash, and residual cash held by the custodian. The proportion with each of the investment managers is shown overleaf.

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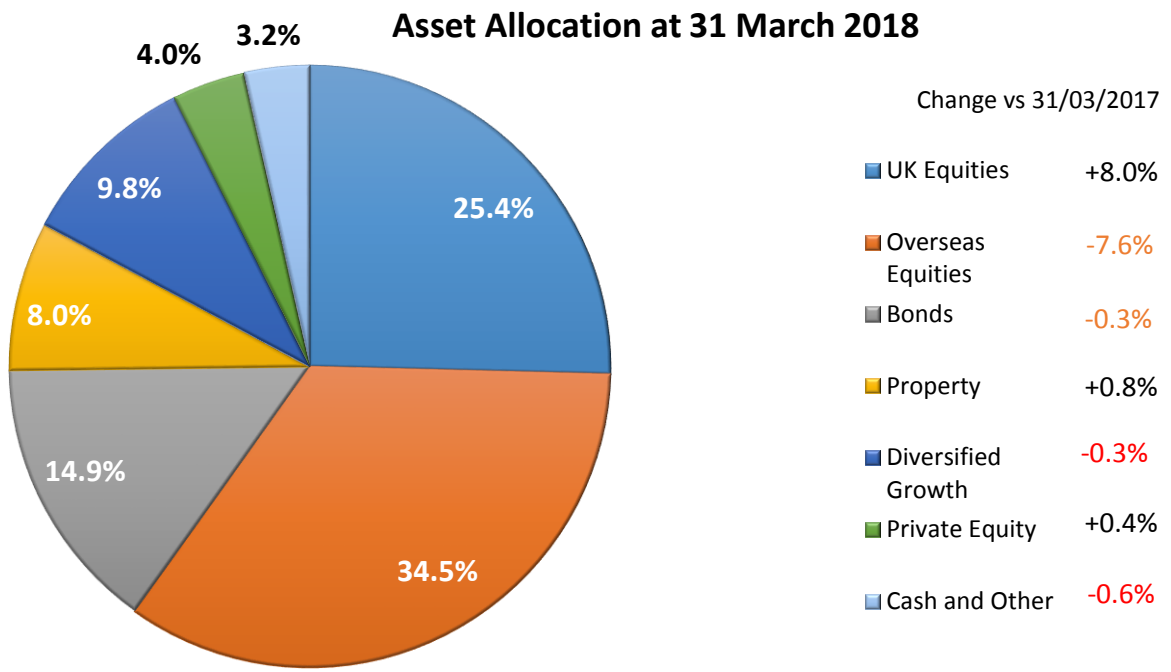
Investment Manager	Mandate	Market value 31 March 2018	Percentage of Funds Under Management
		£000	
Passive			
Legal & General Investment Managers	Multi Asset	1,151,591	28.6
Active			
Majedie Asset Management	UK Equities	373,811	9.3
UBS Asset Management	UK Equities	311,993	7.7
Marathon Asset Management	Global Equities	498,553	12.4
Newton Investment Management	Global Equities	317,106	7.9
Western Asset Management	Fixed Income	322,509	8.0
Franklin Templeton Investments	Unconstrained Fixed Income	73,663	1.8
Baillie Gifford Life Limited	Diversified Growth	150,596	3.7
CBRE Global Multi Manager	Property	260,170	6.5
Darwin Investment Management	Property	73,508	1.8
Ruffer	Diversified Growth	122,576	3.0
Aviva	Diversified Growth	121,117	3.0
Total		**3,777,193**	

The table above excludes the private equity partnerships, internally managed cash, residual cash held by the custodian and other investment balances.

Portfolio Distribution

The distribution of the Fund investments into different asset classes within the portfolio at 31 March 2018 is shown in the below chart, with the prior year allocation shown in the table below.



The chart below shows the investment breakdown by asset class over the last two years.

Change in actual asset allocation over the year.

	Asset Allocation Target	Actual Allocation 31 March 2017	Actual Allocation 31 March 2018	Movement in Year
Fixed interest securities	12.10%	10.00%	9.80%	-0.20%
Index linked securities	5.50%	5.20%	5.10%	-0.10%
Equities	59.80%	59.50%	59.90%	0.4%
Property unit trusts	6.20%	7.20%	8.00%	+0.80%
Diversified growth	11.40%	10.10%	9.80%	-0.30%
Private equity	5.00%	3.80%	3.90%	+0.10%
Cash and other	0.00%	4.20%	3.50%	-0.70%
Total	**100.0%**	**100.0%**	**100.0%**	

Investment Activity

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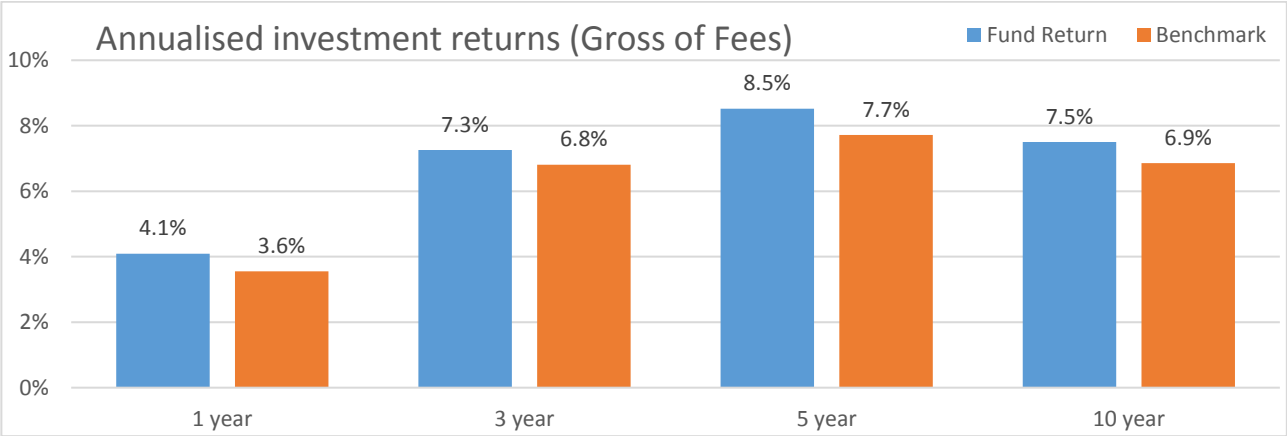
Twelve fund managers undertook the management of investments during 2017/2018 in a mix of passive and active investment. A summary of investment managers and the value of the assets under management is shown on page 31.

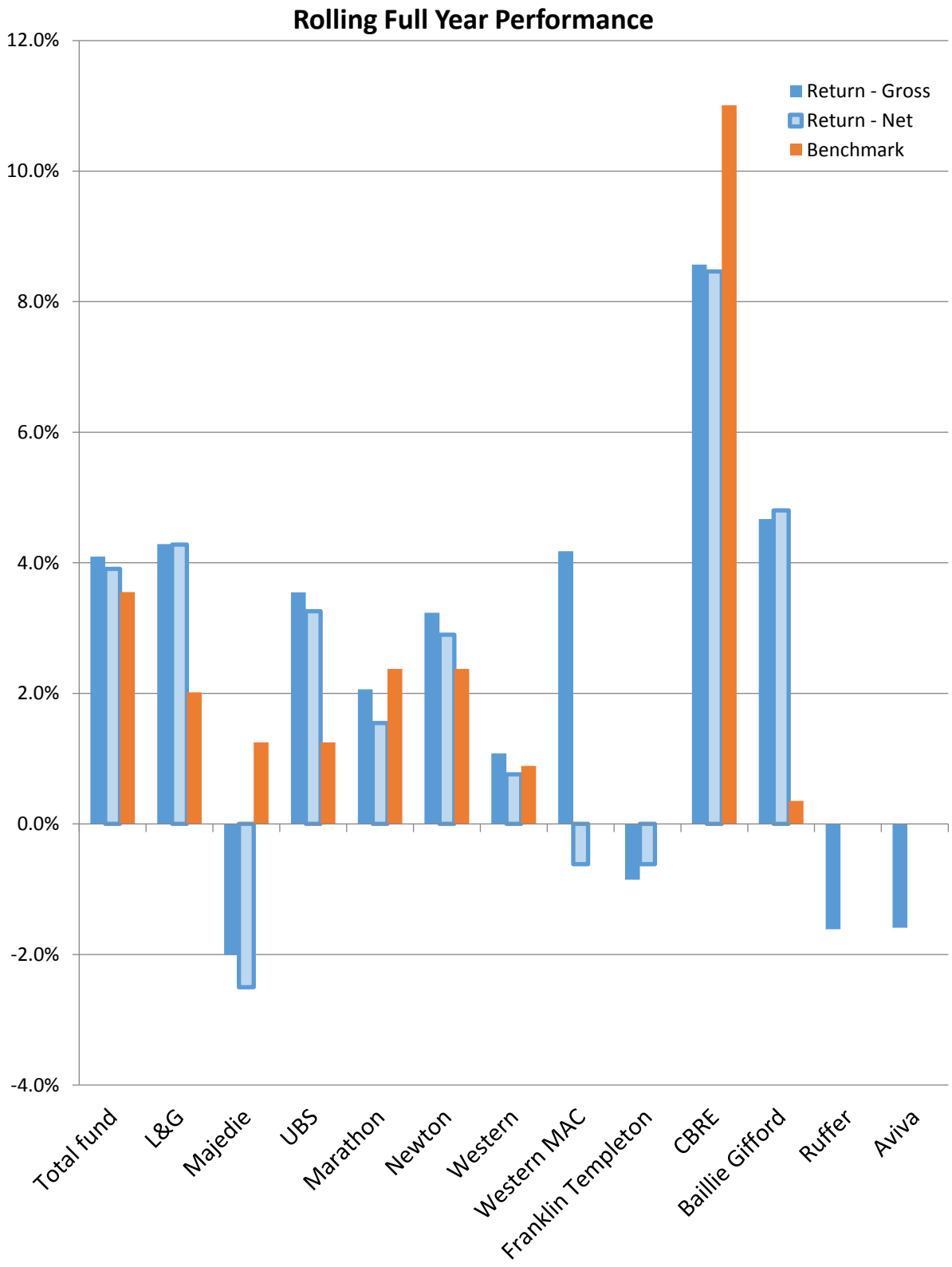
The Fund assess investment performance against a customized benchmark provided by the Fund custodian Northern Trust. This benchmark is derived from a series of investment indices weighted by the Funds asset allocation. This allows the Fund to measure performance against a 100% passive allocation.

Performance against target and benchmark is continually reviewed at regular intervals, as stated in the Fund's Statement of Investment Principles.

The graph below shows how the Fund performed against the benchmark, on an annualised basis, for the previous 1, 3, 5 and 10 year periods.



The fund recorded investment performance above that of the benchmark for the previous 12 months to 31 March 2018 as well as outperformance over the longer term 3 year period, shown in the above chart. The outperformance above the benchmark is partly a result of strong investment returns generated by actively managed portfolios. The annual investment returns as at 31 March 2018 for each fund manager are shown in the below table.


Rolling Full Year Performance
12.0%
10.0%
8.0%
6.0%
4.0%
2.0%
0.0%
-2.0%
-4.0%
Return - Gross
Return - Net
Benchmark
Total fund
L&G
Majedie
UBS
Marathon
Newton
Western
Western MAC
Franklin Templeton
CBRE
Baillie Gifford
Ruffer
Aviva

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The below table shows the investment return for each asset class for the twelve months to 31 March 2018. The table does not include the impact of the Fund's currency hedge.

	Annual Investment Return 12 months to 31 March 2018
Fixed interest securities	1.5%
Equities	2.8%
Property unit trusts	7.1%
Diversified growth	0.8%
Private equity	7.7%
Cash and other assets	3.8%

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Fund Policies

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Investment Strategy Statement

1. Introduction

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.

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**

Responsibility and governance for the Pension Fund, including investment strategy, fund administration, liability management corporate governance is delegated to the Surrey Pension Fund Committee, 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 Committee is advised by a representative of the Fund's professional investment advisor, an independent advisor, the Director of Finance and the Strategic Finance Manager (Pension Fund and Treasury). The Pension Fund Committee meets on a quarterly basis.

Assisting, monitoring and scrutiny are delegated to the Local Pension Board, which is made up of:

- four employer representatives;
- four employee representatives;
- two independent representatives.

The Local Pension Board is advised by the Director of Finance and the Senior Specialist Advisor.

The Local Pension Board meets on a half yearly basis.

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 requires administering authorities to formulate and to publish a statement of its investment strategy, in accordance with guidance issued from time to time by the Secretary of State.

The Investment Strategy Statement will be an important governance tool for the Fund, as well providing transparency in relation to how the Fund's investments are managed. It will be kept under review and revised from time to time in order to reflect any changes in policy.

The Committee complies with the requirements of the Myners Review of Institutional Investment, which can be found in Appendix A, alongside a review of the Fund's compliance with the principles.

The Fund's key investment beliefs are set out below:

(i) Investment Governance

The Fund has access to the necessary skills, expertise and resources to manage the whole Fund, as well as internally managing a small proportion of the Fund's assets, such as private equity and cash.

Investment consultants, independent advisors and Officers are a source of expertise and research to inform and assist Committee decisions.

The Fund should continuously monitor and improve its governance structure where relevant, through bespoke training in order to implement tactical views more promptly, but acknowledges that achieving optimum market timing is very difficult.

There can be a first mover advantage in asset allocation and category selection (where considered appropriate), but it is difficult to identify and exploit such opportunities, and may require the Fund to be willing to take-on unconventional risk, thus requiring Committee members to have a full understanding of the risk.

(ii) Long Term Approach

The strength of the respective employers' covenant and the present cash flow positive nature of the Fund allow a long-term deficit recovery period and enable the Fund to take a long-term view of investment strategy.

The most important aspect of risk is not the volatility of returns, but the risk of absolute loss, and of not meeting the objective of facilitating low, stable contribution rates for employers.

Illiquidity and volatility are risks which offer potential sources of additional compensation to the long term investor. Moreover, it is important to avoid being a forced seller in short term market setbacks.

Participation in economic growth is a major source of long term equity return.

Over the long term, equities are expected to outperform other liquid assets, particularly government bonds and cash.

Well governed companies that manage their business in a responsible manner will likely produce higher returns over the long term.

(iii) Appropriate Investments

Allocations to asset classes other than equities and government bonds (e.g., Corporate Bonds, Private Equity, Diversified Growth Funds and Property) offer the Fund other forms of risk premia.

Diversification across asset classes and manager strategies that have relatively low correlations with each other will tend to reduce the volatility of the overall Fund return.

In general, allocations to bonds are made to achieve additional diversification. When the Fund approaches full funding level, it may also use bond based strategies to mitigate liability risks and thus dampen the volatility of the Fund's actuarial funding level.

(iv) Management Strategies

A well-balanced portfolio has an appropriate mix of passive and active investments.

Passive, index-tracker style management provides low cost exposure to equities and bonds, and is especially attractive in efficient markets.

Active managers can add value over the long term, particularly in less efficient markets, and the Fund believes that, by following a rigorous approach, it is possible to identify managers who are likely to add value, over the long term.

The long term case for value investing is compelling, but it may result in prolonged periods of over and underperformance in comparison to a style neutral approach.

Active management can be expensive but can provide additional performance. Fees should be aligned to the interests of the Fund rather than performance of the market.

Active management performance should be monitored over multi-year rolling cycles and assessed to confirm that the original investment process on appointment is being delivered and that continued appointment is appropriate.

Employing a range of management styles can reduce the volatility of overall Fund returns but can also reduce long term outperformance.

The Committee seeks to ensure that the Fund has sufficient assets to be able to meet 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 Committee 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 robust 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 Committee believes have the potential to consistently achieve the performance objectives set over the long term and to give each appointed manager a clearly defined benchmark and performance objective against which they can be judged.

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 Committee 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 combined portfolio benchmark over rolling three-year periods.

This statement will be reviewed by the Committee at least tri-annually, or more frequently should any significant change occur.

2. Investment strategy and the process for ensuring suitability of investment

The Fund's benchmark investment strategy, along with an overview of the role each asset is expected to perform is set out in the following table:

Asset class	Allocation %	Advisory ranges %	Role(s) within the strategy
Listed Equities	**59.8**	**56.8 – 62.8**	Generate returns in excess of inflation, through exposure to the shares of domestic and overseas companies.
UK	27.5		
Global Developed Markets Equity	28.5		
Emerging Markets	3.8		
Private Equity	**5.0**	**2.0-8.0**	Generate returns in excess of inflation, through exposure to companies that are not publicly traded, whilst providing some diversification away from listed equities and bonds.
Property	**6.2**	**3.2 - 9.2**	Generate returns in excess of inflation through exposure to UK and overseas property markets through income and capital appreciation, whilst providing some diversification away from equities and bonds.

Diversified Growth	**11.4**	**8.4 – 14.4**	Deliver returns in excess of inflation, with a reasonably low correlation to traditional equity markets and providing a degree of downside protection in periods of equity market stress.
Growth Fixed Income Assets	**12.1**	**9.1-15.1**	
Investment Grade Credit	5.3		Expected to provide a relatively low risk income stream and returns in excess of government bonds by investing in bonds issued by high quality companies.
Total Return	2.4		Offer diversified, unconstrained exposure to global fixed income markets.
Multi Asset Credit	4.4		Offer diversified exposure to global credit markets to capture both income and capital appreciation of underlying bonds.
Inflation Linked Gilts	**5.5**	**2.5-8.5**	
Index Linked Gilts	5.5		Low risk income stream with an explicit linkage to inflation.
Total	**100.0**		

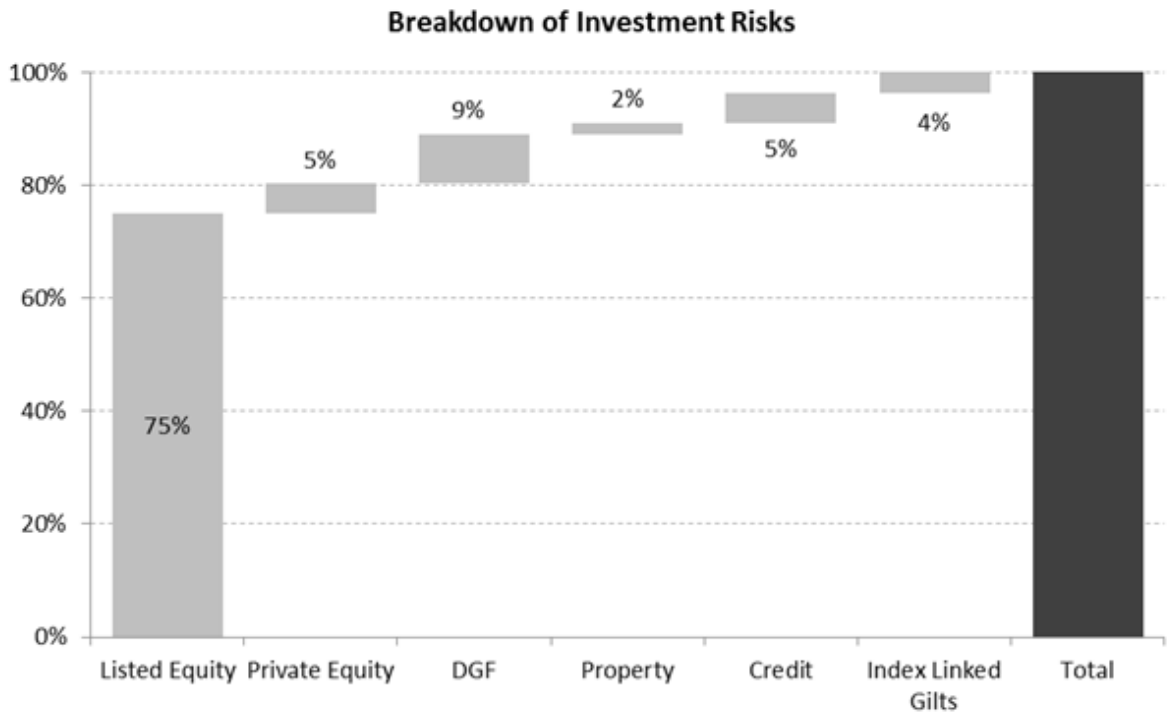
Note: Full details of the asset allocation, including the investment managers and their respective performance benchmarks are included in Appendix B.

3. Risk measurement and management

There are a number of risks to which any investment is exposed. The Committee 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 acceptable overall level of investment risk, the Committee seeks to spread risks across a range of different sources, believing that diversification limits the impact of any single risk. The Committee aims to take on those risks for which a reward, in the form of excess returns, is expected over time.

The graph below provides an indication of the main sources of investment risk (estimated by Mercer) to the Fund's volatility of returns.



Note: Credit risk encompasses the risks within Investment Grade Credit, Total Return Fixed Income and Multi Asset Credit. The chart excludes the risk associated with the change in value of the Fund's liabilities.

The following risks are recognised and considered by the Committee:

Valuation risk: the Actuarial valuation assumes that the Fund generates an expected return equal to or in excess of the Fund's discount rate. An important risk to which the Fund is exposed is that the return is not achieved, either due to unexpected increases in CPI, or if the assets do not deliver as expected.

Longevity risk: this is the risk that the members of the Fund live longer than expected under the Actuarial Valuation assumptions. This risk is captured within the Actuarial Valuation report which is conducted at least triennially and monitored by the Committee, but any increase in longevity will only be realised over the long term.

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

Diversification risk: the Committee 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 Committee aims to ensure that the asset allocation policy results in an adequately diversified portfolio.

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Concentration risk: the Committee takes into consideration 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 Committee recognises that there is liquidity risk in holding assets that are not readily marketable and realisable. Given the long term investment horizon, the Committee 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 Committee 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 hedge in place: 50% of its exposure to the US dollar, Euro and Yen within the liquid equity allocation. For other asset classes, currency hedging is reviewed on a case-by-case basis.

Cashflow risk: the Fund is cashflow positive, in that contributions are expected to exceed outgoings (outgoings are largely expected to be in the form of meeting benefit payments). Excess cashflows are used to rebalance the investment policy closer into line with the target. Over time, it is expected that the size of pensioner cashflows will increase as the Fund matures and greater consideration will need to be given to raising capital to meet outgoings. The Committee recognises that this can present additional risks, particularly if there is a requirement to sell assets at inopportune times.

Governance: members of the Committee and Local Pension Board participate in regular training delivered through a formal programme. Both the Committee and Local Pension Board are aware that poor governance and in particular high turnover of members may prove detrimental to the investment strategy, fund administration, liability management and corporate governance and seeks to minimise turnover where possible.

Environmental, Social and Governance: the Committee wishes to have an active influence on issues of environmental, social or governance (ESG) concern with companies in which the 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 Committee 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.

The full ESG policy of the Fund is outlined in Section 5.

4. Approach to asset pooling

In order to satisfy the requirements of the LGPS (Management and Investment of Funds) Regulations 2016, the Surrey Pension Fund has elected to become a shareholder in Border to Coast Pensions Partnership (BCPP) Limited. BCPP Limited will be a Financial Conduct Authority (FCA) regulated Operator and an Alternative Investment Fund Manager ("AIFM"). The BCPP submission received approval from Government on 12 December 2016.

Asset values total £35.9 billion, supporting 906,000 scheme members and 2,166 employers (data at 31 March 2015).

BCPP is a partnership of the following administering authorities:

- Bedfordshire Pension Fund
- Cumbria Pension Fund
- Durham Pension Fund
- East Riding Pension Fund
- Lincolnshire Pension Fund
- North Yorkshire Pension Fund
- Northumberland Pension Fund
- South Yorkshire Pension Fund
- South Yorkshire Passenger Transport Pension Fund
- Surrey Pension Fund
- Teesside Pension Fund
- Tyne and Wear Pension Fund

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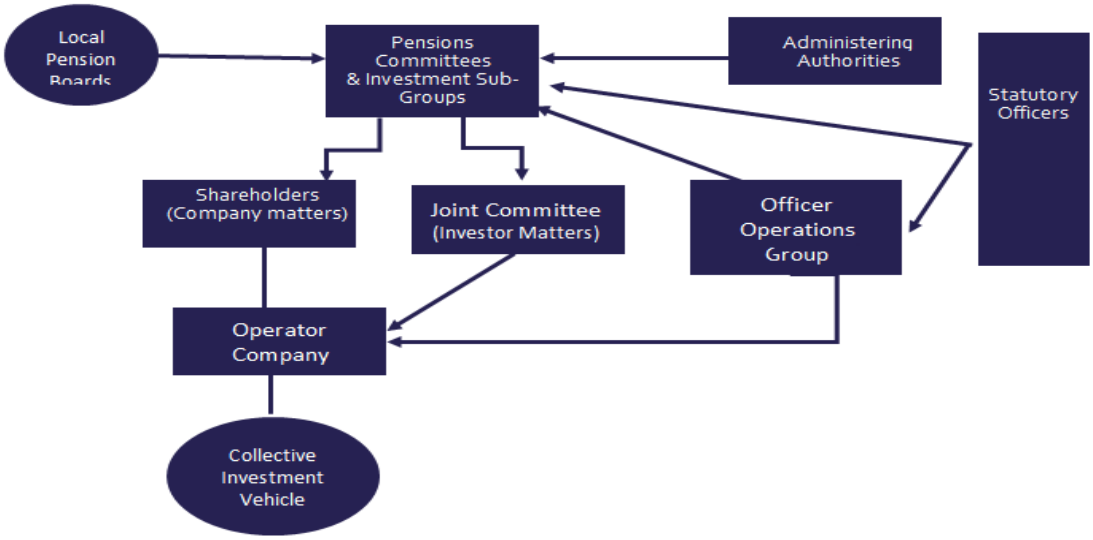
- Warwickshire Pension Fund

The basis of the pooling will be in line with guidance issued by the Secretary of State and meeting the four criteria set out below:

a. Benefits of scale - a minimum asset size per pool of £25bn.
b. Strong governance and decision making
c. Reduced costs and value for money
d. Improved capacity to invest in infrastructure

The proposed governance structure of BCPP is as follows:



The Fund will hold BCPP to account through the following mechanisms:

- A representative on the BCPP Shareholder Board, with equal voting rights, who will provide oversight and control of the corporate operations of BCPP Limited. Each Fund has an equal share in the company.

- A representative on the BCPP Joint Committee who will monitor and oversee the investment operations of BCPP Limited.

- Officer support to the above representatives from the Officer Operations Group and the Statutory Officer Group.

The regulatory changes do not affect the sovereignty of the Surrey Pension Fund which will retain the decision making powers regarding asset allocation and will delegate the investment management function to BCPP Limited. The pooling of LGPS assets will have no impact on the

pension entitlement of members of the fund (pensioners, current employees, and deferred members who are yet to draw their pension).

BCPP has been created by like-minded funds, established around key principals:

- one fund one vote, regardless of size, all Funds will be treated equally;
- equitable sharing of costs;
- to drive efficiencies and work effectively, partner funds must have a complementary investment ethos, risk appetite and investment strategy.

BCPP will have an internal team of investment managers, in addition to appointing external managers. Its role will be to implement the investment strategies of the partner funds, through a range of investment sub-funds, offering internally and externally managed solutions. It is anticipated that a significant proportion of the Fund's investments will be made through BCPP Limited. Where it is not practical or cost effective for assets to be transferred into the pool (existing private equity investments), they will continue to be managed at the Fund level. Whilst these assets are unlikely to be transferred, it is expected that once these investments are fully distributed, the proceeds will be reinvested into BCPP.

5. Environmental, social and corporate governance (ESG) policy

The Fund has no specific policy on investing or divesting investments wholly with regard to ESG issues. However external fund managers are expected to take into account ESG issues when assessing potential investment opportunities. It is the belief of the Fund that well governed companies that manage their business in a responsible manner will produce superior returns over the long term, and the Fund expects these considerations to form part of the investment selection criteria for external fund managers in carry out stock selection.

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

The Fund aims to to be an active shareholder in the exercising of its company share voting rights to promote and support good corporate governance principles. Share voting is undertaken in-house, after consultation with fund managers and a specialist corporate governance advisor. 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.
Responsibility for investment decisions is delegated by the Administering Authority to the Pension Fund Committee. The structure of the Committee, as set out in the opening section of this ISS, includes specific representative members for both employers within the Fund and the scheme membership.

6. Policy of the exercise of rights (including voting rights) attaching to investments

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Stewardship Code Statement

Principle 1: Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.

The Fund takes its responsibilities as a shareholder seriously and has made a commitment to the informed exercise of its ownership rights.

Principle 2: Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.

The Fund expects its fund managers to have effective policies addressing potential conflicts of interest. In respect of conflicts of interest within the Fund, Committee members are required to make declarations of interest prior to panel meetings.

Principle 3: Institutional investors should monitor their investee companies.

Day-to-day responsibility for managing the Fund's equity holdings is delegated to our appointed fund managers and the fund expects them to monitor companies, intervene where necessary, and report back regularly on activity undertaken.

The Fund actively votes all its equity holdings directly and liaises with the fund managers as necessary.

Principle 4: Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.

Responsibility for day-to-day interaction with companies is delegated to the Fund's investment managers, including the escalation of engagement when necessary. On occasion, the Fund may itself choose to escalate activity; this will typically be through our membership of the LAPFF. When this occurs, the Committee will typically take a minuted vote on the decision whether to participate in the proposed activity.

Principle 5: Institutional investors should be willing to act collectively with other investors where appropriate.

The Fund seeks to work collaboratively with other institutional shareholders in order to maximise the influence that it can have on individual companies. This is achieved through our LAPFF membership, together with initiatives proposed by our investment managers or other advisors.

Principle 6: Institutional investors should have a clear policy on voting and disclosure of voting activity.

The Fund aims to exercise all votes associated with its equity holdings and operates a custom policy which reflects the Fund's investment objectives. Fund officers are responsible for voting decisions and are supported by specialist proxy research.

On a general basis, the Fund will support resolutions which are consistent with the UK Governance Code and represent best practice. In overseas markets, we will take account of local best practice

principles. Where resolutions or issues fall short of the expected standards, we will either abstain or vote against, depending on the individual circumstances of the company and the issues presented.

The policy is reviewed at least annually in order to take account of regulatory developments. Controversial issues may be discussed at Committee meetings.

Principle 7: Institutional investors should report periodically on their stewardship and voting activities.

The Fund reports on its stewardship activity to the Committee and employer member representatives at the Annual Meeting where members have an opportunity to ask specific questions.

In addition, quarterly reports of voting actions are posted on the Fund's website (**www.surreypensionfund.org**)

The Committee will provide an annual report on how the Fund satisfies its UK Stewardship Code obligations requirements.

Advice Taken

In constructing this statement, the Committee has taken advice from a representative of the Fund's professional investment advisor (Mercer Limited), an independent advisor, the Director of Finance and the Strategic Finance Manager (Pension Fund and Treasury).

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Appendix A: 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.

✓ **Full compliance**

The Committee and Local Pension Board are supported in their decision making/assisting roles by the Director of Finance and the Pension Fund and Treasury Manager.

Members of the both Boards 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 the Committee on a quarterly basis. Fund managers present to the officers or the Committee 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 Committee, although options other than measuring meeting attendance and the success of the Committee'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**

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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 Committee and half yearly reports to the Local Pension 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.

Appendix B: Investment Manager Performance Targets and Benchmarks

Manager	Portfolio	Allocation (%)	Benchmark Index	Performance Target
UBS	UK Equities	7.6	FTSE All Share	+2.0% p.a. (gross of fees) over rolling 3-year periods
Majedie	UK Equities – Long Only UK Equities – Directional Long/Short	10.4	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
Marathon	Global Equities	11.4	MSCI AC World	+2.0% p.a. (gross of fees) over rolling 3-year periods
Newton	Global Equities	7.6	MSCI AC World	+2.0% p.a. (gross of fees) over rolling 3-year periods
Various*	Private Equity	5.0	MSCI World Index	+5% p.a. (net of fees) over the life of the contract
CBRE	Property	6.2	IPD UK All Balanced Funds	+0.5% p.a. (gross of fees) over rolling 3-year periods
Baillie Gifford	Diversified Growth	3.8	UK Base Rate	+3.5% p.a. (net of fees) over rolling 3-year periods
Ruffer	Diversified Growth	3.8	-	First objective is not to lose money o a rolling 12 month basis. Second objective is to outperform cash and inflation on a consistent basis.
Aviva	Diversified Growth	3.8	UK Base Rate	+5.0% p.a. (gross of fees) over rolling 3-year periods
Western	Investment Grade Credit Multi Asset Credit	5.3 4.4	Merrill Lynch Sterling Non-Gilts Index Total return benchmark	+0.75% p.a. (gross of fees) over rolling 3-year periods +5% to 7% per annum over the market cycle
Franklin Templeton	Unconstrained Global Fixed Income	2.4	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	28.3	FTSE All Share FTSE AW – Dev'd World (ex UK) FTSW AW – All Emerging Markit iBoxx GBP Non Gilts ex BBB	To track the performance of the respective indices within a lowe level of tracking deviation (gross of fees) over rolling 3-year periods

	(ex UK) Dev Equity Index HN – World Emerging Markets Equity Index CN - AAA- AA-A Bonds – All Stocks Index Index-Linked Gilts		All stock Portfolio of single stock funds structured by reference to Fund liabilities	
Internal	Cash		LIBID 7-day rate	LIBID 7 day rate

*See Appendix C

Appendix C: Private Equity

The table below outlines details on the Fund's private equity commitments. 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 Committee 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.

Name	Currency	Inception	Commitment
UK Funds			**£/€/$m**
HG 5	£	2006	7.9
HG 6	£	2009	10.0
HG 7	£	2013	15.0

Capital Dynamics LGPS Collective 2016/2017	£	2016	8.0
Capital Dynamics LGPS Collective 2017/2018	£	2017	8.0
LIVING BRIDGE 4 LP	£	2013	2.1
LIVINGBRIDGE ENTERPRISE 1 LP	£	2013	10.0
Darwin Property Fund	£	2013	60.0
Euro Funds			
Standard Life ESP 2006	€	2006	15.0
Standard Life ESP 2008	€	2008	15.0
Standard Life ESP II	€	2004	10.0
Standard Life ESF I	€	2011	17.5
Dollar Funds			
Blackrock Vesey Street I	$	2001	5.0
Blackrock Vesey Street II	$	2003	5.0
Blackrock Vesey Street Ill	$	2005	17.5
GS PEP 2000 LP	$	2000	9.5
GS PEP 2004 LP	$	2004	10.0
GS PEP 2005 LP	$	2006	17.0
GS PEP X LP	$	2008	18.0
GS PEP XI LP	$	2011	40.0
GS Vintage VI	$	2013	20.0
GS Vintage VII	$	2016	50.0
GS WS EUROPEAN INFRASTRUCTURE LP	$	2017	20.0
Pantheon Global Infrastructure	$	2017	60.0
Capital Dynamics Clean Energy	$	2012	24.9
Standard Life SOF I Feeder	$	2014	20.0
Standard Life SOF II Feeder	$	2014	20.0
Standard Life SOF III Feeder	$	2017	45.0

1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the Surrey Pension Fund ("the Fund"), which is administered by Surrey County Council, ("the Administering Authority").

It has been prepared by the Administering Authority in collaboration with the Fund's actuary, Hymans Robertson LLP, and after consultation with the Fund's employers and investment adviser. It is effective from 1 April 2017.

1.2 What is the Surrey Pension Fund?

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

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

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

1.3 Why does the Fund need a Funding Strategy Statement?

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

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

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

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

There are also regulatory requirements for an FSS, as given in Appendix A.

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

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

1.4 How does the Fund and this FSS affect me?

This depends on who you are:

- to achieve and then maintain a funding target that requires assets equal to 100% of the present value of benefits based on completed service including provision for the effects of future salary growth and inflation up to retirement;
- a member of the Fund, i.e. a current or former employee, or a dependant: the Fund needs to be sure it is collecting and holding enough money so that your benefits are always paid in full;
- an employer in the Fund (or which is considering joining the Fund): you will want to know how your contributions are calculated from time to time, that these are fair by comparison to other employers in the Fund, and in what circumstances you might need to pay more. Note that the FSS applies to all employers participating in the Fund;
- an Elected Member whose council participates in the Fund: you will want to be sure that the council balances the need to hold prudent reserves for members' retirement and death benefits, with the other competing demands for council money;
- a Council Tax payer: your council seeks to strike the balance above, and also to minimise cross-subsidies between different generations of taxpayers.

1.5 What does the FSS aim to do?

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

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- 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, but, are set at an appropriate level to ensure the solvency of the pension fund and the long term cost-efficiency of the scheme, so far as relating to the pension fund;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (**NB** this will also minimise the costs to be borne by Council Tax payers);
- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

1.6 How do I find my way around this document?

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

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

In Section 4 we show how the funding strategy is linked with the Fund's investment strategy.

In the Appendices we cover various issues in more detail if you are interested:

A. the regulatory background, including how and when the FSS is reviewed,

B. who is responsible for what,

C. what issues the Fund needs to monitor, and how it manages its risks,

D. some more details about the actuarial calculations required,

E. the assumptions which the Fund actuary currently makes about the future,

F. a glossary explaining the technical terms occasionally used here.

If you have any other queries please contact John Smith (Senior Specialist Advisor) in the first instance at john.smith@surreycc.gov.uk or on telephone number 020 8213 2700.

2 Basic Funding issues

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

2.1 How does the actuary measure the required contribution rate?

In essence this is a three-step process:

- Calculate the funding target for that employer, i.e. the estimated amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix E for more details of what assumptions we make to determine that funding target;
- Determine the time horizon over which the employer should aim to achieve that funding target. See the table in 3.3 and Note (c) for more details;
- Calculate the employer contribution rate such that it has at least a given probability of achieving that funding target over that time horizon, allowing for different likelihoods of various possible economic outcomes over that time horizon. See 2.3 below, and the table in 3.3 Note (e) for more details.

2.2 What is each employer's contribution rate?

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

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

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

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

2.3 What different types of employer participate in the Fund?

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

In essence, participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst the majority of members will be local authority employees (and ex-employees), the majority of participating employers are those providing services in place of (or alongside) local authority services: academy schools, contractors, housing associations, charities, etc.

The LGPS Regulations define various types of employer as follows:

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

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

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

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

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

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

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

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

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

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

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

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

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2.5 How is a deficit (or surplus) calculated?

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

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

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

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

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

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

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

- Higher Pension Fund contributions may result in reduced council spending, which in turn could affect the resources available for council services, and/or greater pressure on council tax levels;
- Contributions which Academies pay to the Fund will therefore not be available to pay for providing education; and
- Other employers will provide various services to the local community, perhaps through housing associations, charitable work, or contracting council services. If they are required to pay more in pension contributions to the LGPS then this may affect their ability to provide the local services at a reasonable cost.

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

- The Fund provides invaluable financial security to local families, whether to those who formerly worked in the service of the local community who have now retired, or to their families after their death;
- The Fund must have the assets available to meet these retirement and death benefits, which in turn means that the various employers must each pay their own way. Lower contributions today will mean higher contributions tomorrow: deferring payments

does not alter the employer's ultimate obligation to the Fund in respect of its current and former employees;

- Each employer will generally only pay for its own employees and ex-employees (and their dependants), not for those of other employers in the Fund;
- The Fund strives to maintain reasonably stable employer contribution rates where appropriate and possible. However, a recent shift in regulatory focus means that solvency within each generation is considered by the Government to be a higher priority than stability of contribution rates;
- The Fund wishes to avoid the situation where an employer falls so far behind in managing its funding shortfall that its deficit becomes unmanageable in practice: such a situation may lead to employer insolvency and the resulting deficit falling on the other Fund employers. In that situation, those employers' services would in turn suffer as a result;
- Council contributions to the Fund should be at a suitable level, to protect the interests of different generations of council tax payers. For instance, underpayment of contributions for some years will need to be balanced by overpayment in other years; the council will wish to minimise the extent to which council tax payers in one period are in effect benefitting at the expense of those paying in a different period.

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

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

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

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

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

3 Calculating contributions for individual Employers

3.1 General comments

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

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

These and associated issues are covered in this Section.

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

3.2 The effect of paying lower contributions

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

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

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

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

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

3.3 The different approaches used for different employers

Type of employer	Scheduled Bodies			Community Admission Bodies and Designating Employers		Transferee Admission Bodies
Sub-type	**Local Authorities, Police and Town/Parish Councils**	**Colleges**	**Academies**	**Open to new entrants**	**Closed to new entrants**	**(all)**
Funding Target Basis used	Ongoing, assumes long-term Fund participation (see Appendix E)			Ongoing, but may move to "gilts basis" - see Note (a)		Ongoing, assumes fixed contract term in the Fund (see Appendix E)
Primary rate approach	(see Appendix D – D.2)					
Stabilised contribution rate?	Yes - see Note (b)	No	No	No	No	No
Maximum time horizon – Note (c)	20 years	17 years	20 years	Future working lifetime	Future working lifetime	Outstanding contract term
Secondary rate – Note (d)	Monetary amount	Monetary amount	% of payroll	Monetary amount/% of payroll	Monetary amount/% of payroll	Monetary amount/% of payroll
Treatment of surplus	Covered by stabilisation arrangement	Preferred approach: contributions kept at Primary rate. However, reductions may be permitted by the Administering Authority				Preferred approach: contributions kept at future service rate. However, contractors may be permitted to reduce contributions by spreading the surplus over the remaining contract term
Probability of achieving target – Note (e)	66%	80%	70% if part of a MAT/75% if standalone	70% if guaranteed by LA	70% if guaranteed by LA 75% if form of security offered	70% if guaranteed by LA 75% if other form of security offered or has other guarantor (not LA) 80% otherwise

		75% if form of security offered		75% if form of security offered 80% otherwise	80% otherwise	
Phasing of contribution changes	Covered by stabilisation arrangement	At the discretion of the Administering Authority		None	None	None
Review of rates – Note (f)	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations					To be reviewed in last 3 years of contract
New employer	n/a	n/a	Note (g)	Note (h)		Notes (h) & (i)
Cessation of participation: cessation debt payable	Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation debt principles applied would be as per Note (j).			Can be ceased subject to terms of admission agreement. Cessation debt will be calculated on a basis appropriate to the circumstances of cessation – see Note (j).		Participation is assumed to expire at the end of the contract. Cessation debt (if any) calculated on ongoing basis. Awarding Authority will be liable for future deficits and contributions arising.

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

In the circumstances where:

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

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

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

Note (b) (Stabilisation)

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

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

The current stabilisation mechanism applies to Surrey County Council, all District and Borough Councils and Surrey Police Authority:

- This is subject to there being no material events which cause the employer to become ineligible, e.g. significant reductions in active membership (due to outsourcing or redundancies), or changes in the nature of the employer (perhaps due to Government restructuring), or changes in the security of the employer.

On the basis of extensive modelling carried out for the 2016 valuation exercise (see Section 4), the stabilised details are as follows:

- Total contributions have been set to ensure that stabilised employers have at least a 66% chance of being fully funded in 20 years under the 2016 formal valuation assumptions.
- The stabilisation criteria and limits will be reviewed at the 31 March 2019 valuation, to take effect from 1 April 2020. However the Administering Authority reserves the right to review the stabilisation criteria and limits at any time before then, on the basis of membership and/or employer changes as described above.

Note (c) (Maximum time horizon)

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2017 for the 2016 valuation). The Administering Authority may adopt a rolling time horizon or a reducing time horizon at successive triennial valuations depending on specific employer circumstances. The Administering Authority reserve the right to propose alternative time horizons, for example where there are no new entrants.

Note (d) (Secondary rate)

For employers where stabilisation is not being applied, the Secondary contribution rate for each employer covering the three year period until the next valuation will generally be set as monetary amounts, with the exception of Academy rates. However, the Administering Authority reserves the right to amend this approach on a case by case basis where appropriate.

Note (e) (Probability of achieving funding target)

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

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

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

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

Note (f) (Regular Reviews)

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

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

Note (g) (New Academy conversions)

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

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

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

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

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

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

The Fund's policies on academies are subject to change in the light of any amendments to DCLG guidance. Any changes will be notified to academies, and will be reflected in a subsequent version of this FSS. In particular, policies (iv) and (v) above will be reconsidered at each valuation.

Note (h) (New Admission Bodies)

With effect from 1 October 2012, the LGPS 2012 Miscellaneous Regulations introduced mandatory new requirements for all Admission Bodies brought into the Fund from that

date. Under these Regulations, all new Admission Bodies will be required to provide some form of security, such as a guarantee from the letting employer, an indemnity or a bond. The security is required to cover some or all of the following:

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

Transferee Admission Bodies: For all TABs, the security must be to the satisfaction of the Administering Authority as well as the letting employer, and will be reassessed on an annual basis. See also Note (i) below.
Community Admission Bodies: The Administering Authority will only consider requests from CABs (or other similar bodies, such as section 75 NHS partnerships) to join the Fund if they are sponsored by a Scheduled Body with tax raising powers, guaranteeing their liabilities and also providing a form of security as above.

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

Note (i) (New Transferee Admission Bodies)

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

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

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

i) Pooling

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

ii) Letting employer retains pre-contract risks

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

iii) Fixed contribution rate agreed

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

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

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

  redundancy and early retirement decisions.

Note (j) (Admission Bodies Ceasing)

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

- Last active member ceasing participation in the Fund (NB recent LGPS Regulation changes mean that the Administering Authority has the discretion to defer taking action for up to three years, so that if the employer acquires one or more active Fund members during that period then cessation is not triggered. The default position will be for a cessation to be triggered, but the Fund has the discretion on whether to be apply this in any given case.
- The insolvency, winding up or liquidation of the Admission Body;
- Any breach by the Admission Body of any of its obligations under the Agreement that they have failed to remedy to the satisfaction of the Fund;

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- A failure by the Admission Body to pay any sums due to the Fund within the period required by the Fund; or
- The failure by the Admission Body to renew or adjust the level of the bond or indemnity, or to confirm an appropriate alternative guarantor, as required by the Fund.

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

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

(a) Where a guarantor does not exist then, in order to protect other employers in the Fund, the cessation liabilities and final deficit will normally be calculated using a "gilts cessation basis", which is more prudent than the ongoing basis. This has no allowance for potential future investment outperformance above gilt yields, and has added allowance for future improvements in life expectancy. This could give rise to significant cessation debts being required.

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

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

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

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

As an alternative, where the ceasing Admission Body is continuing in business, the Fund at its absolute discretion reserves the right to enter into an agreement with the ceasing

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

3.4 Pooled contributions

The Administering Authority can give consideration to setting up pools for employers with very similar characteristics. This will always be in line with its broader funding strategy. With the advice of the Actuary, the Administering Authority may allow smaller employers of similar types to pool their contributions in order to smooth out the effects of costly events, e.g., ill-health retirements or deaths in service.

Community Admission Bodies that are deemed by the Administering Authority to have closed to new entrants are not usually permitted to participate in a pool. Transferee Admission Bodies are usually also ineligible for pooling. Smaller admitted bodies may be pooled with the letting employer, provided all parties (particularly the letting employer) agree.

Academies who belong to a MAT are permitted to pool for contribution rate purposes from the 2016 valuation onwards.

Employers who are permitted to enter (or remain in) a pool at the 2016 valuation will not normally be advised of their individual contribution rate unless agreed by the Administering Authority. Schools generally are also pooled with their funding Council. However there may be exceptions for specialist or independent schools. Those employers which have been pooled are identified in the Rates and Adjustments Certificate.

3.5 Additional flexibility in return for added security

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

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

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

The degree of flexibility given may take into account factors such as:

- the extent of the employer's deficit;
- the amount and quality of the security offered;
- the employer's financial security and business plan; and

- whether the admission agreement is likely to be open or closed to new entrants.

3.6 Non ill health early retirement costs

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

3.7 Ill health early retirement costs

In the event of a member's early retirement on the grounds of ill-health, a funding strain will usually arise, which can be very large.

Admitted Bodies will usually have an 'ill health allowance'; Scheduled Bodies may have this also, depending on their agreement terms with the Administering Authority. The Fund monitors each employer's ill health experience on an ongoing basis. If the cumulative cost of ill health retirement in any financial year exceeds the allowance at the previous valuation, the cost will be recovered from the Fund's internal ill health insurance as outlined below.

3.8 Internal Ill health insurance

The Fund self-insures against ill health events which applies to all employers in the Fund such that:

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

3.9 Employers with no remaining active members

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

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

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

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

3.10 Policies on bulk transfers

Each bulk transfer case will be treated on its own merits, but in general:

- The Fund will not pay bulk transfers greater than the lesser of (a) the asset share of the transferring employer in the Fund, and (b) the value of the past service liabilities of the transferring members;
- The Fund will not grant added benefits to members bringing in entitlements from another Fund unless the asset transfer is sufficient to meet the added liabilities; and
- The Fund may permit shortfalls to arise on bulk transfers if the Fund employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's Fund contributions to increase between valuations.

Funding strategy and links to investment strategy

3.11 What is the Fund's investment strategy?

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

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

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

The same investment strategy is currently followed for all employers.

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

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

Therefore, the funding and investment strategies are inextricably linked.

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

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

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

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

3.14 How does this differ for a large stable employer?

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

- Prudence - the Fund should have a reasonable expectation of being fully funded in the long term;
- Affordability – how much can employers afford;
- Stewardship – the assumptions used should be sustainable in the long term, without having to resort to overly optimistic assumptions about the future to maintain an apparently healthy funding position; and
- Stability – employers should not see significant moves in their contribution rates from one year to the next, to help provide a more stable budgeting environment.

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

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

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

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

3.15 Does the Fund monitor its overall funding position?

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

Statutory reporting and comparison to other LGPS Funds

3.16 Purpose

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

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

3.17 Solvency

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

(a) the rate of employer contributions is set to target a funding level for the Fund of 100%, over an appropriate time period and using appropriate actuarial assumptions (where appropriateness is considered in both absolute and relative terms in comparison with other funds); and either

(b) employers collectively have the financial capacity to increase employer contributions, and/or the Fund is able to realise contingent assets should future circumstances require, in order to continue to target a funding level of 100%; or

(c) there is an appropriate plan in place should there be, or if there is expected in future to be, a material reduction in the capacity of fund employers to increase contributions as might be needed.

3.18 Long Term Cost Efficiency

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

i. the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual,

ii. with an appropriate adjustment to that rate for any surplus or deficit in the Fund.

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

Relative considerations include:

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

Absolute considerations include:

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

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

Appendix A – Regulatory framework

A1 Why does the Fund need an FSS?

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

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

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

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

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

A2 Does the Administering Authority consult anyone on the FSS?

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

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

a) A draft version of the FSS was issued to all participating employers on 1 February 2017 for comment;

b) Comments will be requested within 30 days;

c) Following the end of the consultation period the FSS will be updated where required and then published before 1 April 2017.

A3 How is the FSS published?

The FSS is made available through the following routes:

- Published on the website
- A copy sent by email to each participating employer in the Fund;
- A copy to the Pension Fund Committee and Local Pensions Board
- A full copy annual report and accounts of the Fund;

- Copies sent to independent advisers;
- Copies made available on request.

A4 How often is the FSS reviewed?

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

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

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

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

A5 How does the FSS fit into other Fund documents?

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues, for example there are a number of separate statements published by the Fund including the Statement of Investment Principles/Investment Strategy Statement, Governance Strategy and Communications Strategy. In addition, the Fund publishes an Annual Report and Accounts with up to date information on the Fund.

These documents can be found on the web at http://www.surreypensionfund.org

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Appendix B – Responsibilities of key parties

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

B1 The Administering Authority should:-

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

B2 The Individual Employer should:-

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

B3 The Fund Actuary should:-

- prepare valuations, including the setting of employers' contribution rates. This will involve agreeing assumptions with the Administering Authority, having regard to the FSS and LGPS Regulations, and targeting each employer's solvency appropriately;
- provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
- provide advice relating to new employers in the Fund, including the level and type of bonds or other forms of security (and the monitoring of these);
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters;
- assist the Administering Authority in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;
- advise on the termination of employers' participation in the Fund; and
- fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

B4 Other parties:-

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

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Appendix C – Key risks and controls

C1 Types of risk

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

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

C2 Financial risks

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning the valuation of liabilities over the long-term.	Only anticipate long-term returns on a relatively prudent basis to reduce risk of under-performing. Assets invested on the basis of specialist advice, in a suitably diversified manner across asset classes, geographies, managers, etc. Analyse progress at three yearly valuations for all employers. Inter-valuation roll-forward of liabilities between valuations at whole Fund level.
Inappropriate long-term investment strategy.	Overall investment strategy options considered as an integral part of the funding strategy. Used asset liability modelling to measure 4 key outcomes. Chosen option considered to provide the best balance.
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	Stabilisation modelling at whole Fund level allows for the probability of this within a longer term context. Inter-valuation monitoring, as above. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.

Risk	Summary of Control Mechanisms
Pay and price inflation significantly more than anticipated.	The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases. Inter-valuation monitoring, as above, gives early warning. Some investment in bonds also helps to mitigate this risk. Employers pay for their own salary awards and should be mindful of the geared effect on pension liabilities of any bias in pensionable pay rises towards longer-serving employees.
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	An explicit stabilisation mechanism has been agreed as part of the funding strategy. Other measures are also in place to limit sudden increases in contributions.
Orphaned employers give rise to added costs for the Fund	The Fund seeks a cessation debt (or security/guarantor) to minimise the risk of this happening in the future. If it occurs, the Actuary calculates the added cost spread pro-rata among all employers – (see 3.9).

C3 Demographic risks

Risk	Summary of Control Mechanisms
Pensioners living longer, thus increasing cost to Fund.	Set mortality assumptions with some allowance for future increases in life expectancy. The Fund Actuary has direct access to the experience of over 50 LGPS funds which allows early identification of changes in life expectancy that might in turn affect the assumptions underpinning the valuation.
Maturing Fund – i.e. proportion of actively contributing employees declines relative to retired employees.	Continue to monitor at each valuation, consider seeking monetary amounts rather than % of pay and consider alternative investment strategies.

Risk	Summary of Control Mechanisms
Deteriorating patterns of early retirements	Employers are charged the extra cost of non ill-health retirements following each individual decision. Employer ill health retirement experience is monitored, and insurance is an option.
Reductions in payroll causing insufficient deficit recovery payments	In many cases this may not be sufficient cause for concern, and will in effect be caught at the next formal valuation. However, there are protections where there is concern, as follows: Employers in the stabilisation mechanism may be brought out of that mechanism to permit appropriate contribution increases (see Note (b) to 3.3). For other employers, review of contributions is permitted in general between valuations (see Note (f) to 3.3) and may require a move in deficit contributions from a percentage of payroll to fixed monetary amounts.

C4 Regulatory risks

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

Changes by Government to particular employer participation in LGPS Funds, leading to impacts on funding and/or investment strategies.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. Take advice from Fund Actuary on impact of changes on the Fund and amend strategy as appropriate.

C5 Governance risks

Risk	Summary of Control Mechanisms
Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements) or not advised of an employer closing to new entrants.	The Administering Authority has a close relationship with employing bodies and communicates required standards e.g. for submission of data. The Actuary may revise the rates and Adjustments certificate to increase an employer's contributions between triennial valuations Deficit contributions may be expressed as monetary amounts.
Actuarial or investment advice is not sought, or is not heeded, or proves to be insufficient in some way	The Administering Authority maintains close contact with its specialist advisers. Advice is delivered via formal meetings involving Elected Members, and recorded appropriately. Actuarial advice is subject to professional requirements such as peer review.
Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.
An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure. The risk is mitigated by: Seeking a funding guarantee from another scheme employer, or external body, where-ever possible (see Notes (h) and (j) to 3.3).

Risk	Summary of Control Mechanisms
	Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice. Vetting prospective employers before admission. Where permitted under the regulations requiring a bond to protect the Fund from various risks. Requiring new Community Admission Bodies to have a guarantor. Reviewing bond or guarantor arrangements at regular intervals (see Note (f) to 3.3). Reviewing contributions well ahead of cessation if thought appropriate (see Note (a) to 3.3).

Appendix D – The calculation of Employer contributions

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

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

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

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

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

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

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

Employer contributions are normally made up of two elements:

a) the estimated cost of ongoing benefits being accrued, referred to as the "Primary contribution rate" (see D2 below); plus

b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "Secondary contribution rate" (see D3 below).

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

D2 How is the Primary contribution rate calculated?

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

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

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

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

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

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

D3 How is the Secondary contribution rate calculated?

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

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

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

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

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

The projections are carried out using an economic modeller developed by the Fund Actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as

asset returns (based on the Fund's investment strategy), inflation, and bond yields. The measured contributions are calculated such that the proportion of outcomes with at least 100% solvency (by the end of the time horizon) is equal to the required probability.

D4 What affects a given employer's valuation results?

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

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

D5 How is each employer's asset share calculated?

Until 31 March 2016 the Administering Authority did not account for each employer's assets separately. Instead, the Fund's actuary apportioned the assets of the whole Fund between the employers, at each triennial valuation.

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

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

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

- member specific salary and pension increases but instead uses weighted averages
- differences in values placed on liabilities due to changes in assumptions at transfer dates and formal valuation dates

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

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

The methodology adopted until 31 March 2016 meant that there were inevitably some difference between the asset shares calculated for individual employers and those that would have resulted had they participated in their own ring-fenced section of the Fund.

The asset apportionment was capable of verification but not to audit standard. The Administering Authority recognised the limitations in the process, and while it considered that the Fund actuary's approach addressed the risks of employer cross-subsidisation to an acceptable degree, it decided to adopt a different apportionment approach going forward.

With effect from 1 April 2016, the Fund uses the Hymans Robertson Employer Asset Tracking model ("HEAT"), which apportions assets at individual employer level allowing for actual monthly Fund returns and monthly cashflows per employer (e.g. contributions received, benefits paid out, investment returns, transfers in and out, etc). This revised approach gives a greater degree of accuracy, for tracking employers' assets.

Appendix E – Actuarial assumptions

E1 What are the actuarial assumptions?

These are expectations of future experience used to place a value on future benefit payments ("the liabilities"). Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits.

Changes in assumptions will affect the measured funding target. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.

The combination of all assumptions is described as the "basis". A more optimistic basis might involve higher assumed investment returns (discount rate), or lower assumed salary growth, pension increases or life expectancy; a more optimistic basis will give lower funding targets and lower employer costs. A more prudent basis will give higher funding targets and higher employer costs.

E2 What basis is used by the Fund?

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

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

E3 What assumptions are made in the ongoing basis?

- **Investment return / discount rate**

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

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

For the purpose of the triennial funding valuation at 31 March 2016 and setting contribution rates effective from 1 April 2017, the Fund actuary has assumed that future investment returns earned by the Fund over the long term will be 2.1% per annum greater than CPI inflation at the time of the valuation. In the opinion of the Fund actuary, based on the current investment strategy of the Fund, this asset out-performance assumption is within a range that would be considered acceptable for the purposes of the funding valuation.

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- **Salary growth**

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

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

This gives a single "blended" assumption of RPI less 0.7%. This is a change from the previous valuation, which assumed a flat assumption of RPI plus 0.5% per annum. The change has led to a reduction in the funding target (all other things being equal).

- **Pension increases**

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

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

- **Life expectancy**

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

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

It is acknowledged that future life expectancy and, in particular, the allowance for future improvements in life expectancy, is uncertain. There is a consensus amongst actuaries, demographers and medical experts that life expectancy is likely to improve in the future. Allowance has been made in the ongoing valuation basis for future improvements in line with the 2013 version of the Continuous Mortality Investigation model published by the Actuarial Profession and a 1.25% per annum minimum underpin to future reductions in mortality rates. This is a similar allowance for future improvements than was made in 2013.

The combined effect of the above changes from the 2013 valuation approach, is to reduce life expectancy by around 0.5 years on average, which reduces the funding target all other

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

- **General**

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

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

12 Governance Compliance Statement

The Local Government Pension Scheme (England and Wales) (Amendment) (No 2) Regulations 2005 came into effect on 14 December 2005. The Regulations provided the statutory framework within which LGPS administering authorities were required to publish a governance policy statement by 1 April 2006. The policy intention was that the statement also described and explained the administering authority's arrangements for the representation and participation of Scheme stakeholders. A copy of the Surrey Pension Fund's current governance policy statement can be found on Surrey CC's website.

The Local Government Pension Scheme (Amendment)/(No 3) Regulations 2007 (SI 2007 No 1561) provided further statutory framework, including the provision that administering authorities produce a statement disclosing the degree to which it complies with best practice in its governance procedures. This statement is reproduced in full below:

GOVERNANCE COMPLIANCE STATUTORY GUIDANCE

Principle	Surrey's Approach	Compliance
STRUCTURE		
The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing council.	Surrey County Council delegates the management of the Surrey Pension Fund to the Pension Fund Committee. The Committee is responsible for these areas under the terms of reference contained in the Council's Constitution.	Comply
That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	Surrey is compliant with these principles. Employers and employee representatives are represented on the Pension Fund Committee. The Committee comprises county councilors, borough/district councilors, an external employer representative and a union representative to represent employees and	Comply

	pensioners. All Committee members have full voting rights.	
That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	There is currently no secondary committee..	n/a
That where a secondary committee or panel has been established, at least one seat on the main committee is allocated for a member from the secondary committee or panel.	There is currently no secondary committee.. Should a secondary committee be established, all members of that secondary committee would sit on the main Pension Fund Committee.	n/a
Principle	**Surrey's Approach**	**Compliance**
REPRESENTATION		
That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include: • employing authorities (including non-scheme	With over 150 employer bodies, not all stakeholders are directly represented on the Pension Fund Committee. All stakeholders are free to make representations in writing to the Committee. The County Council, the eleven districts and	Explain

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employers, e.g., admitted bodies);	boroughs, Office of the Police and Crime Commissioner and employees are directly represented on the Pension Fund Committee.	
• scheme members (including deferred and pensioner scheme members);	The Pension Fund Committee membership includes a trade union representative.	Comply
• independent professional observers; and	The Committee employs an independent consultant who is an experienced ex Chief Investment Officer of an investment house. The consultant is present at all Committee meetings.	Comply
• expert advisors (on an ad hoc basis).	Expert advisors attend the Committee as required, depending on the nature of the decisions to be taken. For example, the actuary attends when the valuation is being considered and the investment consultant attends when strategic asset allocation decisions and investment matters are being discussed.	Comply
That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	All members are treated equally in terms of access to papers and to training that is given as part of the Committee processes.	Comply

Principle	**Surrey's Approach**	**Compliance**

SELECTION AND ROLE OF LAY MEMBERS		
That Committee or Panel members are made fully aware of the status, role and function they are required to perform on either a main or secondary committee.	Committee members are given initial and ongoing training to support them in their role as trustees.	Comply
VOTING		
The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	Surrey is fully compliant with this principle. Most decisions are reached by consensus, but voting rights remain with the Pension Fund Committee because the Council retains legal responsibility as the administering authority.	Comply
TRAINING/FACILITY TIME/EXPENSES		
That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.	This falls within the County Council's normal approach to member expenses. Pension Fund Committee members receive expenses. Training has been referred to above.	Comply
That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	The policy applies equally to all members of the Pension Fund Committee. All members currently enjoy voting rights.	Comply

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Principle	Surrey's Approach	Compliance
MEETINGS (FREQUENCY/QUORUM)		
That an administering authority's main committee or committees meet at least quarterly.	Surrey is fully compliant with this principle by holding quarterly and special appointment meetings. The Chief Finance Officer sends performance data and relevant information as appropriate. The quorum for the committee is three.	Comply
That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committee sits.	There is currently no secondary committee.	n/a
That administering authorities who do not include lay members in their formal governance arrangements, provide a forum outside of those arrangements by which the interests of key stakeholders can be represented	The Pension Fund holds an annual meeting in November each year to which all key stakeholders are invited. The meeting is a two-way process in which all delegates have the opportunity to ask questions and express their views. The Committee welcomes representations on any issue in writing at any time.	Comply
ACCESS		
That subject to any rules in the council's constitution, all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	All members of the Pension Fund Committee have equal access to committee papers, documents and advice.	Comply

Principle	Surrey's Approach	Compliance
SCOPE		
That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements	Surrey is fully compliant with this principle by bringing all investment, liability, benefit and governance issues to the Pension Fund Committee. An agenda will usually include a fund monitoring report, individual reports from managers, and reports on specific investment, administration and governance issues. A business plan is approved each year.	Comply
PUBLICITY		
That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements.	Surrey is fully compliant with this principle by publishing statements in the Annual Report and on its website.	Comply

12 Governance Policy Statement

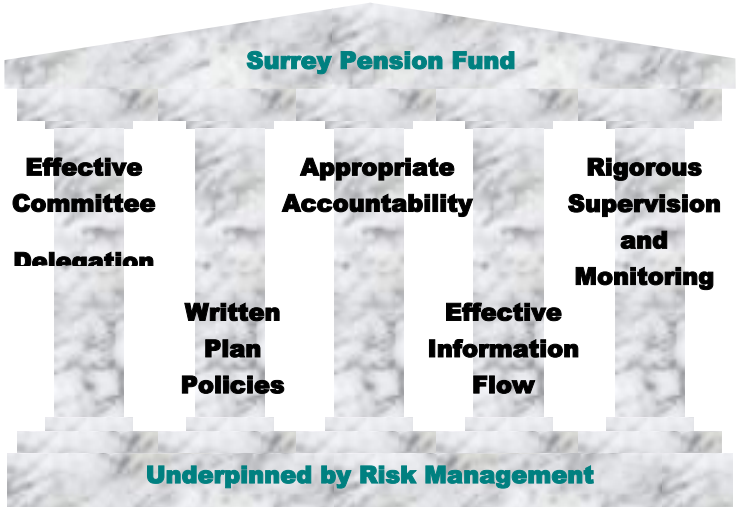
Governance Policy Statement for the Purposes of The Local Government Pension Scheme (Amendment) (No 2) Regulations 2005

This Statement is prepared for the purposes of the above Regulations. It sets out the policy of the Administering Authority in relation to its governance responsibilities for the Local Government Pension Scheme (LGPS).

Contents

1. Overall Governance Framework

The Administering Authority with its advisors has identified the following key areas (the "five principles") to support its overall governance framework.



The governance framework focuses on:

- The effectiveness of the Pension Fund Committee and officers to which delegated function has been passed, including areas such as decision-making processes, knowledge and competencies.
- The establishment of policies and their implementation.
- Clarity of areas of responsibility between officers and Pension Fund Committee members.
- The ability of the Pension Fund Committee and officers to communicate clearly and regularly with all stakeholders.
- The ability of the Pension Fund Committee and officers to ask for the appropriate information and advice and to interpret that information in their supervision and monitoring of the Scheme in all areas.
- The management of risks and internal controls to underpin the framework.

Overall responsibility for the governance of the Local Government Pension Scheme and for the approval of this document resides with the Pension Fund Committee.

2. Delegation of Functions

The following functions are delegated by the Administering Authority:

Scheme Administration

Governance Principles: Effective Committee delegation; appropriate accountability; rigorous supervision and monitoring

Including, but not exclusively or limited to, record keeping, calculation of and payment of benefits, reconciliation and investment of contributions, preparation of annual accounts, provision of membership data for actuarial valuation purposes.

The Administering Authority has responsibility for "Scheme Administrator" functions as required by HM Revenues and Customs (HMRC) under the Finance Act 2004.

Delegated to:

Pension Fund Committee (monitoring)

Chief Finance Officer (Pension Fund administration implementation)

Funding

Governance Principles: Effective Committee delegation; appropriate accountability; written plan policies

Including, but not exclusively or limited to, setting of the appropriate funding target for the Local Government Pension Scheme. The Chief Finance Officer shall be responsible for maintaining the Funding Strategy Statement (FSS). The Pension Fund Committee shall be responsible for approving the FSS.

Delegated to:

Pension Fund Committee (policy approval)

Chief Finance Officer (maintaining FSS and policy implementation)

Investment

Governance Principles: Effective Committee delegation; appropriate accountability; written plan policies

Including, but not exclusively or limited to, setting of an appropriate investment strategy or strategies, selection of investment managers, setting of performance benchmarks and regular monitoring of performance. The Pension Fund Committee shall be responsible for maintaining the Statement of Investment Principles.

Delegated to:

Pension Fund Committee (strategy approval, manager selection, benchmarks, monitoring)

Chief Finance Officer (Pension Fund investment implementation)

Communications

Governance Principle: Effective Information Flow; written plan policies

Including setting of a communication strategy, issuing or arranging to be issued re benefit statements, annual newsletters, annual report. The Pension Fund Committee shall be responsible for maintaining the Communications Policy.

Delegated to:

Pension Fund Committee (policy approval)

Chief Finance Officer (Pension Fund policy implementation)

Risk Management

Effective Committee delegation; appropriate accountability; written plan policies

Including the identification, evaluation and monitoring of risks inherent within the Local Government Pension Scheme. The Pension Fund Committee shall be responsible for approving the Risk Register. The Chief Finance Officer shall be responsible for maintaining the risk register.

Delegated to:

Pension Fund Committee (policy approval)

Chief Finance Officer (Pension Fund policy implementation)

3 Terms of Reference and Decision Making

Terms of Reference:

Governance Principle: Effective Committee delegation; written plan policies

The Pension Fund Committee's Terms of Reference as approved by Full Council on 19 March 2013.

Administration, Funding, Investment, Communications and Risk Management

In line with the Council's Constitution, the Pension Fund Committee shall oversee Pension Fund investments, the overall management of the Fund, the governance surrounding the Fund, and the administration of the Pension Scheme.

Structure of the Pension Fund Committee and representation:

Governance Principle: Effective Committee delegation

The Pension Fund Committee shall be made up of:

4 Conservative members;

1 Liberal Democrat member;

1 Independent member;

2 Districts and Boroughs Members

1 Employer Representative;

1 Employee Representative

Decision Making:

Governance Principle: Effective Committee delegation; rigorous supervision and monitoring

The Pension Fund Committee shall have full decision-making powers.

Each member of the Pension Fund Committee shall have full voting rights.

4. Operational Procedures

Frequency of Meetings:

Governance Principle: Effective Committee delegation; effective information flow

The Pension Fund Committee shall convene no less frequently than four times per year. The Pension Fund Committee shall receive full reports upon all necessary matters as decided by the Chief Finance Officer and any matters requested by members of the Pension Fund Committee.

Provision exists for the calling of special meetings if circumstances demand.

Competencies, Knowledge and Understanding:

Governance Principle: Effective Committee delegation; appropriate accountability

Officers and Members of the Pension Fund Committee shall undertake training to ensure that they have the appropriate knowledge, understanding and competency to carry out the delegated function. It is recommended that such knowledge, understanding and competency is evaluated on an annual basis to identify any training or educational needs of the Officers and the Pension Fund Committee.

Reporting and Monitoring:

Governance Principle: Rigorous supervision and monitoring; effective information flow

The Pension Fund Committee shall report to the Audit and Governance Committee on a frequency, and with such information as shall be agreed and documented, on a no less than annual basis, the minimum provision being the Pension Fund's annual report.

5 Review of this policy statement

Responsibility for this document resides with the Chief Finance Officer. It will be reviewed by the Chief Finance Officer no less frequently than annually. This document will be reviewed if there are any material changes in the administering authority's governance policy or if there are any changes in relevant legislation or regulation.

Pension Fund Committee: Terms of Reference

a) To undertake statutory functions on behalf of the Local Government Pension Scheme and ensure compliance with legislation and best practice.

b) To determine policy for the investment, funding and administration of the pension fund.

c) To consider issues arising and make decisions to secure efficient and effective performance and service delivery.

d) To appoint and monitor all relevant external service providers:

- fund managers;
- custodian;
- corporate advisors;
- independent advisors;
- actuaries;
- governance advisors;
- all other professional services associated with the pension fund.

e) To monitor performance across all aspects of the service.

f) To ensure that arrangements are in place for consultation with stakeholders as necessary

g) To consider and approve the annual statement of pension fund accounts.

h) To consider and approve the Surrey Pension Fund actuarial valuation and employer contributions.

F10	Chief Finance Officer/ Strategic Finance Manager (Pension Fund and Treasury)	Borrowing, lending and investment of County Council Pension Fund moneys, in line with strategies agreed by the Pension Fund Committee. Delegated authority to the Chief Finance Officer to take any urgent action as required between Committee meetings but such action only to be taken in consultation with and by agreement with the Chairman and/or Vice Chairman of the Pension Fund Committee and any relevant Consultant and/or Independent Advisor.
H4	Lead Pensions Manager	To exercise discretion (excluding decisions on admitted body status) in

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H5	Chief Finance Officer	relation to the Local Government Pension Scheme where no policy on the matter has been agreed by the Council and included in the Discretionary Pension Policy Statement published by the Council, subject to any limitations imposed and confirmed in writing from time to time by the Chief Finance Officer. To determine decisions conferring 'admitted body' status to the Pension Fund where such requests are submitted by external bodies.

Responsible Investment Policy

Introduction

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.

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

The fund complies with the Myners Principles of investment management and the UK Stewardship Code.

The Fund will review its Responsible Investment and Stewardship Policy annually. The Fund's officers will carry out this review and propose any changes to the Pension Fund Committee for consideration.

Scope

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.

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.

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.

General Principles

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.

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.

Voting Policy

1 Audit & Accountability

The audit and financial reporting 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, 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 and when the incumbent audit firm was appointed.

- **Approval of Financial Statements**

Where there is a qualified audit statement; where there is uncertainty about the future viability of the business; where there is a restatement 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.

- **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 a suitable alternative resolution, where available, such as the sustainability report.

2 The Committee & Committees

- **Nomination & Succession Planning**

There should be a formal, rigorous and transparent procedure for the appointment of new directors to the Committee. The Committee 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.

Committees should be composed of individuals with adequate professional understanding of the matters to be resolved. This is particularly the case for the audit and risk committee. The fund may choose to abstain where there is insufficient evidence of appropriate competencies.

- **Separation of Chairman & Chief Executive Officer (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.

- **Committee Balance and Diversity**

Companies should seek to ensure that their Committees 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**

Evidence of reward for failure has lead to shareholder concerns over the length of notice periods for directors which have been used in the past to inform severance pay levels. Where the terms of executive pay policy allow overly generous severance pay on early termination of an executive contract, the fund may choose to register concern via an abstention vote.

Director notice periods are significantly important. Where an executive director's notice period exceeds twelve 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 Committee 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.

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, for example, audit or HR.

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 Shareholders' Rights and 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.

- **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 equitable 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.

- **Controlling Shareholder**

Where a controlling shareholder is present on the share register, it is important that minority investors understand fully the nature of the rights held by that shareholder. Minority investors expect a formal relationship agreement to be in place and for this agreement to be fully disclosed to all shareholders.

5 Mergers and Acquisitions (M&A)

Support will be given to mergers and acquisitions that enhance shareholder returns in the longer term and encourage 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 Committee 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 Committee. This includes anti-takeover measures.

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.

7 Political & Charitable Donations

The fund recognises that some legitimate business related expenditure, such as marketing or sponsorship, may be construed as political under the terms of current legislation in some markets. Where authority for political expenditure fails to distinguish the amounts involved, or the period covered, or the amounts or period are considered excessive, the fund will not support the authority.

In addition 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.

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.

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.

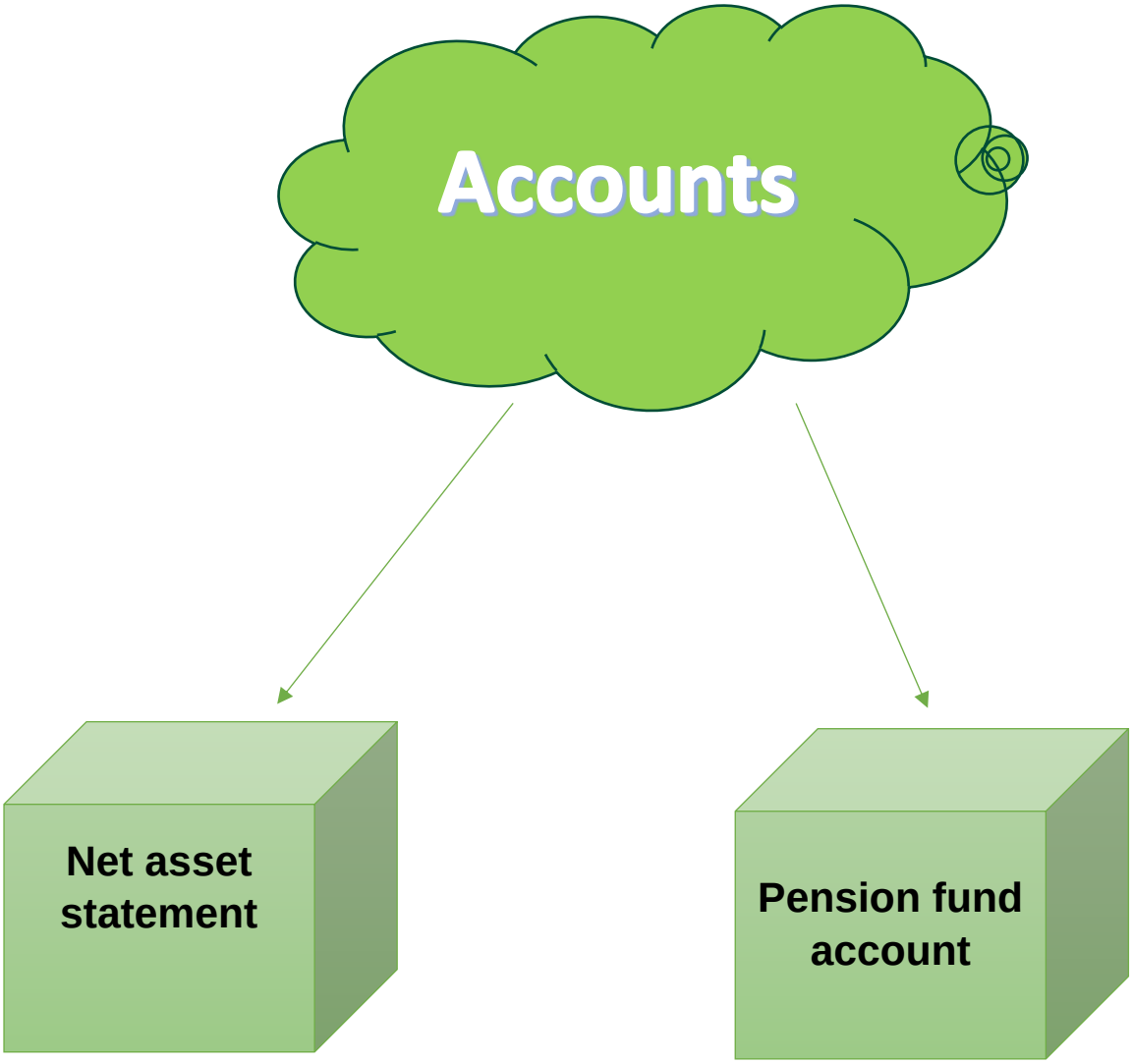
The Principles of the UK Stewardship Code

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 stewardship activities.
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.

The Committee will provide an annual report on how the Surrey Pension Fund satisfies its UK Stewardship Code obligations requirements.

Statement of Accounts



12 Statement of Responsibilities and Certification of Accounts

The Responsibilities of the County Council

The County Council is required:

• to make arrangements for the proper administration of the financial affairs of the Fund and to secure that one of its officers has the responsibility for the administration of those affairs. In this Authority, that officer is the Chief Finance Officer & Deputy Director for Business Services (Chief Finance Officer).
• to manage the Fund's affairs to secure economic, efficient and effective use of resources and safeguard its assets; and
• to approve the statement of accounts.

The Responsibilities of the Chief Finance Officer

The Chief Finance Officer is responsible for the preparation of the Fund's statement of accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in Great Britain ("the Code of Practice").

In preparing this statement of accounts, the Chief Finance Officer has:
•selected suitable accounting policies and then applied them consistently;
• made judgements and estimates that were reasonable and prudent;
• complied with the Code of Practice

The Chief Finance Officer has also:

• kept proper accounting records which were up to date;
• taken reasonable steps for the prevention and detection of fraud and other irregularities.

I certify that the statement of accounts set out on pages 133 present a true and fair view of the Surrey County Council Pension Fund at 31 March 2018 and its income and expenditure for the year then ended.

Kevin Kilburn BA CPFA

ACTING SECTION 151 OFFICER

SURREY PENSION FUND ACCOUNTS 2017/2018

The accounts on the following pages give a stewardship report on the financial transactions of the Surrey Pension Fund during 2017/2018 and of the disposition of its assets at 31 March 2018.

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

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

The number of employees in the fund and the number of pensioners as at 31 March 2017 and 31 March 2018 are:

31 Mar 2017		**31 Mar 2018**
34,298	Employees in the fund	35,802
24,025	Pensioners	25,135
41,573	Deferred pensioners	45,079
99,896	**Total**	**106,016**

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Surrey pension fund account

2016/2017 £000		Note	2017/2018 £000
	Contributions and benefits		
192,802	Contributions receivable	7	**178,283**
6,848	Transfers in	8	**12,881**
199,650			**191,164**
-136,484	Benefits payable	9	**-144,146**
-6,694	Payments to and on account of leavers	10	**-9,527**
-13,217	Investment and governance expenses	14	**-12,222**
-1,250	Administration expenses		**-1,626**
-157,645			**-167,521**
42,005	**Net additions from dealings with members**		**23,643**
	Return on investments		
62,306	Investment income	16	**65,751**
-1,068	Taxes on income	15	**-1,032**
541,953	Change in market value of investments	17	**98,662**
603,191	**Net return on investments**		**163,381**
645,196	**Net increase in the fund during the year**		**187,024**
3,223,663	**Net assets of the fund At 1 April**		**3,868,859**
3,868,859	**At 31 March**		**4,055,883**

Net asset statement

31 Mar 2017 £000		Note	31 Mar 2018 £000
	Investment assets	17	
583,302	Bonds		**601,208**
2,288,136	Equities		**2,413,734**
275,367	Property unit trusts		**321,737**
390,257	Diversified growth		**394,288**
145,113	Private equity		**155,782**
	Derivatives	17c	
	- Futures		
1,050	- Foreign exchange contracts		**1,327**
117,498	Cash		**80,636**
42,000	Other short term investments		**60,000**
8,220	Other investment balances	17b	**4,740**
	Investment liabilities		
	Derivatives	17c	
0	- Futures		**0**
-1,095	- Foreign exchange contracts		**-1**
-4,876	Other investment balances	17b	**-3,393**
0	Borrowings		**0**
3,844,972	**Net investment assets**		**4,030,058**
9,075	**Long-term debtors**	12	**7,260**
22,371	**Current assets**	11	**29,861**
-7,559	**Current liabilities**	13	**-11,296**
3,868,859	**Net assets of the fund at 31 March**		**4,055,883**

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 25 of these accounts. 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.

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Note 1: Description of the fund

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

The following description of the fund is a summary only. For more detail, reference should be made to the Surrey Pension Fund Annual Report 2017/18 and the underlying statutory powers underpinning the scheme, namely the Superannuation Act 1972 and the Local Government Pension Scheme (LGPS) Regulations.

a) General

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

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

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

During 2017/18 the investment decision making and governance of the fund was undertaken by the Pension Fund Board, a committee of the Administering Authority, with representation on behalf of employers and members.

b) Membership

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

Organisations participating in the Surrey Pension Fund include:

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

c) Funding

Benefits are funded by contributions and investment earnings. Contributions are made by active members of the fund in accordance with the LGPS (Benefits, Membership and Contributions) Regulations 2007 and ranged from 5.5% to 12.5% of pensionable pay for the financial year ending 31 March 2018. Employee contributions are matched by employers' contributions which are set based on triennial actuarial funding valuations. The last such valuation was at 31 March 2016 and new rates applied from April 2017. Currently employer contribution rates range from 13.4% to 33.2% of pensionable pay.

d) Benefits

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

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

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).

	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	**LGPS 2014 employee contribution rates for 2017/18**

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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%

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

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

Note 2: Basis of preparation

The Statement of Accounts summarises the fund's transactions for the 2017/18 financial year and its position at the year end at 31 March 2018. The accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

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

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

Accounting standards issued, but not yet adopted.
IFRS 9 Financial instruments – Includes changes to the classification of financial assets and a forward looking 'expected loss' model for impairment rather than the 'incurred loss' model under IAS39.

The impact of the standard issued but not yet adopted cannot yet be quantified.

Note 3: Summary of significant accounting policies

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

Fund account – revenue recognition

a) Contribution income

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

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

b) Transfers to and from other schemes

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

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

c) Investment income

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i) Interest income

Interest income is recognised in the fund account as it accrues using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount premium, transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income

Dividend income is recognised on the date the shares are quoted as ex-dividend. Any amount not received by the end of the reporting period is disclosed in the net asset statement as a current financial asset.

iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net asset statement as a current financial asset.

iv) Movement in the net market value of investments

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during in the year.

d) Private equity

Distributions and drawdowns from private equity partnerships are accounted for according to guidance from the private equity manager as to the nature of the distribution or drawdown. Income and purchases and sales are recognised at the date the capital call or distribution falls due.

Fund account – expense items

e) Benefits payable

Pensions and lump-sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the net asset statement as current liabilities.

f) Taxation

The fund is a registered public service scheme under section 1 (1) of the Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments may be subject to withholding tax in the country of origin. Irrecoverable tax is accounted for as a fund expense as it arises. Tax on income due but unpaid at the 31 March 2018 is reported as a current liability.

g) Administration expenses

Pension administrative expenses reflect the costs incurred in the payment of pensions and other benefits, the maintenance of member records and provision of scheme and entitlement information. Costs incurred in relation to specific employers are recharged to those individual organisations and therefore excluded from the accounts.

All administration expenses are accounted for on an accruals basis. The relevant staffing costs of the pension administration team are recharged to the fund. Management, accommodation and other overheads are apportioned to the fund in accordance with council policy.

h) Investment and governance expenses

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

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

Net assets statement

i) Financial assets

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

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

i) Market quoted investments

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

ii) Fixed interest securities

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

iii) Unquoted investments

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

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

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

iv) Investments in private equity funds and unquoted listed partnerships are valued based on the fund's share of the net assets in the private equity fund or limited partnership using the latest financial statements published by the respective fund managers in accordance with the guidelines set out by the International Private Equity and Venture Capital Guidelines, which follow the valuation principles of IFRS.

v) Limited partnerships

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

vi) Pooled investment vehicles

Pooled investment vehicles are valued at closing bid price if both bid and offer prices are published; or if singularly priced, at the closing single price.

j) Foreign currency transactions

Dividends, interest and purchases and sales of investments in foreign currencies have been accounted for at the spot rate on the date of transaction. End-of-year spot market exchange rates are used to value cash balances held in foreign currency bank accounts, market values of overseas investments and purchases and sales outstanding at the end of the reporting period.

k) Derivatives

The fund uses derivative financial instruments to manage its exposure to specific risks arising from its investment activities. The fund does not hold derivatives for speculation purposes.

Derivative contract assets are fair valued at bid prices and liabilities are fair valued at offer prices. Changes in fair value of derivative contracts are included in the change in market value.

The value of futures 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.

l) Cash and cash equivalents

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash and that are subject to minimal changes in value.

m) Financial liabilities

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

n) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the scheme actuary in accordance with the requirement of IAS 19 and relevant actuarial standards.
As permitted under IAS 26, the fund has opted to disclose the actuarial present value of promised retirement benefits by way of a note to the net asset statement.

o) Additional voluntary contributions

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

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

Note 4: Critical judgements in applying accounting 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 2018 was £155.8 million (£145 million at 31 March 2017).

Pension Fund Liability

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

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

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

The items in the net assets statement or subsequent notes as at 31 March 2018 for which there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	Estimation of the net liability to pay pension depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets. A firm of consulting actuaries is engaged to provide the fund with expert advice about the assumptions to be applied.	The net pension liability of the fund would change. An increase in the discount rate would result in a corresponding decrease in the pension liability. An increase in earnings would increase the value of liabilities, as would an increase in life expectancy.
Private equity	Private equity investments, both limited partnership and fund of funds, are disclosed at fair value, provided by the administrators of the funds. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the financial statement are £145 million. There is a risk that this investment may be over or under stated in the accounts.
Fund of fund investments	Where investments are made into a fund of fund structure there is an additional level of separation from the fund. There may be a lack of clarity over the classification of the sub funds and investment transactions	The total private equity fund of fund investments are £95 million. There is a risk that asset or investment transaction misclassification may occur.

Note 6: Events after the balance sheet date

The Director of Finance and section 151 officer left the Council in July 2018. The Deputy Chief Finance Officer is acting as the interim s151 officer and has certified the Statement of Accounts.

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 Fund's assets and liabilities. Those events taking place after the date of authorisation for issue will not be reflected in the statement of accounts.

Note 7: Contributions receivable

By category

2016/2017 £000		2017/2018 £000
105,316	Employers	97,181
49,390	Employers deficit	42,982
38,096	Members	38,121
192,802		**178,283**

2016/2017 £000		2017/2018 £000
87,529	Administering authority	83,861
85,967	Scheduled bodies	86,022
19,306	Admitted bodies	8,400
192,802		**178,283**

The latest actuarial valuation carried out as at 31 March 2016, set contribution rates for fund employers with effect from April 2017. The financial year 2017/2018 is the first year of the revised employer contribution rates.

Note 8: Transfers in from other pension funds

2016/2017 £000		2017/2018 £000
0	Group transfers from other schemes	0
6,848	Individual transfers in from other schemes	**12,881**
6,848		**12,881**

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Note 9: Benefits payable

By category

2016/17 £000		2017/18 £000
114,054	Pensions	119,064
19,023	Commutation and lump sum retirement benefits	21,606
3,355	Lump sum death benefits	3,399
52	Interest on late payment of benefits	77
136,484		**144,146**

By employer*

2016/2017 £000		2017/2018 £000
64,320	Administering Authority	69,389
61,003	Scheduled Bodies	63,587
11,109	Admitted Bodies	11,093
136,432		**144,069**

Note 10: Payments to and on account of leavers

2016/2017 £000		2017/2018 £000
6,409	Group transfers to other schemes	9,257
0	Individual transfers to other schemes	0
316	Refunds of contributions	283
-31	Payments for members joining state schemes	-13
6,694		**9,527**

Note 11: Current assets

2016/2017 £000		2017/2018 £000
2,619	Contributions - employees	3,215
9,337	Contributions - employer	9,838
10,415	Sundry debtors	16,808
22,371		**29,861**

Analysis of current assets

2016/2017 £000		2017/2018 £000
3,730	Central government bodies	5,612
15,746	Other local authorities	19,122
2,895	Other entities and individuals	5,128
22,371		**29,861**

Note 12: Long term debtors

2016/2017 £000		2017/2018 £000
9,075	Central government bodies	7,260
9,075		**7,260**

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

On 11 March 2013 the total value of the shortfall was agreed as £18.150m, to be made in ten equal, annual instalments commencing on 15 April 2013. The full amount was recognised as contributions during 2012/13. A corresponding debtor was created. The first instalment of £1.815m was received on 26 March 2013 meaning that the remaining nine instalments were due in excess of one year from the 31 March 2013, the whole of the remaining balance was therefore included as a long term debtor in the accounts. The outstanding balance as at 31 March 2018 is £9.075m but £1.815m was due in 2017/18, leaving a long term debtor of £7.260m.

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Note 13: Current liabilities

2016/2017 £000		2017/2018 £000
7,368	Sundry creditors	11,094
123	Benefits payable	202
7,491		**11,296**

Analysis of current liabilities

2016/2017 £000		2017/2018 £000
1,574	Central government bodies	1,418
1,848	Other local authorities	6,254
4,069	Other entities and individuals	3,624
7,491		**11,296**

Note 14: Investment and governance expenses

2016/2017 £000		2017/2018 £000
12,105	Investment management fees	11,263
103	Investment custody fees	239
1,009	Oversight and governance costs	721
13,217		**12,222**

The investment management fees includes £613k (2016/17:£ 1.0million) in respect of performance-related fees paid/payable to the fund's investment managers. It also includes £1.1million in respect of transaction costs (2016/17: £1.5million).

As part of its oversight and governance costs in 2017/18, the fund had also spent £144k in respect of pooling costs as part of Surrey Pension Fund's transition into the Border to Coast Pensions Partnership (BCPP)

Note 15: Taxes on Income

2016/2017 £000		2017/2018 £000
988	Withholding tax – equities	978
80	Withholding tax – property	54
1,068		**1,032**

Note 15b: External Audit Costs

2016/2017 £000		2017/2018 £000
27	Payable in respect of external audit	27
27		**27**

Note 16: Investment income

2016/2017 £000		2017/2018 £000
	Bonds	
4,079	UK	**3,667**
8,060	Overseas	**7468**
	Equities	
22,358	UK	**24,959**
14,274	Overseas	**11,260**
7,808	**Property unit trusts**	**9,062**
1,226	**Diversified growth**	**1,052**
3,249	**Private equity**	**2,315**
745	**Interest on cash deposits**	**4,807**
507	**Other**	**1,161**
62,306		**65,751**

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Note 17a: Reconciliation of movements in investments and derivatives

	Market value at 31 Mar 2017	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Market movements	Market value at 31 Mar 2018
	£000	£000	£000	£000	£000
Bonds	**583,327**	304,323	-283,524	-2,918	**601,208**
Equities	**2,288,136**	1,938,482	-1,845,436	32,552	**2,413,734**
Property unit trusts	**275,367**	88,284	-54,202	12,288	**321,737**
Diversified growth	**390,257**	2,327	0	1,704	**394,288**
Private equity	**145,228**	53,184	-50,680	8,050	**155,782**
Derivatives					
- Futures		311	-406	95	
- Forex contracts	**-45**	28,423	-68,141	41,089	**1,326**
	3,682,270	**2,415,334**	**-2,302,389**	**92,860**	**3,888,075**
Cash	**117,498**			5,802	**80,636**
Other Short Term Investments	**42,000**				**60,000**
Other investment balances	**3,344**				**1,347**
Borrowing					
	3,845,112			**98,662**	**4,030,058**

	Market value at 31 Mar 2016	Purchases during the year and derivative payments	Sales during the year and derivative receipts	Market movements	Market value at 31 Mar 2017
	£000	£000	£000	£000	£000
Bonds	**511,051**	41,289	-33,783	64,745	**583,302**
Equities	**1,851,024**	368,898	-429,215	497,429	**2,288,136**
Property unit trusts	**225,690**	75,125	-25,937	489	**275,367**
Diversified growth	**376,686**	243,208	-242,797	13,160	**390,257**
Private equity	**129,353**	19,465	-29,763	26,058	**145,113**
Derivatives					
- Futures	**26**	-307	38	243	**0**
- Forex contracts	**-6,287**	72,443	-5,711	-60,490	**-45**
	3,087,543	**820,121**	**-767,168**	**541,634**	**3,682,130**
Cash	**64,302**			319	**117,498**
Other short term investments	**47,000**				**42,000**
Other investment balances	**7,501**				**3,344**
Borrowing	**0**				**0**
	3,196,346			**541,953**	**3,844,972**

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Note 17b: Analysis of investments

	31 Mar 2017 £000s	31 Mar 2018 £000s
Fixed interest securities		
UK public sector & quoted	298,283	205,115
UK pooled funds	0	0
Overseas public sector & quoted	66,803	0
Overseas pooled fund	218,216	396,093
	583,302	**601,208**
Equities		
UK quoted	279,493	605,423
UK pooled funds	389,731	418,042
Overseas quoted	990,625	320,896
Overseas pooled funds	628,287	1,069,373
	2,288,136	**2,413,734**
Property unit trusts		
UK property funds	263,100	279,879
Overseas property funds	12,267	41,858
	275,367	**321,737**
Diversified growth		
UK diversified growth funds	0	0
Overseas diversified growth funds	390,257	394,288
	390,257	**394,288**
Private equity		
UK limited partnerships	25,859	22,717
Overseas limited partnerships	24,237	41,411
UK fund of funds	0	0
Overseas fund of funds	95,017	91,654
	145,113	**155,782**
Derivatives		
Futures		
FX forward contracts	-45	1,326
	-45	**1,326**
Cash deposits	**117,498**	**80,636**
Other short term investments	**42,000**	**60,000**
Other investment balances		
Outstanding sales	1,385	357
Outstanding purchases	-4,876	-3,393
Tax due on accrued income	0	
Accrued income - dividends and interest	6,835	4,383
	3,344	**1,347**
Total investments	**3,844,972**	**4,030,058**

Note 17c: Analysis of derivatives

Futures

Futures contracts are exchange traded contracts to buy or sell a standard quantity of a specific asset at a pre-determined future date. As at 31 March 2018 the fund had no future contracts in place. At 31 March 2017 the fund had four futures contracts in place with an unrealised loss of £61k.

31 March 2018

Contract	Expiration date	Expiration date within	Type of underlying investment	Economic exposure £'000	Asset £'000	Liability £'000
Futures	**-**	**-**	**-**	**0**	**0**	**0**
				0	**0**	**0**

31 March 2017

Contract	Expiration date	Expiration date within	Type of underlying investment	Economic exposure £'000	Asset £'000	Liability £'000
Futures	08/06/2017	3 Months	US Treasury Bonds	-966	0	-9
Futures	21/06/2017	3 Months	US Treasury Bonds	844	0	-44
				-1,156		
Futures	21/06/2017	3 Months	US Treasury Bonds		0	0
Futures	28/06/2017	3 Months	UK Government Bonds	-3,572	0	-8
				-4,850	**0**	**-61**

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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 2018 the Fund had forward currency contracts in place with a net unrealised gain of £1,327k (net unrealised loss of £45k at 31 March 2017).

2017/18

No of contracts	Contract settlement date within	Currency		Notional amount (local currency)		Asset	Liability
		Bought	Sold	Bought (000)	Sold (000)	£'000	£'000
1	One Month	GBP	JPY	137	-20,650	0	0
5	Two Months	GBP	EUR	118450	-134,064	702	0
5	Two Months	GBP	JPY	66,837	-9,954,387	19	0
8	Two Months	GBP	USD	374,615	-525,891	606	0
						1,327	**0**

2016/17

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	1 Month	CAD	GBP	381	-230	0	-1
2	1 Month	EUR	GBP	31	-26	0	0
1	2 Months	EUR	GBP	143	-123	0	-1
1	1 Month	GBP	AUD	8	-13	0	0
1	1 Month	GBP	BRL	13	-51	0	0
1	1 Month	GBP	EUR	3	-4	0	0
6	2 Months	GBP	EUR	7,635	-8,831	76	0
5	3 Months	GBP	EUR	109,884	-128,613	0	-268
1	1 Month	GBP	HKD	21	-207	0	0
1	2 Months	GBP	JPY	1,834	-254,405	7	0
4	3 Months	GBP	JPY	79,531	-11,190,096	0	-843
1	2 Months	GBP	SEK	3,205	-35,130	56	0
1	1 Month	GBP	USD	36	-45	0	0
4	2 Months	GBP	USD	12,531	-15,672	9	0
7	3 Months	GBP	USD	349,613	-436,628	902	0
1	1 Month	GBP	ZAR	49	-818	1	0
1	1 Month	IDR	GBP	1,011,204	-61	0	0
3	1 Month	JPY	GBP	222,490	-1,611	0	-14
3	1 Month	JPY	USD	46,526	-419	0	-1
1	2 Months	JPY	USD	254,440	-2,230	0	45
1	1 Month	USD	GBP	146	-117	0	-1
2	2 Months	USD	GBP	2,200	-1,769	0	-11
1	1 Month	USD	JPY	4	-450	0	0
1	1 Month	ZAR	GBP	11	-1	0	0
						1,050	**-1,095**

Stock Lending

Stock lending is the act of loaning a stock, derivative or other security to an investor or firm. During the financial year 2017/18 the fund operated a stock lending programme in partnership with the fund custodian. As at 31 March 18 the value of quoted securities on loan was £132.5million in exchange for collateral held by the fund custodian at fair value of £144.1million.

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Note 17d: Investments analysed by fund manager

Market value 31 March 2017 £000	%	Manager	Market value 31 March 2018 £000	%
1,066,206	27.8	Legal & General Investment Management	1,151,591	28.6
382,372	10.0	Majedie Asset Management	373,811	9.3
300,771	7.8	UBS Asset Management	311,993	7.7
486,154	12.7	Marathon Asset Management	498,553	12.4
307,211	8.0	Newton Investment Management	317,106	7.9
312,688	8.2	Western Multi Asset Credit	322,509	8.0
74,119	1.9	Franklin Templeton Investments	73,663	1.8
143,695	3.7	Baillie Gifford Life Limited	150,596	3.7
232,323	6.1	CBRE Global Multi-Manager	260,170	6.5
68,875	1.8	Darwin Property Investment Management	73,508	1.8
123,768	3.2	Ruffer	122,576	3.0
122,793	3.2	Aviva	121,117	3.0
3,620,975			**3,777,193**	

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 2017 £000	% of total fund	Security	Market value 31 March 2018 £000	% of total fund
464,390	14.5	Legal & General World Developed Equity Index	496,453	12.3
0	0	Marathon Global Contractual Fund	494,553	12.3
355,919	11.1	Legal & General UK Equity Index	376,553	9.3

Note 18a: Classification of financial instruments

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

As at 31 March 2017				As at 31 March 2018		
Designated as fair value though profit and loss £000	Loans and receivables £000	Financial liabilities at amortised costs £000		Designated as fair value though profit and loss £000	Loans and receivables £000	Financial liabilities at amortised costs £000
			Financial assets			
583,802	0	0	Bonds	601,208		
2,288,136	0	0	Equities	2,413,735		
275,367	0	0	Property unit trusts	321,737		
390,257	0	0	Diversified growth	394,288		
145,113	0	0	Private equity	155,782		
1,098	0	0	Derivatives			
0	117,498	0	Cash		80,636	
	42,000		Other short term investments		60,000	
8,220	0	0	Other investment balances	4,739		
0	31,446	0	Debtors		37,121	
3,691,493	**190,944**	**0**	**Total financial assets**	**3,891,489**	**177,757**	
			Financial liabilities			
-1,142	0	0	Derivatives	-1		
-4,876	0	0	Other investment balances	-3393		
0	0	-7,559	Creditors			-11,296
0	0	0	Borrowings			
-6,018	**0**	**-7,559**	**Total financial liabilities**	**-3394**		**-11,296**
3,685,518	**190,944**	**-7,559**		**3,888,095**	**177,757**	**-11,296**

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Note 18b: Net gains and losses on financial instruments

31 March 2017 £000		31 March 2018 £000
	Financial Assets	
602,124	Designated at Fair Value through profit and loss	92,860
319	Loans and Receivables	5,802
	Financial Liabilities	
-60,490	Fair Value through profit and loss	0
0	Financial liabilities at amortised cost	0
541,953	**Total**	**98,662**

Note 18c: 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 2018	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 through profit & loss	3,510,908	209,388	223,545	3,943,841
Total financial assets	3,510,908	209,388	**223,545**	3,943,841
Financial liabilities				
Financial liabilities through profit & loss	0	-3,393	0	-3,393
Total financial liabilities	**0**	**-3,393**	**0**	**-3,393**
Net financial assets	**3,510,908**	**205,995**	**223,545**	**3,940,448**

31 March 2017	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 through profit & loss	3,322,216	172,746	195,477	3,690,439
Total financial assets	**3,322,216**	**172,746**	**195,477**	**3,690,439**
Financial liabilities				
Financial liabilities through profit & loss	-4,876	0	0	-4,876
Total financial liabilities	**-4,876**	**0**	**0**	**-4,876**
Net financial assets	**3,317,340**	**172,746**	**195,477**	**3,685,563**

Note 18c: Book cost

The book cost of all investments at 31 March 2018 is £3,055million (£2,760million at 31 March 2017).

Note 19: Outstanding commitments

At 31 March 2018 the Fund held part paid investments on which the liability for future calls amounted to £127.0million (£89million as at 31 March 2017).

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

Risk and risk management

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

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

a) **Market risk**

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

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

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

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

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

Other price risk – Sensitivity Analysis
PIRC Ltd has provided the fund with an analysis of historical asset class returns to determine potential movements in the market price risk of investments during 2017/18 reporting period. The potential volatilities are consistent with a one standard deviation movement in the change in value of the assets over the latest three years.

Asset type	Value at 31 March 2018 £000	Change	Value on increase £000	Value on decrease £000
UK equities	1,023,466	9.35%	1,119,188	927,744
Overseas equities	1,390,269	9.54%	1,522,927	1,257,611
Bonds	601,208	4.38%	627,541	574,875
Cash	80,636	0.03%	83,055	78,217
Other short term investments	60,000	0.03%	60,020	59,980
Property	321,747	3.46%	332,866	310,608
Alternatives	155,782	6.61%	166,079	145,485
Diversified growth fund	394,288	3.74%	409,037	379,539
Other assets	2,625	0.03%	3,585	3,585
Total Investment Assets	4,030,021	6.01%	4,324,298	3,737,644

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Asset type	Value at 31 March 2017 £000	Change	Value on increase £000	Value on decrease £000
UK equities	669,225	8.89%	728,704	609,746
Overseas equities	1,618,911	9.28%	1,769,124	1,468,698
Fixed interest bonds	383,930	5.95%	406,770	361,090
Index linked	199,371	8.89%	217,095	181,647
Cash	49,844	0.01%	49,849	49,839
Other short term investments	42,000	0.01%	42,004	41,996
Property	275,367	1.96%	280,764	269,970
Alternatives	145,113	6.96%	155,213	135,013
Diversified growth fund	390,257	3.84%	405,229	375,285
Other assets	3,299	0.01%	3,585	3,585
Total Investment Assets	3,777,317	5.98%	4,058,337	3,496,869

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

Interest rate risk

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

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

The fund's direct exposure to interest rate movements as at 31 March 2018 and 31 March 2017 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value.

As at 31 March 2017 £000		As at 31 March 2018 £000
49,844	Cash & cash equivalents	80,636
42,000	Other short term investments	60,000
383,930	Fixed interest securities	396,093
475,774	**Total**	**536,729**

Interest rate risk sensitivity analysis

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

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

Asset type	Carrying amount as at 31 March 2018	Change in net assets +100 bps	- 100 bps
	£000	£000	£000
Cash & cash equivalents	80,636	81	-81
Other short term investments	60,000	60	-60
Fixed interest securities	396,093	396	-396
Total	**536,729**	**537**	**-537**

Asset type	Carrying amount as at 31 March 2017	Change in net assets +100 bps	- 100 bps
	£000	£000	£000
Cash & cash equivalents	49,844	50	-50
Other short term investments	42,000	42	-42
Fixed interest securities	383,930	384	-384
Total	**475,774**	**476**	**-476**

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.

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Currency risk – sensitivity analysis
PIRC Ltd has provided the fund with an analysis of historical exchange rate movements to determine potential changes in the fair value of assets during the 2017/18 reporting period due to exchange rate movements.

The analysis assumes all other variables remain constant.

Asset type	Value at 31 March 2018 £000	% Change	Value on increase £000	Value on decrease £000
Equities	877,881	4.93%	921,173	834,589
Fixed interest	396,093	4.93%	415,626	376,560
Property and Private Equity	174,923	4.93%	183,549	166,297
Diversified Growth	394,288	4.93%	413,732	374,844
Cash and Other Assets	7,397	4.93%	7,762	7,032
Total	1,850,582	4.93%	1,941,842	1,759,322

For comparison last year figures are included below.

Asset type	Value at 31 March 2017 £000	% Change	Value on increase £000	Value on decrease £000
Equities	1,141,725	8.2%	1,235,371	1,048,079
Fixed interest	229,245	8.2%	248,048	210,442
Property and Private Equity	131,522	8.2%	142,310	120,734
Diversified Growth	390,257	8.2%	422,267	358,247
Cash and Other Assets	38,880	8.2%	42,069	35,691
Total	1,931,629	8.2%	2,090,065	1,773,193

b) Credit risk

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

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

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

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

The fund has agreed a total of £60m in short fixed term deposits as part of the treasury management strategy; these include £60 million of fixed term deposits with other Local Authorities.

Fixed Term Deposits	**No. of days**	**Balance at 31 March 2018 £000**
Leeds City Council	141	10,000
London Borough of Barking & Dagenham	91	5,000
Eastleigh Borough Council	89	5,000
Eastleigh Borough Council	90	5,000
Plymouth City Council	92	5,000
Leeds City Council	91	10,000
Woking Borough Council	120	5,000
Thurrock Council	120	5,000
Glasgow City Council	94	10,000
Other short term investments		**60,000**

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

The fund has a call account with Natwest Bank and Lloyds Bank, an account with a money market fund, managed by Goldman Sachs Asset management and a term deposit placed with Nationwide Building society. In line with the treasury strategy, the maximum deposit level allowed with each counterparty is £25 million.

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Balance at 31 March 2017 £000		Balance at 31 March 2018 £000
	Term Deposits	
	Nationwide	0
	Call account	
	Natwest	0
0	Lloyds	20,000
	Money market fund	
490	Goldman Sachs	4,000
25,000	Aberdeen MMF	5,500
	Current account	
586	HSBC	64
26,076	**Internally Managed Cash**	**29,564**
91,422	Externally Managed Cash	51,072
117,498	**Total Cash**	**80,636**

The fund's cash holding under its treasury management arrangements as at 31 March 2018 was £29.6million (£26.0million at 31 March 2017).

c) Liquidity risk

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

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

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

The fund is able to borrow cash to meet short-term cash requirements, no such instances occurred during 2016/17 or 2017/18

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

d) Derivative risk

Some portfolios in which the fund invests may utilise financial derivative instruments to reduce risks or costs or to generate additional returns to meet the portfolio's objectives. Use of such derivatives does not guarantee a positive result for the portfolio.

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

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

Note 21: Related party transactions

i) Employer pension contributions paid by Surrey County Council in 2017/18 amounted to £62,796k (£67,508k in 2016/17).

2016/2017 £000		2017/2018 £000
44,261	Employers' current service contributions	41,031
22,351	Lump sum payments to recover the deficit in respect of past service	21,287
896	Payments into the fund to recover the additional cost of early retirement liabilities	479
67,508		**62,796**

ii) Surrey Pension Fund paid Surrey County Council £1,847k for services provided in 2017/18 (£1,508k in 2016/17).

2016/2017 £000		2017/2018 £000
258	Treasury management, accounting and managerial services	221
1,250	Pension administration services	1,626
1,508		**1,847**

iii) Net amounts owed by Surrey County Council to the fund as at 31 March 2018 were £5,218k (£5,621k at 31 March 2017).

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Note 22: Key management personnel

The below employees of Surrey County Council hold key positions in the financial management of the Surrey Pension Fund. Their financial relationship with the fund is disclosed as a proportion of salary costs, including employer pension contributions and national insurance contributions that can be attributed to the fund. From 2nd October 2017 The Treasury Team had been separated as a function from the Pensions Team which had an effect on the time Key Management allocated to the Pension Fund.

2016/17 £	Position	2017/18 £	
22,859	Director of Finance	24,109	1
75,795	Head of Pensions	80,681	2
47,139	Senior Specialist Advisor	25,398	2
55,545	Senior Accountant	49,059	3
201,338		**179,247**	

2016/17
1. 15% of time allocated to pension fund
2. 70% of time allocated to pension fund
3. 100% of time allocated to pension fund

Oct 2017 - Onwards
1. 15% of time allocated to pension fund
2. 100% of time allocated to pension fund
2. 100% of time allocated to pension fund

Note 23: Custody

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

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

Private Equity Manager	Custody Provider
BlackRock	PNC Bank
Goldman Sachs	State Street Global Advisors
HG Capital	Bank of New York Mellon
Livingbridge (Formerly ISIS)	Lloyds Banking Group
SL Capital	State Street Global Advisors, Deutsche Bank & JP Morgan
Capital Dynamics	Bank of America
Pantheon	State Street Bank & Trust Co. NA New York

Note 24 : Actuarial statement for 2017/18 - funding arrangements

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

Description of Funding Policy

The funding policy is set out in the Administering Authority's Funding Strategy Statement (FSS), approved March 2017. In summary, the key funding principles are as follows:

- 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 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 around a 66% chance that the Fund will return to full funding over 20 years.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 62 of the Local Government Pension Scheme Regulations 2013 was as at 31 March 2016. This valuation revealed that the Fund's assets, which at 31 March 2016 were valued at £3,892 million, were sufficient to meet 83% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2016 valuation was £679 million.

Each employer had contribution requirements set at the valuation, with the aim of achieving full funding within a time horizon and probability measure as per the FSS. Individual employers' contributions for the period 1 April 2017 to 31 March 2020 were set in accordance with the Fund's funding policy as set out in its FSS.

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Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2016 valuation report.

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 2016 valuation were as follows:

Financial assumptions	31 March 2016
Discount rate	4.2%
Salary increase assumption	2.4%
Benefit increase assumption (CPI)	2.1%

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the Fund's VitaCurves with improvements in line with the CMI 2013 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 as follows:

	Males	Females
Current Pensioners	22.5 years	24.6 years
Future Pensioners*	24.1 years	26.4 years

*Aged 45 at the 2016 Valuation.

Copies of the 2016 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

Experience over the period since 31 March 2016

Since the last formal valuation, the Fund has achieved strong asset returns, particularly during 2016/17. This will have improved the funding position at 31 March 2018.

The next actuarial valuation will be carried out as at 31 March 2019. The Funding Strategy Statement will also be reviewed at that time.

Barry McKay FFA
For and on behalf of Hymans Robertson LLP
10 May 20184 September 2018
Hymans Robertson LLP20 Waterloo Street,
Glasgow, G2 6DB

Note 25: Actuarial present value of future retirement benefits

CIPFA's Code of Practice on Local Authority Accounting 2017/18 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. I have been instructed by the Administering Authority to provide the necessary information for the Surrey Pension Fund ("the Fund").

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 the pension fund accounts:

- showing the figure in the Net Assets 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 actuarial 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 Fund's funding assumptions.

Present value of promised retirement benefits

Year ended	31/03/2018	31/03/2017
Active members (£m)	2,559	2,335
Deferred members (£m)	1,359	1,370
Pensioners (£m)	1,921	2,005
	5,839	**5,710**

The promised retirement benefits at 31 March 2018 have been projected using a roll forward approximation from the latest formal funding valuation as 31 March 2016. The approximation involved in the roll forward model means that the split of benefits between the three classes of member may not be reliable. However, I am satisfied that the total figure is a reasonable estimate of the actuarial present value of benefit promises.

The above figures include both vested and non-vested benefits, although the latter is assumed to have a negligible value. Further, I have not made any allowance for unfunded benefits.

It should be noted the above figures are appropriate for the Administering Authority only for preparation of the pension fund accounts. 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 and are different as at 31 March 2018 and 31 March 2017. I estimate that the impact of the change in financial assumptions to 31 March 2018 is to decrease the actuarial present value by £112m. There is no impact from any change in the demographic and longevity assumptions because they are identical to the previous period.

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Financial assumptions

Year ended (% p.a.)	31 March 2018	31 March 2017
Pension Increase Rate	2.4%	2.4%
Salary Increase Rate	2.7%	2.7%
Discount Rate	2.7%	2.6%

Longevity assumptions

Life expectancy is based on the Fund's VitaCurves with improvements in line with the CMI 2013 model, assuming the current rate of improvements has reached a peak and will converge to a long term rate of 1.25% p.a.. Based on these assumptions, the average future life expectancies at age 65 are summarised below:

	Males	Females
Current pensioners	22.5 Years	24.6 Years
Future pensioners (assumed to be aged 45 at the latest formal valuation)	24.1 Years	26.4 Years

Please note that the longevity assumptions have not changed since the previous IAS26 disclosure for the Fund.

Commutation assumptions

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.

Sensitivity Analysis

CIPFA guidance requires the disclosure of the sensitivity of the results to the methods and assumptions used. The sensitivities regarding the principal assumptions used to measure the liabilities are set out below:

Sensitivity to the assumptions for the year ended 31 March 2018	Approximate % increase to liabilities	Approximate monetary amount (£m)
0.5% p.a. increase in the Pension Increase Rate	8%	474
0.5% p.a. increase in the Salary Increase Rate	1%	76
0.5% p.a. decrease in the Real Discount Rate	10%	582

The principal demographic assumption is the longevity assumption. For sensitivity purposes, I estimate that a 1 year increase in life expectancy would approximately increase the liabilities by around 3-5%.

Professional notes

This paper accompanies my covering report titled ‘Actuarial Valuation as at 31 March 2018 for accounting purposes’. 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.

Anne Cranston AFA (For and on behalf of Hymans Robertson LLP)

10 May 2018

Note 26: Additional Voluntary Contributions

Market Value 2016/17 £000	Position	Market Value 2017/18 £000
12,401	Prudential	13,621
12,401		**13,621**

Additional Voluntary Contributions, net of returned payments, of £2.8million were paid directly to Prudential during the year (£2.7million during 2016/17).

Note 27: Investment Strategy Statement

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

Note 28: Annual report

The Surrey Pension Fund Annual Report 2017/2018 provides further details on the management, investment performance and governance of the Fund.

12 Scheme Advisory Committee Statistics

Financial Performance and Forecast:

	2017/18 Budget £000	2017/18 Actuals £000	2017/18 Variance £000	2018/19 Budget £000
Income				
Employers contributions	156,274	140,163	-16,111	145,067
Members contributions	38,667	38,121	-546	38,693
Total contributions	**194,941**	**178,284**	**-16,657**	**183,760**
Transfers in	**6,360**	**12,881**	**6,521**	**8,416**
Investment income	**61,062**	**65,751**	**4,132**	**77,691**
Total income	**249,038**	**256,916**	**-6,004**	**269,867**
Expenditure				
Pensions	-118,445	-119,064	-619	-127,825
Commutation and lump sum retirement benefits	-17,500	-21,606	-4,106	-19,300
Other benefits	-2,300	-3,476	-1,176	-3,732
Total benefits	**-138,245**	**-144,146**	**-5,901**	**-150,857**
Leavers	**-6,970**	**-9,527**	**-2,557**	**-7,661**
Administrative expenses	**-1,275**	**-1,626**	**-351**	**-1,467**
Oversight and governance costs	**-728**	**-721**	**-7**	**-1,006**
Investment expenses	**-14,076**	**-11,502**	**2,574**	**-17,690**
Taxes on income	**-1,171**	**-1,032**	**139**	**-1,476**
Total expenditure	**-162,465**	**-168,554**	**6,089**	**-180,157**
Net income	**100,455**	**88,362**	**-12,093**	**89,710**
Change in market value	**76,899**	**98,662**	**21,763**	**80,601**
Net Asset Value	**4,046,214**	**4,055,883**	**9,669**	**4,226,194**

The most significant variances between budget and actuals for 2017/18 financial year were related to employer contributions, transfers into the fund, investment management expenses and the change in market value of investments.

Investment management expenses incurred was below forecast, weaker investment performance for the year led to a reduction of performance fees.

Three Year Forecast:

	2018/19 Budget £000	2019/20 Budget £000	2020/21 Budget £000	2018/21 Budget £000
Income				
Contributions	183,760	187,020	188,144	**558,924**
Transfers in	8,416	8,416	8,416	**25,247**
Investment income	77,691	78,407	79,120	**235,218**
Total income	**269,867**	**273,843**	**275,679**	**819,388**
Expenditure				
Benefits	150,857	159,538	169,159	**479,554**
Transfer out	7,661	7,661	7,661	**22,983**
Management expenses	21,639	23,309	23,969	**68,917**
Total expenditure	**180,157**	**190,509**	**200,788**	**571,454**
Net income	**89,710**	**83,334**	**74,890**	**247,934**

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Investment Assets and Income

Investment Assets	UK	Non UK	Global	Total
	£m	£m	£m	£m
Equities	606	1,808		2,414
Bonds	396	205		601
Property	280	42		322
Alternatives	23	133	394	550
Cash and cash equivalent			81	81
Other			62	62
Total	**1,305**	**2,188**	**537**	**4,030**

Investment Income	UK	Non UK	Global	Total
	£000	£000	£000	£000
Equities	25,639	11,260		36,899
Bonds	3,667	7,469		11,136
Property	7,546	1,516		9,062
Alternatives	1,057	1,258	1,052	3,367
Cash and cash equivalent			5,287	5,287
Other				
Total	**37,909**	**21,503**	**6,339**	**65,751**

Asset Allocation Movement

	Asset Allocation Target	Actual Allocation 31 March 2017	Actual Allocation 31 March 2018	Movement in Year
Fixed interest securities	15.20%	10.00%	9.80%	-0.20%
Index linked securities	3.80%	5.20%	5.10%	-0.10%
Equities	59.80%	59.50%	59.90%	+0.40%
Property unit trusts	6.70%	7.20%	8.00%	+0.80%
Diversified growth	9.50%	10.10%	9.80%	-0.30%
Private equity	5.00%	3.80%	3.90%	+0.10%
Cash and other	0.00%	4.20%	3.50%	-0.70%
Total	**100.00%**	**100.00%**	**100.00%**	

Membership and Employer Statistics

	31 March 2012	31 March 2013	31 March 2014	31 March 2015	31 March 2016	31 March 2017	31 March 2018
Contributory Employees	29,120	30,023	32,530	32,851	34,072	34,298	35,802
Pensioners and Dependants	19,664	20,572	21,598	22,481	23,197	24,025	25,135
Deferred Pensions	26,583	28,256	30,639	33,833	34,158	41,573	45,079
Total	**75,367**	**78,851**	**84,767**	**89,165**	**91,427**	**99,896**	**106,016**

A table of the active employers with employee and employer contributions made during the year is shown overleaf.

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Contacts

Benefits and Contributions

Enquiries should be directed in writing to Pension Services at the following address:

Pensions Unit
Room 243
Kingston Upon Thames
Surrey KT1 2EB
Telephone: 020 8541 9289 or 9292
E Mail: pensions@surreycc.gov.uk
Fax: 020 8541 9287

Accounts and Investments

Information regarding the accounts and investments can be obtained from The Pension Fund and Treasury Manager on 020 8541 9894.

Pension Scheme Regulations

1997 Regulations S.I. 1997/1612
Copies may be obtained from:

The Stationery Office Ltd
2nd Floor, St Crispins
Duke Street
Norwich
NR3 1PD

Website:
www.opsi.gov.uk/si/si1997/19971612.htm

Useful Addresses

Occupational Pensions
Board

PO Box 1NN
Newcastle upon Tyne
NE99 1NN
Tel: 0191 225 6316

The Pensions Advisory Service (TPAS)
11 Belgrave Road
London
SW1V 1RB

Tel: 0845 601 2923
Email:enquiries@pensionsadvisoryservice.org.uk

Pensions Ombudsman
11 Belgrave Road
London
SW1V 1RB

Tel: 0207 630 2200
Email:enquiries@pensions-ombudson.org.uk

Employee and Employer Guides

The Department for Community and Local Government has produced guides to the Pension Scheme Regulations. These are available on request from Pension Services.

National Website
www.lgps.org.uk

Glossary of Terms

Active Management
A style of management where the fund manager aims to outperform a benchmark **by superior** asset allocation**, market timing or** stock selection **(or a combination of these). Compare with** passive management

Actuary
An independent consultant who advises the County Council on the financial position of the Fund. See **actuarial valuation.**

Actuarial Valuation
This is an assessment done by an **actuary**, usually every three years. The actuary will work out how much money needs to be put into a pension fund to make sure pensions can be paid in the future.

Additional Voluntary Contribution (AVC)
An option available to individuals to secure additional pensions benefits by making regular payments in addition to the 5.5%-7.5% of basic earnings payable.

Admitted Bodies
Employers whose staff can become members of the Fund by virtue of an admission agreement made between the administering authority and the employer.

Asset Allocation
The apportionment of a fund's assets between asset classes and/or world markets. The long-term strategic asset allocation of a fund will reflect the fund's investment objectives. In the short term, the fund manager can aim to add value through **tactical asset allocation** decisions.

Benchmark
A yardstick against which the investment policy or performance of a fund manager can be compared. The Surrey Fund's benchmark is customised, meaning that it is tailored to the Fund's **liability profile**.

Bond
A debt investment with which the investor loans money to an entity (company or government) that borrows the funds for a defined period of time at a specified interest rate.

Book cost
The value of an asset as it appears on a balance sheet, equivalent to how much was paid for the asset (less liabilities due). Book cost often differs substantially from **market value**.

Broker
An individual or firm that charges a fee or commission for executing buy and sell orders submitted by an investor.

Commission
A service charge assessed by an agent in return for arranging the purchase or sale of a security or real estate. The commission must be fair and reasonable, considering all the relevant factors of the transaction. (Underwriting commission)

Corporate Bond
A debt security issued by a corporation, as opposed to those issued by the government.

Corporate Governance
The system by which companies are run, and the means by which they are responsible to their shareholders, employees and other stakeholders.

Creditors
Amounts owed by the pension fund.

Custody
Safe-keeping of securities by a financial institution. The custodian keeps a record of the client's investments and may also collect income, process tax reclaims and provide other services such as performance measurement.

Debtors
Amounts owed to the pension fund.

Derivative
Used to describe a specialist financial instrument such as **options** or **futures contracts**. Financial instruments are agreements to buy or sell something, under terms laid out in a contract.

Diversification
A risk management technique that mixes a wide variety of investments within a portfolio. It is designed to minimize the impact of any one security on overall portfolio performance.

Dividend
Distribution of a portion of a company's earnings, decided by the board of directors, to a class of its shareholders. The amount of a dividend is quoted in the amount each share receives or in other words dividends per share.

Dividend Yield
An indication of the income generated by a share, calculated as Annual Dividend per Share/Price per Share

Emerging Markets
There are about 80 stock markets around the world of which 22 markets are generally considered to be mature. The rest are classified as emerging markets.

Equity
Stock or any other security representing an ownership interest.

Ex-dividend
Purchase of shares without entitlement to current dividends. This entitlement remains with the seller of the shares.

Final Salary Scheme
An employer pension scheme, the benefits of which are linked to length of service and the final salary of the member (also known as defined benefit).

Fixed interest
A loan with an interest rate that will remain at a predetermined rate for the entire term of the loan. See bond.

FTSE All-Share
An arithmetically weighted index of leading UK shares (by market capitalisation) listed on the London Stock Exchange (LSE). The FTSE 100 Index covers only the largest 100 companies.

Funding Level
A comparison of a scheme's assets and liabilities.

Futures Contract
A contract to buy goods at a fixed price and on a particular date in the future. Both the buyer and

seller must follow the contract by law.

Gilts
The familiar name given to sterling, marketable securities (or bonds) issued by the British Government.

Hedge
Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such as a **futures contract**.

Index Linked

A **bond** which pays a **coupon** that varies according to some underlying index, usually the Consumer Price Index.

LGPS
Local Government Pension Scheme.

LSE
London Stock Exchange

Mandate
The agreement between a client and investment manager laying down how the portfolio is to be managed, including performance targets.

Market Value

A security's last reported sale price (if on an exchange) i.e. the price as determined dynamically by buyers and sellers in an open market. Also called market price.

Option
The name for a contract where somebody pays a sum of money for the right to buy or sell goods at a fixed price by a particular date in the future. However, the goods do not have to be bought or sold.

Passive Management
A style of fund management that aims to construct a portfolio to provide the same return as that of a chosen index. Compare with **active management**.

Pension Fund
A fund established by an employer to facilitate and organise the investment of employees' retirement funds contributed by the employer and employees. The **pension fund** is a common asset pool meant to generate stable growth over the long term, and provide pensions for employees when they reach the end of their working years and commence retirement.

Private Equity
When equity capital is made available to companies or investors, but not quoted on a stock market. The funds raised through private equity can be used to develop new products and technologies, to expand working capital, to make acquisitions, or to strengthen a company's balance sheet. Also known as **development capital**.

Property Unit Trusts
Pooled investment vehicles that enable investors to hold a stake in a diversified portfolio of properties.

Return
Synonymous with profit, be it income received, capital gain or income and capital gain in combination. Usually expressed as a percentage of the nominal value of the asset.

Risk
The likelihood of performance deviating significantly from the average. The wider the spread of investment in an investment sector or across investment sectors, i.e. the greater the diversification, the lower the risk.

Scheme Employers
Local authorities and other similar bodies whose staff automatically qualify to become members of the pension fund.

Security
An investment instrument, other than an insurance policy or fixed annuity, issued by a corporation, government, or other organisation, which offers evidence of debt or equity.

Socially Responsible Investment (SRI)
Investments or funds containing stock in companies whose activities are considered ethical.

Specialist Manager
A fund management arrangement whereby a number of different managers each concentrate on a different asset class. A specialist fund manager is concerned primarily with **stock selection** within the specialist asset class. **Asset allocation** decisions are made by the investment committee, their consultant or by a specialist tactical asset allocation manager (or combination of the three).

Stock
A type of security that signifies ownership in a corporation and represents a claim on part of the corporation's assets and earnings. Also known as shares or **equity.**

Stock Selection
The process of deciding which stocks to buy within an asset class.

Tracking Error
An unplanned divergence between the price behaviour of an underlying stock or portfolio and the price behaviour of a benchmark. Reflects how closely the make-up of a portfolio matches the make-up of the index that it is tracking.

Transaction Costs

Those costs associated with managing a portfolio, notably brokerage costs and taxes.

Transfer Value
The amount transferred to/from another pension fund should a member change employment. The amount transferred relates to the current value of past contributions.

Transition
To move from one set of investment managers to another.

Underwriting
The process by which investment bankers raise investment capital from investors on behalf of corporations and governments that are issuing securities (both equity and debt).

Unit Trust
A pooled fund in which investors can buy and sell units on an ongoing basis.

Unlisted Security
A security which is not traded on an **exchange.**

Unrealised Gains/(losses)
The increase/(decrease) at year-end in the market value of investments held by the fund since the date of their purchase.

Yield
The rate of income generated from a stock in the form of dividends, or the effective rate of interest paid on a bond, calculated by the coupon rate divided by the bond's market price. Furthermore, for any investment, yield is the annual rate of return expressed as a percentage.

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Grant Thornton

Audit Findings

Year ending 31 March 2018

Surrey Pension Fund

July 2018

Contents

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Headlines

Introduction

This table summarises the key issues arising from the statutory audit of Surrey Pension Fund ('the Pension Fund') and the preparation of the Pension Fund's financial statements for the year ended 31 March 2018 for those charged with governance.

Financial Statements	Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion: • the Pension Fund's financial statements give a true and fair view of the financial position of the Pension Fund and its income and expenditure for the year, and have been properly prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting;	Our audit work was completed on site during June and July. Our findings are summarised in this report. We have not identified any adjustments to the financial statements that have resulted in a change to the Fund's reported financial position. Audit adjustments which relate to disclosures and classification errors are detailed in Appendix B. We have also raised recommendations for management as a result of our audit work in Appendix A. Subject to outstanding queries being resolved, we anticipate issuing an unqualified audit opinion following the Audit & Governance Committee meeting on 26 July 2018. These outstanding items include: - final internal quality review - receipt of the management representation letter; and - review of the final set of financial statements.

Acknowledgements
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.

Summary

Overview of the scope of our audit

- This Audit Findings presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management.
- As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

Audit approach

Our audit approach was based on a thorough understanding of the Pension Fund's business and is risk based, and in particular included:

- An evaluation of the Pension Fund's internal controls environment, including its IT systems and controls;
- We brought forward controls testing of the scheme contributions, and carried out controls testing of member data and the benefit payment systems; and
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks

Conclusion

We have substantially completed our audit of your financial statements and subject to outstanding queries being resolved, we anticipate issuing an unqualified audit opinion following the Audit & Governance Committee meeting on 26 July 2018.

Our approach to materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

Our planning materiality was based on 1% of your net assets in the 2016/17 financial statements.

Our assessment of the value of materiality has been adjusted to reflect 1% of your net assets in the draft financial statements 2017/18. We detail in the table below our assessment of materiality for Surrey Pension Fund.

	Amount (£)
Materiality for the financial statements	38,689,000
Performance materiality	23,213,000
Trivial matters	1,934,450

Significant audit risks

	Risks identified in our Audit Plan	Commentary
1	**Improper revenue recognition** Under ISA 240 (UK) there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.	**Auditor commentary** Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Fund, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: – there is little incentive to manipulate revenue recognition – opportunities to manipulate revenue recognition are very limited – the culture and ethical frameworks of local authorities, including Surrey County Council as the Administering Authority of Surrey Pension Fund, mean that all forms of fraud are seen as unacceptable Therefore we do not consider this to be a significant risk for Surrey Pension Fund.
2	**Management override of controls** Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. We identified management override of controls as a risk requiring special audit consideration.	**Auditor commentary** • Summary of work performed and audit findings: – gained an understanding of the accounting estimates, judgements applied and decisions made by management and considered their reasonableness – obtained a full listing of journal entries, identified and tested unusual journal entries for appropriateness – evaluated the rationale for any changes in accounting policies or significant unusual transactions Our audit work has not identified any issues in respect of management override of controls.

Significant audit risks

Risks identified in our Audit Plan	Commentary
3 The valuation of Level 3 investments is incorrect **Under ISA 315 significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.** **We identified the valuation of level 3 investments as a risk requiring special audit consideration.**	**Auditor commentary** Summary of work performed and audit findings: – gained an understanding of the Fund's process for valuing level 3 investments and evaluated the design of the associated controls – reviewed the nature and basis of estimated values and considered what assurance management has over the year end valuations provided for these types of investments – for a sample of investments, tested the valuation by obtaining and reviewing the audited accounts, (where available) at the latest date for individual investments and agreeing these to the fund manager reports at that date. Reconciled those values to the values at 31 March 2017 with reference to known movements in the intervening period. Our audit work has not identified any issues in respect of the valuation of Level 3 investments.

Reasonably possible audit risks

Risks identified in our Audit Plan	Commentary
4 **Contributions** Contributions from employers and employees' represents a significant percentage of the Fund's revenue. We therefore identified occurrence and accuracy of contributions as a risk requiring particular audit attention	**Auditor commentary** Summary of work performed and audit findings: – evaluated the Fund's accounting policy for recognition of contributions for appropriateness; – gained an understanding of the Fund's system for accounting for contribution income and evaluated the design of the associated controls; – performed a trend analysis of scheme contributions across the year to assess the completeness of scheme contributions – tested a sample of contributions to source data to gain assurance over their accuracy and occurrence; – rationalised contributions received with reference to changes in member body payrolls and the number of contributing pensioners to ensure that any unusual trends are satisfactorily explained. Our audit work has not identified any issues in respect of contributions
5 **Pension Benefits Payable** Pension benefits payable represents a significant percentage of the Fund's expenditure. We identified completeness of pension benefits payable as a risk requiring particular audit attention:	**Auditor commentary** Summary of work performed and audit findings: – evaluated the Fund's accounting policy for recognition of pension benefits expenditure for appropriateness; – gained an understanding of the Fund's system for accounting for pension benefits expenditure and evaluated the design of the associated controls; – performed a trend analysis of benefit payments across the year to assess the completeness of benefit payments – tested a sample of individual pensions in payment by reference to member files; – rationalised pensions paid with reference to changes in pensioner numbers and increases applied in year to ensure that any unusual trends are satisfactorily explained. Our audit work has not identified any issues in respect of pension benefits payable

Reasonably possible audit risks

Risks identified in our Audit Plan	Commentary
6 The valuation of Level 2 investments is incorrect While level 2 investments do not carry the same level of inherent risks associated with level 3 investments, there is still an element of judgement involved in their valuation as their very nature is such that they cannot be valued directly. We identified valuation of level 2 investments as a risk requiring particular audit attention.	**Auditor commentary** Summary of work performed and audit findings: – gained an understanding of the Fund's process for valuing Level 2 investments and evaluated the design of the associated controls. – reviewed the reconciliation of information provided by the fund managers, the custodian and the Pension Funds' own records and sought explanations for any variances – where deemed necessary for additional assurance, we tested a sample of level 2 investment prices from the custodian / fund manager to independently obtained prices. Our audit work has not identified any issues in respect of the valuation of Level 2 investments

Accounting policies

Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	The financial statements include policies for recognition of the following: • Investment income • Contribution income • Transfers into the scheme Revenue for the first two categories is recognised on an accruals basis, whilst the third category is recognised on a cash basis, with the exception of bulk transfers, which are accounted for on an accruals basis in accordance with the terms of the transfer agreement.	• Review of your polices for revenue recognition confirms they are in line with the CIPFA Code of Practice and cover all the expected areas in accordance with the Fund's activates. • Our testing has confirmed that these policies have been correctly and consistently applied.	●
Judgements and estimates	• Key estimates and judgements include: – Valuation of level 3 investments – The assumptions made by your actuary	We identified the valuation of level 3 investments as a significant risks and have reported to you earlier in this report the work we have carried out to reduce the risk of a material misstatement in the financial statements to an acceptable level. We tested the assumptions made by your actuary by using our own auditor expert and following up local areas which were not covered by this review, such as completeness of information sent to your actuary. We are satisfied that the assumptions made by your actuary are reasonable.	●
Other critical policies		We have reviewed the Pension Fund's policies against the requirements of the CIPFA Code of Practice. The Pension Fund's accounting policies are appropriate and consistent with previous years.	●

Assessment
- ● Marginal accounting policy which could potentially be open to challenge by regulators
- ● Accounting policy appropriate but scope for improved disclosure
- ● Accounting policy appropriate and disclosures sufficient

Other communication requirements

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

	Issue	Commentary
1	**Matters in relation to fraud**	• We have previously discussed the risk of fraud with management and the Chair of the Audit & Governance Committee. We have not been made aware of any material fraud in the period and no material fraud has been identified during the course of our audit procedures.
2	**Matters in relation to related parties**	• We are not aware of any related parties or related party transactions which have not been disclosed
3	**Matters in relation to laws and regulations**	• You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
4	**Written representations**	• A standard letter of representation has been requested from the Pension Fund
5	**Confirmation requests from third parties**	• We requested permission from management to send a confirmation request to HSBC. This permission was granted and the requests were sent and returned with positive confirmation.
6	**Disclosures**	• Our review found no material omissions in the financial statements
7	**Significant difficulties**	• Draft financial statements provided for audit and uploaded to Surrey County Council's website were not of sufficient quality, a significant number of figures were rolled forward form the prior year and had not been updated for 2017/18. • The original working papers provided to the audit team did not agree to the financial statements and key working papers were missing form the requested list. • Delay in receiving key supporting information, for example the trial balance, full journal listing and payroll information • Delays in the pensions admin team responding to audit queries, including delays in receiving the MSATEMP report which details the pensioners numbers that are included in the accounts. • We were initially told there were no new fund managers in the year, however upon completing work in the investments section we discovered there was a new private equity manager (Pantheon), which delayed the sending and receipt of the confirmation letter. • There were six versions of the accounts since draft due to the number of changes required.
8	**Matters on which we report by exception**	• We are required to give a separate opinion for the Pension Fund Annual Report on whether the financial statements included therein are consistent with the audited financial statements. Due to statutory deadlines the Pension Fund Annual Report is not required to be published until the 1st December 2018 and therefore this report has not yet been produced. We have therefore not given this separate opinion at this time and are unable to certify completion of the audit of the administering authority until this work has been completed.

Independence and ethics

Independence and ethics

- We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Financial Reporting Council's Ethical Standard and confirm that we, as a firm, and each covered person, are independent and are able to express an objective opinion on the financial statements

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in December 2017 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

Details of fees charged are detailed in Appendix C

Audit and Non-audit services

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Pension Fund. No non-audit services were identified.

Action plan

We have identified two recommendations for the Pension Fund as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2018/19 audit. 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.

	Assessment	Issue and risk	Recommendations
1	●	• New starter members - Not all members received letters to inform them of their enrolment to their pension scheme. This has been an issue since approximately July 2017. This process is to be started again due to new processes and procedures being in place.	• Ensure new starters receive notification of their enrolment into the scheme **Management response** • The administration team is recruiting additional pensions administrators who would deal with this area of work, this would mean that backlogs would not build up and new scheme joiners would receive their notifications within the prescribed disclosure timeframes. • The new Customer and Service Improvement Officer is currently reviewing the New Starter process to ensure any waste is removed and the result is a more efficient process. This in turn will improve the service we provide to new scheme joiners.
2	●	• Leavers (members) - only 10 of the 25 leavers sampled had the expected documents (equite form and LG5.24 form) attached to their profiles. Therefore 15 people had no clear audit trail as to why they had been set as a leaver on the system.	• There should be a clear protocol to be followed by pension operations colleagues to ensure there is a clear audit trails as to why a member has been set as a leaver **Management response** • The administration team is recruiting additional pensions administrators who would deal with this area of work, this would mean that administrators have the capacity to scan paperwork to member records at the time of processing the cases. • The administration team also trialling iConnect software system shortly which will allow scheme employers to upload data directly to the Altair system therefore removing the need to send forms that require scanning to member records.

Controls
- High – Significant effect on control system
- Medium – Effect on control system
- Low – Best practice

Audit Adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Impact of adjusted misstatements

There were no misstatements which impact on the key statements and the reported net expenditure for the year.

Misclassification and disclosure changes

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

Disclosure omission	Detail	Adjusted?
Fund account: Change in market value of investments	Prior year adjustment had not been correctly recorded in the change in market value of investment line in the pension fund account.	✓
Note 13: Current liabilities	On version 5 of accounts, the analysis of current liabilities was incorrectly stated in the note.	✓
Note 17a 2017 disclosures	2017 note did not agree to prior year signed accounts, has since been updated and agrees.	✓
Note 17d	Market Value of Darwin investment was not correctly updated for the prior year audit adjustment in the note.	✓
Note 18a: Classification of financial instruments	Bank figures as at 31 March did not agree to bank figure in the note; note was incorrect.	✓
Note 18b: Net gains and losses on financial instruments	Financial Assets were incorrectly classified as liabilities in the draft note.	✓
Note 18c	2017 split of level 1, 2 and 3 investments did not agree to prior year signed accounts.	✓
Note 19: Outstanding commitment	The value of 207/18 outstanding commitments was incorrectly stated in the note.	✓

Fees

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

Audit Fees

	Proposed fee	Final fee
Pension Fund Audit	27,105	TBC
Total audit fees (excluding VAT)	**£27,105**	**£TBC**

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA). The final fee is pending agreement of fee variations by PSAA.

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SURREY
COUNTY COUNCIL

Our Ref
Your Ref: SLGPS LoR 2017-18

Grant Thornton UK LLP
30 Finsbury Square
London
EC2A 1AG

30 July 2018

Dear Sirs

Surrey pension Fund
Financial Statements for the year ended 31 March 2018

This representation letter is provided in connection with the audit of the financial statements of Surrey Pension Fund ('the Fund) for the year ended 31 March 2018 for the purpose of expressing an opinion as to whether the Fund financial statements are presented fairly, in all material respects in accordance with International Financial Reporting Standards and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 and applicable law.

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

Financial Statements

i We have fulfilled our responsibilities for the preparation of the Fund's financial statements in accordance with International Financial Reporting Standards and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 ("the Code"); in particular the financial statements are fairly presented in accordance therewith.

ii We have complied with the requirements of all statutory directions affecting the Fund and these matters have been appropriately reflected and disclosed in the financial statements.

iii The Fund has complied with all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of any regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

iv We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud.

v We acknowledge our responsibilities for making the accounting estimates included in the financial statements. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable. Where it was necessary to choose between estimation techniques that comply with the Code, we selected the estimation technique considered to be the most appropriate to the Fund's particular circumstances for the purpose of giving a true and fair view. Those estimates reflect our judgement based on our knowledge and experience about past and current events and are also based on our assumptions about conditions we expect to exist and courses of action we expect to take.

vi We are satisfied that the material judgements used in the preparation of the financial statements are soundly based, in accordance with the Code and adequately disclosed in the financial statements. There are no other material judgements that need to be disclosed.

vii Except as disclosed in the financial statements:

a there are no unrecorded liabilities, actual or contingent

b none of the assets of the Council has been assigned, pledged or mortgaged

c there are no material prior year charges or credits, nor exceptional or non-recurring items requiring separate disclosure.

viii Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of International Financial Reporting Standards and the Code.

ix All events subsequent to the date of the financial statements and for which International Financial Reporting Standards and the Code require adjustment or disclosure have been adjusted or disclosed.

x We have considered the misclassification and disclosures changes schedules included in your Audit Findings Report. The financial statements have been amended for these misclassifications and disclosure changes and are free of material misstatements, including omissions.

xi Actual or possible litigation and claims have been accounted for and disclosed in accordance with the requirements of International Financial Reporting Standards.

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

xiii 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.

Information Provided

xiv We have provided you with:

a. access to all information of which we are aware that is relevant to the preparation of the Fund 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 within the Fund from whom you determined it necessary to obtain audit evidence.

xv We have communicated to you all deficiencies in internal control of which management is aware.

SURREY COUNTY COUNCIL

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

xvii 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.

xviii We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the Fund and involves:

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.

xix We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, analysts, regulators or others.

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

xxi We have drawn to your attention all correspondence and notes of meetings with regulators.

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

xxiii 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.

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

Approval

The approval of this letter of representation was minuted by the Audit and Governance Committee at its meeting on 26 July 2018.

Yours faithfully

Name.....

Signed.....

Position.....

Date.....

12

Name KEVIN KILBURN

Signed

Position Deputy CFO and Interim section 151 officer

Date 30/07/2018

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

SURREY COUNTY COUNCIL

PENSION FUND COMMITTEE

DATE: **14 SEPTEMBER 2018**

LEAD OFFICER: **KEVIN KILBURN, ACTING SECTION 151 OFFICER**

SUBJECT: **LOCAL BOARD REPORT**

SUMMARY OF ISSUE:

This report is a summary of administration and governance issues reviewed by the Local Pension Board at its meeting of 25 July 2018 that need to be brought to the attention of the Pension Fund Committee.

RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Considers the recommendations from the Local Pension Board with regard to the Administration Performance Report.

2. Provides an update to the Local Pension Board on the current position regarding pension member representation in the BCPP governance structure.

3. Concludes whether there are any reviews as to the compliance of particular cases, projects or processes that the Local Pension Board should undertake.

REASON FOR RECOMMENDATIONS:

In order to achieve best possible performance alongside optimal risk management.

LOCAL PENSION BOARD MEETINGS

1. The most recent Local Board meeting was on 25 July 2018 (minutes of this meeting are included as Annex 1).

2. The next Local Board meeting is scheduled for 23 October 2018

THE ADMINISTRATION PERFORMANCE REPORT (APR)

Background

3. At the Pension Fund Committee meeting of 15 September 2017, the Pension Fund Committee (Committee) approved a new Administration Performance Report (APR) to replace the existing Key Performance Indicators (KPR) from quarter 3 of 2017/18.

4. At the Pension Fund Committee meeting of 10 November 2017, the Committee agreed that future administrations statistics reports be presented to the Committee after the full APR has been scrutinised by the Local Board. To avoid unnecessary duplication it was agreed that this report be in the form of a summarised report of the APR and will include any relevant Board recommendations.

APR Summarised report

5. The APR measures member and employer caseloads against performance levels, with red, amber and green ratings. A green rating indicates the tolerable performance level has been met. An amber rating indicates that performance levels were below tolerable by 5% or less. A red rating indicates that performance levels were below tolerable by more than 5%.

6. It was noted that is important to take the context into consideration when interpreting this quarter's figures as a number of key posts have been replaced and it is, perhaps, understandable that the figures have suffered.

7. Of the 26 pension administration case load details sub-categories, there were Improvements in three areas and a decline in thirteen. The deferred benefits (increased to 63%), refunds (fallen to 51%), death dependants' benefits initial (fallen to 80%), death on pension initial (fallen to 63%) were all below the tolerable level (red) and death dependants' benefits complete (fallen to 85%) was on the cusp (amber).

8. Following the report on robotics at the last board meeting members asked officers when robotic process automation was expected to go live. The Pensions Service Delivery Manager informed the Board that the automated solution was a work in progress and assured members an update on the development could be provided at a later date.

9. The Pension Service Delivery Manager commented that it was difficult for her to comment on past performance as she had only been here for such a short amount of time; however, she drew attention to the various initiatives they are implementing in order to improve the service offered to customers (members and employers).She drew attention to the following issues;

- Lack of resource – The Lead Pensions Manager is working on a resource plan and has identified where our resource gaps are .They are currently working with HR and Finance to recruit staff to fill these gaps so that they have a full complement of staff.

- Employer Data concerns – the Pension Section has issues with the data provided by some scheme employers which it is addressing.

Local Board recommendations

10. After review at its meeting of 18 January 2018, the Local Board recommended there be a further review of the appropriateness of current "performance aspiration" and "tolerable" performance standard; however, officers are of the view that 100% is the only appropriate aspiration.

11. The Investments Risk Register; in addition to the recommendation to change four of the first five risks on the risk register officers identified a number of, mostly minor, improvements to other areas of the register. The Board noted that the new risk of change in Section 151 Officer was added to the register.

FURTHER ADMINISTRATION AND GOVERNANCE ITEMS

Administration items

12. Commissioning training for the Local Pension Board was discussed at March's meeting and it was advised that the LGA Trustee training modules have been reissued and dedicated investment training had been offered by Goldman Sachs and potential dates had been circulated to members.

13. The Board expressed its concern about the number of employers that had not submitted discretions policies during March's meeting and officers reported that an internal exercise to address this issue would be launched in August 2018. The project will be structured so as to ensure that employers who fail to respond are monitored, reminded and offered assistance. There will also be a parallel exercise to offer employers support in hearing appeals under the internal disputes resolution procedure (IDRP) which will be rolled out simultaneously.

14. Officers reported the parameters that the Pension Section sets for identifying members who are at risk of breaching the annual / lifetime allowance and how they monitor members who are in danger of breaching the limits and incurring a tax charge.

15. The Pension Service Delivery Manager advised the Board that the active member's newsletter would draw attention to the annual allowance, lifetime allowance and the 50-50 scheme. Members stressed that officers needed to identify members who opted-out due to difficulties in paying the full pension contribution and alert them to the 50-50 scheme alternative.

16. Officers provided an update report on the exercise to review and quality assure the fund's AVC provision. The Board was advised that four firms of actuaries had been asked for quotations for carrying out a review of the market place and identifying the best providers in terms of quality, service and investment performance had been approached.

17. It was noted that the guaranteed minimum pension (GMP) reconciliation exercise is close to completion and Members requested the statistics and an analysis of data which the supplier undertook to provide by the end of July 2018.

18. The Pension Service Delivery Manager informed the Board that a Customer and Service Improvement Officer had been appointed to explore and review processes in order to make them more efficient. Members raised concerns about staff turnover and were advised that there were currently six vacancies and that designations and pay grades were being reviewed in order to match the roles to the volume and distribution of the work.

19. The Pension Service Delivery Manager informed the Board that the annual data cleanse would take place in September 2018 in order to prepare for the triennial valuation in 2019.

20. The Pensions Service Delivery Manager clarified that the significant increase in cash-flow was due to some employers delaying paying over contributions / deficit contributions until the year end.

21. Pension Administration Complaints; the highest incidence of complaints was service delay (42%) followed by lack of communication (33%); however, it was noticed that these figures did not agree with the statistics reported in annex 1. The Board commended the Pension Section on the low level of complaints and the trade union representative in attendance praised the work of the help desk.

22. The Pensions Service Delivery Manager noted members' recommendation to prioritise death cases as the performance levels were below tolerable.

23. Internal disputes resolution procedure (IDRP); one stage two determination was made, one case was appealed to the Pensions Ombudsman and one determination was received from the Pensions Ombudsman (a separate case).

24. Officers reported that the Pension Section had produced a privacy statement which it had published on its website in order to comply with GDPR. It will use the August 2018 annual benefit statements to draw active and deferred members' attention to it.

25. Officers reported on the pre-valuation project plan; it was noted that the Fund actuary, Hymans Robertson, carried out the triennial valuation of the Fund's assets and liabilities. The primary and secondary rates for all employers in the

Fund were derived from this exercise. The next valuation is scheduled for 31 March 2019 (effective 1 April 2020) and the Board was presented with a draft project plan. Officers clarified that the references to 'HEAT' in the report referred to 'Hymans Employer Asset Tracker' and it was noted that the purpose of the plan was to track changes and support the production of accurate results.

Governance items

26. The Local Pension Board discussed the matter of pension member representation as observers on the Border to Coast Pensions Partnership (BCPP) Board and noted that the Scheme Advisory Board had recommended that***, "in*** *line with the UK Corporate Governance Code principle of 'comply or explain', any pool making a decision to exclude member representatives from their formal oversight structures should publish this decision and formally report the reasons to the local pension boards which the pool serves."*

27. The Local Pension Board – exclusion of the public; it was resolved that under Section 100(A) of the Local Government Act 1972, the public be excluded from meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information under the relevant paragraphs of part 1 of Schedule 12A of the Act.

CONSULTATION:

28. The Chairman of the Pension Fund Committee has been consulted on this report.

RISK MANAGEMENT AND IMPLICATIONS:

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

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

30. The performance of the Pensions Administration function does present potential financial and value for money implications to the Pension Fund. The monitoring of these implications is discussed within the report.

SECTION 151 OFFICER (DIRECTOR OF FINANCE) COMMENTARY

31. The Acting Section 151 Officer is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

LEGAL IMPLICATIONS – MONITORING OFFICER

32. A Local Pension Board is a requirement under the Public Service Pensions Act 2013. There are no legal implications or legislative requirements.

EQUALITIES AND DIVERSITY

33. The approval of the various options will not require an equality analysis, as there is no major policy, project or function being created or changed.

OTHER IMPLICATIONS

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

WHAT HAPPENS NEXT

35. The following next steps are planned: receive further reports and continue collaboration between the Pension Fund Committee and Local Pension Board.

Contact Officer:
Neil Mason, Head of Pensions

Consulted:
Pension Fund Committee Chairman.

Annexes:

Annex 1: Minutes of the Local Pension Board meeting of 25th July 2018

Annex 2: Quarter 2 APR

Annex 3. Risk Register.

Sources/background papers:

MINUTES of the meeting of the **SURREY LOCAL PENSION BOARD** held at 10.00 am on 25 July 2018 at County Hall, Penrhyn Road, Kingston upon Thames, KT1 2DW.

These minutes are subject to confirmation by the Board at its meeting on 23 October 2018.

Members:
*present

*	Paul Bundy
*	Ellwood Graham (Vice-Chairman)
*	Mr Nick Harrison (Chairman)
*	Tina Hood
*	Paresh Rajani
*	David Stewart
	Claire Williams-Morris
	Trevor Willington

32/18 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS [Item 1]

Apologies were received from Claire William-Morris and Trevor Willington.

33/18 MINUTES FROM THE PREVIOUS MEETING: 23 APRIL 2018 [Item 2]

The minutes were agreed as an accurate record of the meeting.

34/18 DECLARATIONS OF INTEREST [Item 3]

There were none.

35/18 QUESTIONS AND PETITIONS [Item 4]

The Board received no questions and petitions.

36/18 LOCAL PENSION BOARD ACTION TRACKER [Item 5]

Key points raised during the discussion:

1. The Board received a summary of responses to Freedom of Information requests provided by the Fund during the last quarter.

2. Officers provided a progress update on the Additional Voluntary Contributions (AVC) arrangement, advising members that four potential candidates were being reviewed and that officers were exploring the best options. It was agreed that the Chairman would be briefed on the recommendations for appointing one of the candidates in August and officers would report back to the Board at its next meeting in October 2018.

3. It was highlighted that employer discretions would be addressed in the communications report for quarter one.

4. It was noted that the Administration update report included management's response to the 2016/17 administration audit.

5. It was further noted that the Pension Service Delivery Manager was due to provide dates for completion of actions on the administration final management action plan would be completed.

6. Officers reported on annual and lifetime allowances detailing how the Pensions Team monitors these.

7. The Board were informed that investment training had been offered by Goldman Sachs and dates had been circulated to members to agree.

8. The Pensions Service Delivery Manager agreed to forward the link to the fundamentals programme to allow members to book training.

Actions/further information to be provided:

a) The Pensions Service Delivery Manager to provide dates for completion of the management action plan and the link to the fundamentals programme to allow members to book training.

b) Officers to brief the Chairman on AVC recommendations.

Recommendations:

The Board noted the content of this report.

37/18 LOCAL PENSION BOARD FORWARD PLAN [Item 6]

Key points raised during the discussion:

1. Members noted that one further Board meeting was scheduled for the remainder of the calendar year and suggested that the Board's forward plan be maintained on a rolling basis. It was agreed that AVC's and the GMP reconciliation would be added to the agenda for the next meeting.

Actions/ further information to be provided:

The forward plan to be updated.

Recommendations:

The Board noted the content of this report.

38/18 PENSION FUND COMMITTEE UPDATE [Item 7]

Declarations of interest:

None

Witnesses:

John Smith, Senior Advisor
Graham Ellwood, Vice-Chairman

Key points raised during the discussion:

1. It was noted that work was underway to address concerns with the administration and monitoring of members in danger of breaching the annual or lifetime allowances. The Pensions Service Delivery Manager explained that this was becoming a national issue, that there was a general lack of awareness reported in this area. To remedy this officers highlighted that the service were looking into ways to provide members' education through road shows and drop-in surgeries.The Pensions Service Delivery Manager indicated that surveys would be carried out and feedback generated from the road would could be shared with the Board.

2. The Pensions Service Delivery Manager highlighted that the active members newsletter would include information on annual/ lifetime allowances and 50/50 scheme alternatives. The Board stressed the need for officers to identify members who were opting out due to not being able to afford contributions, it was felt that members were not aware of the 50/50 scheme. To support members of the Board playing an active role, officers agreed to share newsletters in draft stage.

3. There was a discussion around investments and officers agreed to provide a brief note to explain the Pension Fund arrangement to members.

4. The Senior Advisor clarified that the cash-flow increase was a result of some employers paying deficit contributions at year end.

5. The Board were notified that the Director of Finance had left the Council on 6 July 2018 and that an interim Director had been appointed.

6. Members referred to the Pension Fund Business Plan 2017/18: Outturn report and queried why some outcomes were referenced as 'partially achieved'. Officers clarified that these outcomes were work in progress.

Actions/ further information to be provided:

a) Officers to provide the Board with a draft copy of the Active Members Newsletter for comment before its publication in August and to report back on road shows and surgeries.

b) The Board to receive a briefing note on investments explaining the Pension Fund arrangements.

13

Recommendations:

The Board noted the content of this report.

39/18 ADMINISTRATION PERFORMANCE REPORT: 1 APRIL 2018 TO 30 JUNE 2018 [Item 8]

Declarations of interest:

None

Witnesses:

Clare Chamber, Pensions Service Delivery Manager

Key points raised during the discussion:

1. Officers reported that a range of initiatives were being developed to improve the level of service to customers.

2. It was highlighted that an employer's issue log would be implemented to support the processing of employer data issues.

3. The Board noted that a recruitment process was underway to fill resource gaps in the service. The Pensions Service Delivery Manager said that a Customer & Service Improvement Officer had been recruited to review and explore options to make current processes more efficient. Members raised concerns regarding the impact of recent staff turnover and questioned how resilience could be improved. The Board were advised that six vacancies were available and that pay grades were being reviewed/converted to balance the volume of work and handling across the team.

4. The Pensions Service Delivery Manager noted members' requests to prioritise death cases as performance levels were below tolerable.

5. Members queried the robotic process automation and when the service expected to see this go live. The Pensions Service Delivery Manager informed the Board that the automated solution was a work in progress and assured members an update on the development would be provided at a later date.

Actions/ further information to be provided:

None

Recommendations:

The Board noted the content of this report. No recommendations were to be put forward to the Pension Fund Committee for their attention.

40/18 ADMINISTRATION UPDATE: 1 APRIL 2018 TO JUNE 2018 [Item 9]

Declarations of interest:

None

Witnesses:

Clare Chambers, Pensions Service Delivery Manager

Key points raised during the discussion:

1. The Pensions Service Delivery Manager introduced the report by informing members that an Annual Data Cleanse would take place in autumn 2018 in order to prepare for the next triennial Valuation due to take place in 2019. It was highlighted that the cleanse would help identify missing data and/or errors, flagging any discrepancies such as salary and member details.

General Data Protection Regulations (GDPR)

2. In accordance with new legislation regarding GDPR, it was reported that the Pension Section produced a privacy statement made available on its website. To publicise this information members would be drawn to it through annual benefit statements dispatched in August 2018.

Guaranteed Minimum Pension (GMP) Reconciliation

3. It was noted that the GMP Reconciliation process was in the final stages. Members requested statistics on the data analysis, to be provided by the supplier at the end of July 2018.

Annual Benefit Statements

4. It was reported that 11 scheme employers had yet to return their End of Year Data submission.

5. Members were informed that 23,500 annual benefit statements were to be published on the member portal and all active statements would be dispatched by 24 August 2018.

6. It was advised that the final dispatch date was purposely scheduled close to the statutory deadline (31 August 2018) to accommodate for late data.

7. The Pension Service Delivery manager agreed to share annual benefit statement templates with the Board.

8. The Board noted that Call Credit had been employed recently to review and check addresses.

Actions/further information to be provided:

The Board to receive;

a) statistics on the number of queries identified by the GMP reconciliation process.

b) annual benefit statement templates.

Recommendations:

The Board noted the content of this report and made no further recommendations.

41/18 REVIEW OF INTERNAL DISPUTE RESOLUTION CASES IN 2018/19: QUARTER ONE [Item 10]

Declarations of interest:

None

Witnesses:

John Smith, Senior Advisor

Key points raised during the discussion:

1. It was highlighted that three cases were received/resolved during quarter one (2018/19);

    I. One stage 2 determination was made in respect of an appeal received at the end of the previous quarter,
    II. One appeal to the Pensions Ombudsman was received and
    III. One determination was received from the Pensions Ombudsman relating to a separate case.

Actions/ further information to be provided:

None.

Recommendations:

The Board noted the content of this report.

42/18 CUSTOMER COMPLAINTS REPORT: QUARTER 1 [Item 11]

Declarations of interest:

None

Witnesses:

Clare Chambers, Pensions Service Delivery Manager

Key points raised during the discussion:

1. Members noted an error in the report, it was highlighted that Annex 1 showed the highest subject of complaints received was for service delay (42%) and lack of communication (33%).

2. The Board commended the low number of complaints considering the size of the membership.

3. The trade union representative in attendance also commended the work of the Helpdesk, having received positive feedback in this area.

4. The Board agreed it would be useful to receive data from the Helpdesk to review top issues.

Actions/further information to be provided:

The Board to receive information from the Helpdesk outlining top issues.

Recommendations:

The Board noted the content of the report and annex.

43/18 COMMUNICATIONS UPDATE [Item 12]

Declarations of interest:

None

Witnesses:

Clare Chambers, Pensions Service Delivery Manager

Key points raised during the discussion:

1. It was reported that the service had prepared a draft discretion policy to roll out to employers with a tutorial at the end of July 2018 to encourage employers to document discretions.Members supported the exercise and suggested that employer discretions should be covered as a topic at the Pension Fund AGM in November 2018.

2. It was noted that the service were also rolling out support for Surrey Pension Scheme employers with internal disputes resolution procedures.

Actions/further information to be provided:

None

Recommendations:

The Board noted the content of this report and recommended Pension Fund discretion be covered as a topic at the pension Fund AGM.

13

44/18 CYBER SECURITY [Item 13]

Declarations of interest:

None

Witnesses:

Ayaz Malik, Pensions Accountant Advisor

Key points raised during the discussion:

1. The Board received an update on cyber security policies and procedures affecting the Northern Trust as the Fund's custodian and the Council.

Actions/further information to be provided:

The Board to receive a presentation from the IMT Manager on the Council's implementation of Cyber Security.

Recommendations:

The Board noted the content of this report.

45/18 RISK REGISTERS 2018/19: QUARTER 1 [Item 14]

Declarations of interest:

None

Witnesses:

John Smith, Senior Advisor
Clare Chambers, Pensions Service Delivery Manager

Key points raised during the discussion:

1. Officers summarised changes made to existing risks in the Fund Risk Register requested by the Board in a meeting of 23 April 2018.

2. The Board noted the new risk identified due to the change in Section 151 Officer.

Actions/further information to be provided:

Officers to update comments for A12 in the Administration Risk Register to highlight the further progress made with the GMP reconciliation.

Recommendations:

The Board noted the content of this report, the Fund Risk Register and Administration Risk Register.

46/18 LOCAL PENSION BOARD ANNUAL REPORT [Item 15]

Declarations of interest:

None

Witnesses:

Ayaz Malik, Pensions Accountant Advisor

Key points raised during the discussion:

1. Members received a copy of the Local Pension Board Annual report (attached to the minutes as Annex 1) to be presented to the Pension Fund Committee at its meeting on 14 September 2018.

Actions/further information to be provided:

None

Recommendations:

The Board noted the content of this report.

47/18 TRAINING BULLETIN: QUARTER 1 [Item 16]

Declarations of interest:

None

Witnesses:

John Smith, Senior Advisor

Key points raised during the discussion:

1. There was a discussion around recent developments in pensions and the Board noted key changes in the 2018 amendment regulations and AVCs.

Actions/further information to be provided:

None

Recommendations:

The Board noted the content of this report.

13

48/18 PRE-VALUATION PROJECT PLAN [Item 18]

Declarations of Interest:

None.

Witnesses:

John Smith, Senior Advisor
Ayaz Malik, Pensions Account Advisor

Key points raised during the discussion:

1. It was noted that the Fund actuary, Hymans Robertson, carried out the triennial valuation of the Fund's assets and liabilities. The primary and secondary contribution rates for employers were derived from this valuation. The next triennial valuation was scheduled for 31 March 2019 (effective 1 April 2020). The project timeline for the next valuation runs from June 2018 to June 2019. The Board were presented with a draft project plan, attached as Annex 1 to the submitted report.

2. Officers clarified that the reference 'HEAT' mentioned in the report referred to 'Hymans Employer Asset Tracker'.

3. It was highlighted that the purpose of the project plan was to track changes and support the production of timely results. Officers assured the Board that regular updates would be provided on the progress of the valuation.

Actions/further information to be provided:

None

Recommendation:

The Board noted the content of this report.

49/18 EXCLUSION OF THE PUBLIC [Item 17]

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

50/18 BORDER TO COAST UPDATE [Item 19]

Key points raised during the discussion:

1. The Chairman agreed to take this meeting into Part 2 for this item.

Actions/further information to be provided:

None

Recommendation:

The Board noted the content of this report.

51/18 PUBLICITY OF PART 2 ITEMS [Item 20]

Key points raised during the discussion:

1. The Board agreed that Item 18, the Pre-valuation Project Plan which was published as Part 2 Private could be made available to the public as there was no disclosure of exempt information (attached as Annex 1). Members of the public were also invited to stay for this item.

RESOLVED: The Board agreed not to disclose the information relating to Item 19, the Part 2 item, Border to Coast update as it was commercially sensitive.

52/18 DATE OF THE NEXT MEETING [Item 21]

The next meeting of the Local Pension Board will be held on 23 October 2018.

Meeting ended at: 12.00 pm

Chairman

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SURREY
COUNTY COUNCIL

Surrey Local Pension Board
25 July 2018

Administration Performance Report 1 April 2018 to 30 June 2018

Recommendations:

The Board is asked to **note** the content of this report and **make recommendations** to the Pension Fund Committee if appropriate.

Background

1. At the Pension Fund Committee of 15 September 2017, the Pension Fund Committee (Committee) approved a new Administration Performance Report (APR) to replace the existing Key Performance Indicators (KPR) from quarter 3 of 2017/18.

2. The new APR is designed give a wider snap shot of the administrative function. It is designed to provide an overview of the administration function including ongoing workflow, oversight of customer feedback and future performance plans. It also allows the Committee and Board oversight of statutory compliance and meets a recommendation from the 2016/17 internal audit.

3. At the Committee meeting of 10 November 2017, the Committee agreed that future administrations statistics reports presented to the Committee be in the form of focused summary of the APR. This summary will be produced after the full APR has been scrutinised by the Board and will include any relevant Board recommendations.

The 2017/18 Quarter 4 APR

Summary

4. The APR contains three sections:
    - Ongoing workflow;
    - Performance standards; and
    - Administration forward plan.
    -

5. The Ongoing workflow section provides detail of the activities of the administration function, along with measurement against performance standards. It includes the following sub-sections:
    - Overview;
    - Caseload detail (members);
    - Caseload details (employers); and
    - Complaints/breaches

6. The Performance standards section highlights functions that are a regulatory requirement but also concentrates on customer driven performance criteria to inform continuous improvement work. This section consists of the following sub-sections:
    - Scrutiny;
    - Data quality;
    - Communications;
    - Value for money; and
    - Projects.

7. The Administration forward plan include reports scheduled to be brought to the Committee and Board.

Caseload performance RAG

8. Member and employer caseloads are measured against performance levels, with red, amber and green ratings. A green rating indicates the tolerable performance level has been met. An amber rating indicates that performance levels were below tolerable by 5% or less. A red rating indicates that performance levels were below tolerable by more than 5%.

9. The board debated lowering the existing aspiration from 100% to 95% for a variety of reasons; however, upon mature consideration it was decided that 100% was the only appropriate target.

Material changes since 2017/18 Quarter 4

10. The context is important in this quarter as a number of key posts have been replaced and it is, perhaps, understandable that the figures have suffered.

11. Of the 26 pension administration case load details sub-categories, there were improvements in three areas and a decline in thirteen. The deferred benefits (increased to 63%), refunds (fallen to 51%), death dependent's benefits initial (fallen to 80%), death on pension initial (fallen to 63%) were all below the tolerable level (red) and death dependent's benefits complete (fallen to 85%) was on the cusp (amber).

12. The previous Lead Pensions Manager advised that the processing of Deferred Benefits and other leavers prior to retirement are traditionally high volume resource intensive transactions that have understandably been viewed by administrators as an area that can be treated as lower priority than other key functions because there is no immediate entitlement to benefits. However, we recognised some time ago that excessive numbers were building up and have spent the last 12 months developing an automated solution (robotic process automation – RPA) that will provide significant

long term efficiency savings. This has resulted in an excessive build-up of unprocessed leavers but it is anticipated these can be processed very efficiently once RPA is live.

13. The Pension Service Delivery Manager has kindly provided the Pension Section's observations on the statistics, which are set out immediately below.

    Rather than add separate comments on each red item, I would like to caveat the report with a general update on performance (which I think is more or less covered in the Admin Update Report). It is difficult for me to comment on past performance when I have only been here for such a short amount of time, however I can comment on the various initiatives we are implementing going forward in order to work towards improving the service we offer to customers (members and employers).

    In summary these are:

- Lack of resource – The Lead Pensions Manager and I are working on a resource plan and have identified where our resource gaps are. We are currently working with HR and Finance to start the recruitment to fill these gaps so that we have a full complement of the necessary staff.
- Employer Data Issues – we have issues with the data received from some scheme employers and the team spend a significant amount of their day querying data with employers which in turns holds them back from being able to progress cases. We are implementing an employer's issue log so that the team can detail what the issues are and with who, as and when they occur. I will then review this on a regular basis to identify the problem employers so that we can target them and also identify any common training needs.
- Processes – we have recruited a Customer & Service Improvement Officer to review our current processes with a view to removing unnecessary waste and streamline processes.
- Self-Service – we are looking at investing time in improving the online information/services provided to members and employers so that we can encourage them to self-serve and reduce the amount of contact into the team allowing us to focus on more complex tasks.
- Productivity – I am meeting regularly with Team Leaders to review productivity and accuracy of the team, and address any concerns. We are also looking at skills matrices and training plans to identify knowledge gaps and SPOF's.

Once implemented all of the above should significantly increase our ability to meet KPI's and in turn provide an excellent level of service to our customers. Hopefully, this will reassure the Board more than drilling down into the detail of why individual KPI's have failed.

Additional categories added

14. In the meeting of 18 January 2018 the Board recommended the following:
    - *Ill-health statistics should be split between active and deferred cases*: Ill-health retirement quotations and actuals have been split between actives and deferred beneficiaries as requested by the board. This means that the latest statistics cannot be compared with previous quarters on a like for like basis, albeit that the overall figures have improved.

- *Invoicing should be reviewed so that strain costs are recharged in a timely manner:* Two new lines have been added to the APR for this quarter, one to measure the number of invoices issued and the other to monitor the number of invoices paid. We shall be able to drill down to find more detail should invoices remain unpaid at the end of the quarter.
- *The Communications Strategy should be reviewed*: This is included in the APR Report Forward Plan

Next steps

15. The Board is asked to **note** the content of this report and the 2018/19 Quarter 1 APR Report (shown as Annex 1) and **make recommendations** to the Pension Fund Committee if appropriate.

Report contact: John Smith, Senior Advisor (Investments, Finance and Governance)

Contact details: T: 020 8213 2700 E: john.smith@surreycc.gov.uk

Sources/background papers:

Annexes:

1. 2018/19 Quarter 1 APR Report

2018/19 Quarter 1 Fund Risk Register

Annex 3

Risk Group	Risk Ref.	Previous	Risk Description	Impact: Fund	Impact: Employers	Impact: Reputation	Impact: Total	Likelihood	Total risk score	Mitigation actions	Revised Likelihood	Net risk score	Reviewed on	Changes made during review
Funding	1	1	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	TOLERATE- 1) The discount rate used for the 2016 actuarial valuation will be derived from CPI inflation so the value of Fund liabilities will be calculated with reference to CPI. 2) The fund holds investment in index-linked bonds within a liability driven investment portfolio to mitigate risk. 3) Liability driven investment strategy implementation designed to hedge against future risk approved by Pension Fund Committee on 13 February 2015. Future trigger points for leverage will provide liability protection against inflation risk with the full protection framework in place.	4	48	Jun-18	Action changed to Tolerate from Treat.
Funding	2	2	Pensioners living longer: adding one year to life expectancy will increase the future service rate by 0.8%	4	4	1	9	5	45	TOLERATE- 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 and postcode specific.	5	45	Jun-18	Action changed to Tolerate from Treat.
Funding	3	3	Pay increases are significantly more than anticipated for employers within the Fund.	4	4	3	11	4	44	TREAT/TOLERATE- 1) Fund employers should monitor own experience. 2) Assumptions made on pay and price inflation (for the purposes of IAS19/FRS102 and actuarial valuations) should be long term assumptions, any employer specific assumptions above the actuaries long term assumption would lead to further review. 3) Employers to be made aware of generic impact that salary increases can have upon final salary linked elements of LGPS benefits.	4	44	Jun-18	Action changed to Treat and Tolerate from Treat.
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 Committee officers and consultants. 2) 2017/18 Investment strategy review is current. 3) Separate source of advice from Fund's independent advisor. 4) Setting of Fund specific benchmark relevant to the current position of fund liabilities. 5) Fund manager targets set and based on market benchmarks or absolute return measures. Overall investment benchmark and out-performance target is fund specific.	3	30	Jun-18	Unchanged
Investment	5	5	Increased risk to global financial stability. Outlook deteriorates in advanced economies because of heightened uncertainty and setbacks to growth and confidence, with declines in oil	4	3	3	10	4	40	TREAT/TOLERATE- 1) Increased vigilance and continued dialogue with managers as to events on and over the horizon. 2) Continued investment strategy involving portfolio diversification and risk control. 3) Investment strategy review will follow post actuarial 2016 valuation.	3	30	Jun-18	Action changed to Treat and Tolerate from Treat.
Investment	6	7	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 £3.9m	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 Committee 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	Jun-18	Unchanged
Financial	7	8	Financial loss of cash investments from fraudulent activity	4	4	4	12	3	36	TREAT and TOLERATE - 1) Policies and 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 SAS70 or similar (statement of internal controls).	2	24	Jun-18	Action changed to Treat and Tolerate from Tolerate.
Operational	8	9	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	Jun-18	Unchanged
Investment	9	10	Significant volatility and negative sentiment in investment markets following the outcome of the US presidential election.	4	3	3	10	2	20	TREAT/TOLERATE- 1) Continued dialogue with managers as to the management of increasing political risk in developed markets. 2) Investment strategy involving portfolio diversification and risk control. 3) Investment strategy review will follow post actuarial 2016 valuation.	2	20	Jun-18	Action changed to Treat and Tolerate from Treat. **Nonetheless, we recommend that the board deletes this risk.**
Investment	10	11	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	TOLERATE- 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 continuously 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 a measure over CPI over gilts is regarded as achievable over the long term when compared with historical data.	2	20	Jun-18	Action changed to Tolerate from Treat.
Funding	11	13	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	Jun-18	Unchanged
Governance	12	15	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	Jun-18	Unchanged
Investment	13	16	Volatility caused by uncertainty with regard to the withdrawal of the UK from the European Union and its after effects	3	3	2	8	3	24	TOLERATE- 1) Officers to consult and engage with advisors. 2) Future possibility of looking at move from UK to Global benchmarks on UK Equities and UK Property. 3) Possibility of further hedging of currency movements against Sterling.	2	16	Jun-18	Action changed to Tolerate from Treat.
Operational	14	18	Insufficient attention to environmental, social and governance (ESG) leads to reputational damage	1	1	3	5	4	20	TREAT-1) Review ISS 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	Jun-18	Unchanged
Governance	15	19	Implementation of proposed changes to the LGPS (pooling) 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, seminars, conferences. 2) Officers engage in early planning for implementation against agreed deadlines. 3) Future secondment of Surrey officers onto pooling project teams.	2	14	Jun-18	Unchanged
Operational	16	20	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 Committee will be mindful of the proposed CIPFA Knowledge and Skills Framework when setting objectives and establishing training needs.	2	14	Jun-18	Unchanged
Operational	17	22	Failure to hold personal data securely	1	1	4	6	3	18	TREAT- 1) Data encryption technology is in place, which allow secure the sending of data to external service providers. 2) Phasing out of holding records via paper files. 3) Pensions Admin records are locked daily in a secure safe. 4) SCC IT data security policy adhered to.	2	12	Jun-18	Unchanged
Funding	18	23	Impact of government policy on the employer workforce	3	2	1	6	3	18	TREAT/TOLERATE- 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.	2	12	Jun-18	Action changed to Treat and Tolerate from Treat.
Governance	19	24	Changes to LGPS regulations	3	2	1	6	3	18	TREAT/TOLERATE-1) Fundamental change to LGPS regulations implemented from 1 April 2014. 2) Impact on contributions and cashflows will considered during the 2016 valuation process. 3) Fund will respond to consultations. 4) Impact of LGPS (Management of Funds) Regulations 2016 to be monitored.	2	12	Jun-18	Action changed to Treat and Tolerate from Treat.
Governance	20	25	Change in membership of Pension Fund Committee 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 Committee members. 3) Pension Fund Committee 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 Committee members to take the test.	2	12	Jun-18	Unchanged
Operational	21	26	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	Jun-18	Unchanged
Operational	22	27	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) Regular meetings and conversations with Northern Trust take place. 3) Actuarial and investment consultancies are provided by two different providers.	2	12	Jun-18	Unchanged
Governance	23	28	That the Border to Coast Pensions Partnership disbands or the partnership fails to produce a proposal deemed sufficiently ambitious.	3	2	4	9	1	9	TOLERATE-1) Partners for the pool were chosen based upon the perceived expertise and like-mindedness of the officers and members involved with the fund to ensure compliance with the pooling requirements. Ensure that ongoing fund and pool proposals are comprehensive and meet government objectives.	1	9	Jun-18	Unchanged
Governance	24	29	Failure to comply with legislative requirements e.g. ISS, 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	Jun-18	Unchanged
Operational	25	30	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.	1	6	Jun-18	Unchanged
Governance	26	31	Failure to comply with recommendations from the local pension board, resulting in the matter being escalated to the scheme advisory board and/or the pensions regulator	1	1	4	6	1	6	TOLERATE -1) Ensure that an cooperative, effective and transparent dialogue exists between the pension committee and local pension board.	1	6	Jun-18	Unchanged

Risk Group	Risk Ref.	Previous	Risk Description	Impact				Likelihood	Total risk score	Mitigation actions	Revised Likelihood	Net risk score	Reviewed on	Changes made during review
				Fund	Employers	Reputation	Total							
Financial	27	32	Counterparty risk within the SCC treasury management operation	2	2	2	6	2	12	TOLERATE - 1) Lending limits with approved banks and other counterparties are set at prudent levels 2) The pension fund treasury management strategy is based on that of SCC.	1	6	Jun-18	Unchanged
Financial 13	28	34	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 and other counterparties 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	Jun-18	Unchanged

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