Pension Fund Investment Sub-Committee

19 May 2014

Agenda

The Pension Fund Investment Sub-Committee will meet at **Shire Hall, Warwick** on **19 May 2014** at **10:00am**

1. General

(1) Apologies

(2) Members' Disclosures of Pecuniary and Non-Pecuniary Interests.

Members are required to register their disclosable pecuniary interests within 28 days of their election of appointment to the Council. A member attending a meeting where a matter arises in which s/he has a disclosable pecuniary interest must (unless s/he has a dispensation):

- Declare the interest if s/he has not already registered it
- Not participate in any discussion or vote
- Must leave the meeting room until the matter has been dealt with (Standing Order 42).
- Give written notice of any unregistered interest to the Monitoring Officer within 28 days of the meeting

Non-pecuniary interests must still be declared in accordance with the new Code of Conduct. These should be declared at the commencement of the meeting.

(3) Minutes of the previous meeting and matters arising

2. Infrastructure Managers

3. Funding Strategy Statement

4. The 2013 Actuarial Valuation

5. Investment Performance

6. Review of Investment Strategy

7. Share Voting Policy

8. Directions Order/ Fair Deal

EXEMPT ITEMS

9. Reports Containing Confidential or Exempt Information

To consider passing the following resolution:
'That members of the public be excluded from the meeting for the item mentioned below on the grounds that their presence would involve the disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972'.

10. (Exempt) minutes of the meeting held on 10 February 2014

11. (Exempt) Nuneaton and Bedworth Borough Council Leisure Services (1)

12. (Exempt) Nuneaton and Bedworth Borough Council Leisure Services (2)

13. (Exempt) Nuneaton and Bedworth Leisure Services (3)

14. Any other items

Which the Chair decides are urgent.

JIM GRAHAM
Chief Executive
Shire Hall
Warwick

Membership of the Pension Fund in Investment Sub-Committee

Councillors John Appleton (Chair), Sara Doughty, Bill Gifford, John Horner (Vice Chair), and Brian Moss

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Minutes of the Pension Fund Investment Sub-Committee meeting held on 10 February 2014

Present:

Members
Councillors Bill Gifford, Brian Moss, Izzi Seccombe (replacing John Appleton) and David Shilton (replacing John Horner).

Officers
Sally Baxter, Democratic Services Officer
John Betts, Head of Finance
Neil Buxton, Pensions Services Manager
Mathew Dawson, Treasury and Pension Fund Manager
John Galbraith, Senior Solicitor, Pension Fund Services
Andrew Lovegrove, Head of Corporate Financial Services

Invitees
Robert Bilton, Hymans Robertson
Peter Jones, Independent Investment Advisor
Paul Potter, Investment Advisor, Hymans Robertson
Rick Di Masio, Inalytics
John Wright, Hymans Robertson

1. General

(1) Apologies

Apologies were received from Councillors John Appleton, Sara Doughty and John Horner.

(2) Disclosures
None.

(3) Minutes of the previous meeting
The minutes of the meeting held on 11 November 2013 were agreed as a true record.

2. Scheme Membership

2.1 Neil Buxton, Pensions Manager, in response to the Committee's request, provided an update regarding the membership of the Warwickshire Local Government Pension Scheme (LGPS) following the auto enrolment Staging Date of 1 May 2013.

2.2 He reported that membership had increased with a further seven employers auto enrolling employees on to the Warwickshire LGPS. A discussion ensued about cash flow and whether the income being drawn was considered adequate.

2.3 In response to a question, Neil Buxton stated that Elected Members had not been included in the auto enrolment figures as they were awaiting guidance from Central Government. Existing Elected Members could remain in the LGPS but it was unknown whether new Elected Members would be able to join.

2.4 Resolved

That the Pension Fund Investment Sub-Committee notes the Scheme Membership report.

3. Share Voting Policy

3.1 The Committee agreed that this item be deferred to the next meeting scheduled for 19 May 2014. More Information would be provided in advance of the meeting to aid robust decision making. The Committee requested that all information to be presented to the Committee in future, be produced and presented in a timely manner.

3.2 Resolved

That the Committee consider the Share Voting Policy at the next meeting of the Pension Fund Investment Sub-Committee scheduled for 19 May 2014.

4. The 2013 Actuarial Valuation

4.1 Robert Bilton, Hymans Robertson, explained the results of the 2013 Actuarial Valuation to the Committee and distributed a detailed analysis of the valuation for the period 31 March 2010 to 31 March 2013.

4.2 The report was the initial summary of the outcome of the valuation however, a final version would be considered at the Committee scheduled for 19 May 2014. The results included information in relation to the deficit and funding levels, common contribution rate, past service contributions rate and individual employer contribution rates.

4.3 It was noted that the risk of liabilities had been reduced in 2013 which was in part following the low amount of salary increases. In addition to this, the impact of the new structure adopted for the LGPS was also attributed to reducing liabilities.

4.4 The Committee was informed that the current actuary uses different assumptions to those used by the previous actuary. John Galbraith, Senior Solicitor, observed that the difference between actuaries would be apparent when evaluating future benefits in so far a more cautious approach was being undertaken but this was in response to the changed market outlook which had resulted in an increased deficit.

4.5 The Committee identified that the risk for the Council was that the liabilities had increased but the number of employees had reduced. In response, Mathew Dawson, explained that measures were being put in place to mitigate against this such as requesting employers to pay a cash lump sum.

4.6 A detailed discussion ensued regarding the revised structure of the LGPS for 2014 and the effects this would have on existing and future members. In particular, it was highlighted that it would be beneficial for some employers but not all.

4.7 It was reported that with regards to the past service position, the rise in liabilities had outweighed the value of the assets and the deficit in cash terms had grown which should be taken into consideration when quoting funding levels. The payroll had decreased since 2010 therefore the contribution rate had increased.

4.8 The contribution rate strategies had adopted an approach whereby each employer had an individual account however, for colleges and some academies, a risk based model had been adopted.

4.9 Resolved

The Pension Fund Investment Sub Committee notes the 2013 Actuarial Valuation results.

5. 2013/14 Business Plan

5.1 Mathew Dawson, provided an overview of the Warwickshire County Council Pension Fund Business Plan and Actions for 2014/15.

5.2 The Plan incorporated various elements including:

- Administration,
- Communication,
- Actuarial/funding,
- Pension Fund Investment Sub-Committee Members,
- Financial and Risk Management and;
- Investment.

5.3 The Annual Employer's Forum was held in January 2014 and engagement with employers had taken place to ensure members had been communicated with in a timely manner and had a good understanding of their benefit statements. Proposed rates following the 2013 actuarial valuation had been sent to employers with a deadline of 28 February 2014 for a response. It was reported that some responses had been received which indicated that the new employer rates were considered unaffordable.

5.4 Resolved

That the Pension Fund Investment Sub-Committee approve the Warwickshire County Council Pension Fund Business Plan for 2014/15.

6. Exempt Items – Reports containing Confidential or Exempt Information

6.1 The Pension Fund Investment Sub-Committee passed the following resolution: That members of the public be excluded from the meeting for the item mentioned below on the grounds that their presence would involve the disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972.

7. Pooling and Risk Sharing (Commissioning Services)

7.1 John Wright, Hymans Robertson, presented the report and Peter Jones provided advice, during discussion, as per the exempt minutes.

8. Exempt Minutes of the meeting of the Pension Fund Investment Sub Committee – 11 November 2013

8.1 The Pension Fund Investment Sub-Committee agreed the exempt minutes of the meeting held on 11 November 2013 as a true and accurate record subject to amendment of 9.5 as per the exempt minutes.

9. Equity Managers (Presentation by Inalytics)

9.1 Rick Di Masio, Inalytics, provided an overview of the services provided by Inalytics and the potential benefits that could arise such as enhanced governance when holding Fund Managers to account and evaluation of the effectiveness of performance.

9.2 Following questions from the Committee, it was agreed that a sample report produced by Inalytics would be distributed to Committee Members and considered at a future meeting.

9.3 Resolved

That the Committee would consider the sample report and Inalytics would attend a future meeting to discuss the services they provide.

10. Any other items

None.

The Sub Committee rose at 11.35am

………………………………………
Chair

Pension Fund Investment Sub Committee

19 May 2014

Infrastructure Managers

Recommendation

(1) That the sub-committee approve the current position with regard to the ongoing fund manager appointment process.

1 Introduction

1.1 This paper considers the implementation of the new investment arrangements following the appointment of SL Capital Partners and Partners Group.

2 Asset Allocation

2.1 At meeting of 11 November 2013 the sub-committee approved the proposal for officers to instruct Hymans Robertson to start initial work around infrastructure fund managers.

2.2 Following this meeting Hymans Robertson undertook a manager search which included both fund of fund and single fund managers for consideration. A subsequent conference call with the vice chair, officers, independent advisor and consultants took place to determine a short list. Short listed managers were subsequently interviewed on 20 March 2014.

2.3 The total allocation to infrastructure will be £55m (around 4% of the fund). It was decided that the fund would split the allocation to invest in a fund of funds and a single manager to best access the benefits of the asset class.

2.5 The single fund selected is the SL Capital Infrastructure I, a closed ended fund which will run for initial period of 12 years and will manage between 6-8 assets with a target AUM of £500m. Warwickshire will be investing £20m into this pooled product as a first close investor which will give the fund a preferential fee rate.

2.6 The fund of funds manager is Partners Group Global Infrastructure 2014. This product is a 12 year closed ended fund that will invest in primary and secondary investments as well as direct investments. Warwickshire will be investing £35m into this fund.

Transition manager

3.1 The Fund’s transition manager, Blackrock, will be asked to manage the necessary transfers of assets.

3.2 The amendments to the asset allocation to allow for these managers will be presented in the July meeting as part of the Hymans review of the fund’s investments.

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Pension Fund Investment Sub Committee

19 May 2014

Funding Strategy Statement

Recommendation

That the sub-committee approve the Funding Strategy Statement in point 4.1

1 Introduction

1.1 Under LGPS Regulations, the Fund has to prepare and publish a Funding Strategy Statement (FSS). In doing so, it must take guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) into account and “consult such persons as it considers appropriate”. This is generally taken to be employers as they are the group that are responsible for meeting the balance of the cost of benefits promised to members.

1.2 The natural time to review and update the FSS is at the end of each triennial actuarial valuation cycle. It should reflect all of the funding decisions made by the Fund during the valuation year. Given that there is a requirement for the fund to consult with employers the draft statement was published on the Fund’s website prior to this meeting.

1.3 The draft FSS appended to this paper allows for the most recent guidance issued by CIPFA in 2012. The Fund plans to formally consult with employers following the Investment Sub Committee meeting on 19 May. Following the consultation, the final version of the FSS will be published on the Fund’s website.

2 Legislative Background

2.1 At meeting of 11 November 2013 the sub-committee approved the proposal for officers to instruct Hymans Robertson to start initial work around infrastructure fund managers.

3 Key highlights in the FSS

3.1 Funding objectives

- to ensure the long term solvency of the Fund
- to ensure that employer contribution rates are relatively stable (where appropriate)
- to minimise employer contributions over the longer term (and Council Tax costs), by recognising how assets and liabilities interact and by adopting an investment strategy that balances risk and return
- to set contribution rates that allow for the different risk profiles of participating employers
- to reduce the risk to other employers (and ultimately the Council Tax payer) of an employer defaulting on its pension obligations.

3.2 It is worth noting that, in relation to the last bullet, the Investment Sub Committee approved an updated terminations policy that covers employers leaving the Fund at its meeting on 11 November 2013.

3.3 Employer contribution rate setting

3.4 The way in which employer contribution rates were set at the 2013 valuation were discussed and agreed between the Fund Actuary and the Fund's officers and Investment Sub Committee over the course of the last year. As mentioned, various meetings were held with employers to help them to understand the process.

3.5 The approaches that were agreed across the various employer groupings are summarised in the table on page 9 of the draft FSS. It refers to the stabilised approach to contribution rate setting that was adopted for the tax-raising bodies and the risk based approach used for other bodies in the Fund. Amongst other things, it outlines how funding differs between employers that are open and closed to new entrants, shows the deficit recovery period that applies to each type of employer and confirms that deficit repayments will be collected as monetary amounts (rather than as a percentage of pay to protect against the risk of payroll falling in future).

3.6 Employer contribution rate setting

3.7 One of the key objectives is to ensure that the Fund can meet all benefit payments as and when they fall due. It achieves this via a combination of contributions (arising from the funding strategy) and investment returns and income (arising from the investment strategy). If investment returns are lower than expected, then contributions need to be higher, and vice versa. In other words, the strategies are interlinked.

3.8 The draft FSS explains how the funding policy is consistent with the investment strategy. In particular, it outlines how the asset-liability modelling carried out during 2013 allowed the Fund to set stable contribution rates whilst maintaining its aim of funding on a prudent basis.

3.9 Risks and control mechanisms

3.10 The Appendix at the back of the FSS looks at risks under four headings:

- Financial e.g. underperforming assets, falls in bond yields
- Demographic e.g. members living longer, high levels of early or ill health retirements
- Regulatory e.g. pensions reform, tax regime changes
- Governance e.g. poor communication with employers, employers unexpectedly terminating with a deficit

3.11 The valuation is a good time to have a think about the risks that the Fund faces. The FSS also summarises how the Fund manage and control these risks.

4 Recommendation

4.1 That the sub-committee approve the attached Funding Strategy Statement.

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HYMANS ROBERTSON

Warwickshire County Council Pension Fund

Funding Strategy Statement

April 2014

PUBLIC SECTOR

Contents

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1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the Warwickshire County Council Pension Fund ("the Fund"), which is administered by Warwickshire 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 19 May 2014.

1.2 What is the Warwickshire County Council 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 Warwickshire County Council Pension Fund, in effect the LGPS for the Warwickshire 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;
- 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 (see Section 4).

1.4 How does the Fund and this FSS affect me?

This depends who you are:

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

- 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.

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 Neil Buxton in the first instance at e-mail address neilbuxton@warwickshire.gov.uk or on telephone number 01926 412195.

2 Basic Funding issues

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

2.1 How does the actuary calculate a contribution rate?

Employer contributions are normally made up of two elements:

a) the estimated cost of future benefits being built up from year to year, referred to as the "*future service rate*"; plus

b) an adjustment for the difference between the assets built up to date and the value of past service benefits, referred to as the "*past service adjustment*". If there is a deficit the past service adjustment will be an increase in the employer's total contribution; if there is a surplus there may be a reduction in the employer's total contribution. Any past service adjustment will aim to return the employer to full funding over an appropriate period (the "deficit recovery period").

2.2 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, 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.

A larger deficit will give rise to higher employer contributions. If a deficit is spread over a longer period then the annual employer cost is lower than if it is spread over a shorter period.

2.3 How are contribution rates calculated for different employers?

The Fund's actuary is required by the Regulations to report the *Common Contribution Rate*, for all employers collectively at each triennial valuation, combining items (a) and (b) above. This is based on actuarial assumptions about the likelihood, size and timing of benefit payments to be made from the Fund in the future, as outlined in Appendix E.

The Fund's actuary is also required to adjust the *Common Contribution Rate* for circumstances specific to each individual employer. The sorts of specific circumstances which are considered are discussed in Section 3. It is this adjusted contribution rate which the employer is actually required to pay, and the rates for all employers are shown in the Fund's Rates and Adjustments Certificate.

In effect, the *Common Contribution Rate* is a notional quantity, as it is unlikely that any employer will pay that exact rate. Separate future service rates are calculated for each employer together with individual past service adjustments according to employer-specific circumstances.

Details of the outcome of the Actuarial Valuation as at 31 March 2013 can be found in the formal valuation report dated 31 March 2014, including an analysis at Fund Level of the *Common Contribution Rate*. Further details of individual employer contribution rates can also be found in the formal report.

2.4 What else might affect the employer's contribution?

Employer covenant, and likely term of membership, are also considered when setting contributions: more details are given in Section 3.

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.

If an employer is approaching the end of its participation in the Fund then its contributions may be amended appropriately, so that the assets meet (as closely as possible) the value of its liabilities in the Fund when its participation ends.

Employers' contributions are expressed as minima, with employers able to pay contributions at a higher rate. Account of the higher rate will be taken by the Fund Actuary at subsequent valuations.

2.5 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, 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** ("CABs") or those providing a service on behalf of a scheme employer – **transferee admission bodies** ("TABs"). 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.

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;
- 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.

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;
- 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 Fund 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. This helps the Fund establish a picture of the financial standing of the employer, i.e. its ability to meet its long term Fund commitments.

For instance, where an employer is considered relatively low risk then the Fund will permit greater smoothing (such as stabilisation or a longer deficit recovery period relative to other employers) which 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, an employer whose risk assessment indicates a less strong covenant will generally be required to pay higher contributions (for instance, with a more prudent funding basis or a shorter deficit recovery period relative to other employers). This is because of the higher probability that at some point it will fail or be unable to meet its pension contributions, with its deficit in the Fund then falling to other Fund employers.

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, there are a number of methods which the Administering Authority may permit, in order to improve the stability of employer contributions. These include, where circumstances permit:-

- capping of employer contribution rate changes within a pre-determined range ("stabilisation")
- the use of extended deficit recovery periods
- the phasing in of contribution rises or reductions
- the pooling of contributions amongst employers with similar characteristics
- the use of some form of security or guarantee to justify a lower contribution rate than would otherwise be the case.

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 contributions below the theoretical level

Employers which are permitted to use one or more of the above methods will often be paying, for a time, contributions less than the theoretical contribution rate. 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 choice of method,
- 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 will lead to higher contributions in the long-term, and
- it will take longer to reach full funding, 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 and Police**	**Colleges, other FE establishments and Academies**	**Open to new entrants**	**Closed to new entrants**	**(all)**
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)
Future service rate	Projected Unit Credit approach (see Appendix D – D.2)			Attained Age approach (see Appendix D – D.2)	Projected Unit Credit approach (see Appendix D – D.2)
Stabilised rate?	Yes - see Note (b)	Risk Based Model			No
Maximum deficit recovery period – Note (c)	19 years	19 years	19 years	Future working lifetime, subject to 19 years maximum	Outstanding contract term
Deficit recovery payments – Note (d)	Monetary amounts	Monetary amounts	Monetary amounts	Monetary amounts	Monetary amounts
Treatment of surplus (where applicable)	Covered by stabilisation arrangement	Preferred approach: contributions kept at future service rate unless fully funded on a gilts basis.			Reduce contributions by spreading the surplus over the remaining contract term
Phasing of contribution changes	Covered by stabilisation arrangement	3 years - Note (e)	3 years - Note (e)	None	None
Review of rates – Note (f)	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations				Particularly reviewed in last 3 years of contract
New employer	n/a	Note (g)	Note (h)		Notes (h) & (i)
Cessation of participation: cessation debt payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation debt principles applied would be as per Note (j).		Can be ceased subject to terms of admission agreement. Cessation debt will be calculated on a basis appropriate to the circumstances of cessation – see Note (j).		Participation is assumed to expire at the end of the contract. Cessation debt (if any) calculated on ongoing basis. Awarding Authority will be liable for future deficits and contributions arising.

Note (a) (Basis for CABs and Designating Employers (that are not Parish or Town Councils) 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 vary the discount rate used to set the employer's contribution rate. In particular contributions may be set for an employer to achieve full funding on a more prudent basis (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 if:

- the employer satisfies the eligibility criteria set by the Administering Authority (see below) and;
- there are 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).

On the basis of extensive modelling carried out for the 2013 valuation exercise (see Section 4), the stabilised details are as follows:

Type of employer	Local Authority or Police
Max contribution rate increase	+0.75% of pay per annum
Max contribution rate decrease	-0.75% of pay per annum

The stabilisation criteria and limits will be reviewed at the 31 March 2016 valuation, to take effect from 1 April 2017. This will take into account the employer's membership profiles, the issues surrounding employer security, and other relevant factors.

Note (c) (Deficit Recovery Periods)

The deficit recovery period starts at the commencement of the revised contribution rate (1 April 2014 for the 2013 valuation). The Administering Authority would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative spreading periods, for example where there were no new entrants.

Where stabilisation applies, the resulting employer contribution rate would be amended to comply with the stabilisation mechanism.

For employers with no (or very few) active members at this valuation, the deficit should be recovered by a fixed monetary amount over a period to be agreed with the body or its successor, not to exceed 19 years.

Note (d) (Deficit Recovery Payments)

The deficit recovery payments for each employer covering the three year period until the next valuation are set as a monetary amount as default.

Note (e) (Phasing in of contribution changes)

All phasing is subject to the Administering Authority being satisfied as to the strength of the employer's covenant.

Employers which have no active members at this valuation will not be phased.

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 employers)

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

a) 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;

b) 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;

c) 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;

d) The new academy's initial contribution rate will be set with reference to the following contribution rates:

Year	Contribution rate (% of pay)
2014/15	19.7%
2015/16	20.9%
2016/17	22.0%

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 (c) and (d) 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;
- the current deficit.

For all new Transferee Admission Bodies, 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.

The Administering Authority will only consider requests from Community Admission Bodies (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/commissioning 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 "commission" 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 the 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 doesn't pay any cessation deficit.

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;
- 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;
- 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;
- Any breach by the Admission Body of any of its obligations under the Fund's admissions and termination policy that they have failed to remedy to the satisfaction of the Fund;
- A failure by the Admission Body to pay any sums due to the Fund within the period required by the Fund; or
- The failure by the Admission Body to renew or adjust the level of the bond or indemnity, or to confirm an appropriate alternative guarantor, as required by the Fund.

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

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

a) Where there is a guarantor for future deficits and contributions, the cessation valuation will normally be calculated using the ongoing basis as described in Appendix E;

b) Alternatively, 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;

c) 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.

Under (a) and (c), 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 look to any bond, indemnity or guarantee in place for the employer.

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.

The Fund has a formal cessation policy which was last reviewed in November 2013. Full details are available on request.

3.4 Pooled contributions

From time to time the Administering Authority may set up pools for employers with similar characteristics. This will always be in line with its broader funding strategy.

With the advice of the Actuary the Administering Authority allows smaller employers of similar types to pool their contributions as a way of sharing experience and smoothing out the effects of costly but relatively rare events such as 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.

Smaller admitted bodies may be pooled with the letting employer, provided all parties (particularly the letting employer) agree.

Employers who are permitted to enter (or remain in) a pool at the 2013 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 deficit recovery period, 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;

- whether the admission agreement is likely to be open or closed to new entrants.

3.6 Non ill health early retirement costs

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

With the agreement of the Administering Authority the payment can be spread as follows:

Major Employing bodies	- up to 5 years
Community Admission Bodies and Designating Employers	- payable immediately
Academies	- payable immediately
Transferee Admission Bodies	- payable immediately

3.7 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 employees.

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.

3.8 Policies on bulk transfers

The Fund will be treat each case 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;
- The Fund may permit shortfalls to arise on bulk transfers if the Fund employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's Fund contributions to increase between valuations.

4 Funding strategy and links to investment strategy

4.1 What is the Fund's investment strategy?

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

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 (SIP), 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 after each actuarial valuation, and is kept under review annually between actuarial valuations to ensure that it remains appropriate to the Fund's liability profile.

The same investment strategy is currently followed for all employers.

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

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

Therefore, the funding and investment strategies are inextricably linked.

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

In the opinion of the Fund actuary, the current funding policy is consistent with the current investment strategy of the Fund. The asset outperformance assumption contained in the discount rate (see 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 A1).

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

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

4.4 How does this differ for a large stable employer?

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

- Prudence - the Fund should have a reasonable expectation of being fully funded in the long term;
- Affordability – how much can employers afford;
- Stewardship – the assumptions used should be sustainable in the long term, without having to resort to overly optimistic assumptions about the future to maintain an apparently healthy funding position;
- Stability – employers should not see significant moves in their contribution rates from one year to the next, and this will help to 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 2017, it should be noted that this will need to be reviewed following the 2016 valuation.

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 the Chartered Institute of Public Finance and Accountancy (CIPFA) (most recently in 2012) and to its Statement of Investment Principles.

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 made available to all participating employers during April and May 2014 for comment;

b) Comments were requested within 30 days;

c) Following the end of the consultation period the FSS was updated where required and then published following the May 2014 sub-committee meeting.

A3 How is the FSS published?

The FSS is made available through the following routes:

- Published on the website, at www.warwickshire.gov.uk/pensions
- A full copy included in the annual report and accounts of the Fund;
- Copies sent to investment managers and 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 2016.

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, 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 www.warwickshire.gov.uk

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 (SIP) 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;
- prepare and maintain a FSS and a SIP, 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/SIP 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 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 Admission Bodies' 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 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;
- 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.

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 return 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.
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. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.
Pay and price inflation significantly more than anticipated.	The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases. 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.

Risk	Summary of Control Mechanisms
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, express contributions as monetary amounts rather than % of pay and consider alternative investment strategies.
Deteriorating patterns of early retirements	Employers are charged the extra cost of non ill-health retirements following each individual decision.
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 deficit contributions have moved 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 have been 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.

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 (under Regulation 38) between triennial valuations Deficit contributions are 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

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

Appendix D – The calculation of Employer contributions

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

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 future benefits being accrued, referred to as the "future service rate"; plus

b) an adjustment for the funding position of accrued benefits relative to the Fund's solvency target, "*past service adjustment*". If there is a surplus there may be a reduction in the employer's contribution rate. If there is a deficit there will be an increase in the employer's contribution rate, with the surplus or deficit spread over an appropriate period. The aim is to return the employer to full funding over that period. See Section 3 for deficit recovery periods.

The Fund's actuary is required by the regulations to report the *Common Contribution Rate*[1], for all employers collectively at each triennial valuation. It combines items (a) and (b) and is expressed as a percentage of pay; it is in effect an average rate across all employers in the Fund.

The Fund's actuary is also required to adjust the Common Contribution Rate for circumstances which are deemed "peculiar" to an individual employer[2]. It is the adjusted contribution rate which employers are actually required to pay. The sorts of "peculiar" factors which are considered are discussed below.

In effect, the *Common Contribution Rate* is a notional quantity. Separate future service rates are calculated for each employer together with individual past service adjustments according to employer-specific past service deficit spreading and increased employer contribution phasing periods.

D2 How is the Future Service Rate calculated?

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

The future service 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 calculation is on the "ongoing" valuation basis (see Appendix E), but where it is considered appropriate to do so the Administering Authority reserves the right to set a future service rate by reference to liabilities valued on a more prudent basis (see Section 3).

The approach used to calculate each employer's future service contribution rate depends on whether or not new entrants are being admitted. Employers should note that it is only Admission Bodies and Designating Employers that may have the power not to automatically admit all eligible new staff to the Fund, depending on the terms of their Admission Agreements and employment contracts.

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[1] See LGPS (Administration) Regulations 36(5).
[2] See LGPS (Administration) Regulations 36(7).

a) Employers which admit new entrants

These rates will be derived using the “Projected Unit Method” of valuation with a one year period, i.e. only considering the cost of the next year’s benefit accrual and contribution income. If future experience is in line with assumptions, and the employer’s membership profile remains stable, this rate should be broadly stable over time. If the membership of employees matures (e.g. because of lower recruitment) the rate would rise over time.

b) Employers which do not admit new entrants

To give more long term stability to such employers’ contributions, the “Attained Age” funding method is normally adopted. This measures benefit accrual and contribution income over the whole future anticipated working lifetimes of current active employee members.

Both approaches include expenses of administration to the extent that they are borne by the Fund, and include allowances for benefits payable on death in service and ill health retirement.

D3 How is the Solvency / Funding Level calculated?

The Fund’s actuary is required to report on the “solvency” of the whole Fund in a valuation which should be carried out at least once every three years. As part of this valuation, the actuary will calculate the solvency position of each employer.

‘Solvency” is defined to be the ratio of the market value of the employer’s asset share to the value placed on accrued benefits on the Fund actuary’s chosen assumptions. This quantity is known as a funding level.

For the value of the employer’s asset share, see D5 below.

For the value of benefits, 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).

D4 What affects a given employer’s valuation results?

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

- past contributions relative to the cost of accruals of benefits;
- different liability profiles of employers (e.g. mix of members by age, gender, service vs. salary);
- the effect of any differences in the valuation basis on the value placed on the employer’s liabilities;
- any different deficit/surplus spreading periods or phasing of contribution changes;
- the difference between actual and assumed rises in pensionable pay;
- the difference between actual and assumed increases to pensions in payment and deferred pensions;
- the difference between actual and assumed retirements on grounds of ill-health from active status;
- the difference between actual and assumed amounts of pension ceasing on death;
- the additional costs of any non ill-health retirements relative to any extra payments made;

over the period between each triennial valuation.

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.

D5 How is each employer's asset share calculated?

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

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

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

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

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

Appendix E – Actuarial assumptions

E1 What are the actuarial assumptions?

These are expectations of future experience used to place a value on future benefit payments ("the liabilities"). Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits.

Changes in assumptions will affect the measured value of future service accrual and past service liabilities, and hence the measured value of the past service deficit. 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 liability values and lower employer costs. A more prudent basis will give higher liability values and higher employer costs.

E2 What basis is used by the Fund?

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

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

E3 What assumptions are made in the ongoing basis?

a) Investment return / discount rate

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

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

For the purpose of the triennial funding valuation at 31 March 2013 and setting contribution rates effective from 1 April 2014, the Fund actuary has assumed that future investment returns earned by the Fund over the long term will be 1.6% per annum greater than gilt yields 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.

b) Salary growth

Pay for public sector employees is currently subject to restriction by the UK Government until 2016. 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, the salary increase assumption at the 2013 valuation has been set to 1% above the retail prices index (RPI) per annum. This is a change from the previous valuation, which assumed long term growth at RPI plus 1.5% per annum.

c) Pension increases

Since 2011 the consumer prices index (CPI), rather than RPI, has been the basis for increases to public sector pensions in deferment and in payment. This change was allowed for in the valuation calculations as at 31 March 2010. 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 propose a reduction of 0.8% per annum.

d) Life expectancy

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

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

It is acknowledged that future life expectancy and, 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 CMI 2010 model assuming future improvements in life expectancy have peaked and that longer term mortality rates will fall at a rate of 1.25% p.a. for men and women. This is a higher allowance for future improvements than was made in 2010.

The combined effect of the above changes from the 2010 valuation approach, is to add around one year of life expectancy on average. The approach taken is considered reasonable in light of the long term nature of the Fund and the assumed level of security underpinning members' benefits.

e) General

The same financial assumptions are adopted for all employers, in deriving the past service deficit and the future service rate: as described in (3.3), these calculated figures are translated in different ways into employer contributions, depending on the employer's circumstances.

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

Appendix F – Glossary

Actuarial assumptions/basis	The combined set of assumptions made by the actuary, regarding the future, to calculate the value of **liabilities**. The main assumptions will relate to the **discount rate**, salary growth, pension increases and longevity. More prudent assumptions will give a higher liability value, whereas more optimistic assumptions will give a lower value.
Administering Authority	The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".
Admission Bodies	Employers which voluntarily participate in the Fund, so that their employees and ex-employees are **members**. There will be an Admission Agreement setting out the employer's obligations. For more details (see 2.5).
Common contribution rate	The Fund-wide **future service rate** plus **past service adjustment**. It should be noted that this will differ from the actual contributions payable by individual **employers**.
Covenant	The assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term.
Deficit	The shortfall between the assets value and the **liabilities** value. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).
Deficit repair/recovery period	The target length of time over which the current **deficit** is intended to be paid off. A shorter period will give rise to a higher annual **past service adjustment** (deficit repair contribution), and vice versa.
Designating Employer	Employers such as town and parish councils that are able to participate in the LGPS via resolution. These employers can designate which of their employees are eligible to join the Fund.
Discount rate	The annual rate at which future assumed cashflows (in and out of the Fund) are discounted to the present day. This is necessary to provide a **liabilities** value which is consistent with the present day value of the assets, to calculate the **deficit**. A lower discount rate gives a higher liabilities value, and vice versa. It is similarly used in the calculation of the **future service rate** and the **common contribution rate**.
Employer	An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **liabilities** values for each employer are individually tracked, together with its **future service rate** at each **valuation**.
Funding level	The ratio of assets value to **liabilities** value: for further details (see 2.2).

Future service rate	The actuarially calculated cost of each year's build-up of pension by the current active **members**, excluding members' contributions but including Fund administrative expenses. This is calculated using a chosen set of **actuarial assumptions**.
Gilt	A UK Government bond, ie a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but their main use in funding is as an objective measure of solvency.
Guarantee / guarantor	A formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's **covenant** to be as strong as its guarantor's.
Letting employer	An employer which outsources or transfers a part of its services and workforce to another employer (usually a contractor). The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer. A letting employer will usually be a local authority, but can sometimes be another type of employer such as an Academy.
Liabilities	The actuarially calculated present value of all pension entitlements of all **members** of the Fund, built up to date. This is compared with the present market value of Fund assets to derive the **deficit**. It is calculated on a chosen set of **actuarial assumptions**.
LGPS	The Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 101 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
Maturity	A general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.
Members	The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).
Past service adjustment	The part of the employer's annual contribution which relates to past service **deficit** repair.

Pooling	Employers may be grouped together for the purpose of calculating contribution rates, so that their combined membership and asset shares are used to calculate a single contribution rate applicable to all employers in the pool. A pool may still require each individual employer to ultimately pay for its own share of **deficit**, or (if formally agreed) it may allow **deficits** to be passed from one employer to another. For further details of the Fund's current pooling policy (see 3.4).
Profile	The profile of an employer's membership or liability reflects various measurements of that employer's **members**, ie current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.
Rates and Adjustments Certificate	A formal document required by the LGPS Regulations, which must be updated at least every three years at the conclusion of the formal **valuation**. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.
Scheduled Bodies	Types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).
Solvency	In a funding context, this usually refers to a 100% **funding level**, ie where the assets value equals the **liabilities** value.
Stabilisation	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund. Different methods may involve: probability-based modelling of future market movements; longer deficit recovery periods; higher discount rates; or some combination of these.
Theoretical contribution rate	The employer's contribution rate, including both **future service rate** and **past service adjustment**, which would be calculated on the standard **actuarial basis**, before any allowance for **stabilisation** or other agreed adjustment.
Valuation	An actuarial investigation to calculate the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too. This is normally carried out in full every three years (last done as at 31 March 2013), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.

Item 4

Pension Fund Investment Sub-Committee

19 May 2014

The 2013 Actuarial Valuation

Recommendation

That the Sub-Committee note the results.

1 Introduction

1.1 At the meeting of 10 February 2014 the draft results of the 2013 actuarial valuation were presented by the fund actuary.

1.2 Following this meeting the results were finalised and the report issued by the 31 March 2014 statutory deadline.

1.3 This report sets out the outcome of the valuation. The final valuation report in **Appendix A** shows the full results and includes all rates, assumptions and a detailed explanation behind the methodology adopted.

2 Valuation Results

Funding Level

2.1 At 31 March 2013, the fund has a funding level of 77%. The table below gives an analysis of how this was derived alongside a comparison of the 2010 valuation results.

Past Service Position	**31/03/2010 (£m)**	**31/03/2013 (£m)**
Past Service Liabilities	1,328	1,798
Market Value of Assets	1,099	1,379
Surplus / (Deficit)	(229)	(419)
Funding Level	**83%**	**77%**

Warwickshire County Council

Contribution Rates

2.2 The table below summarises the contribution rates required for the next three financial years and how this compares with the previous valuation.

Contribution Rates	31/03/2010 (% of pay)	31/03/2013 (% of pay)
Employer future service rate (incl. expenses)	12.8	19.5
Past Service Adjustment (19 year spread)	4.8	9.6
Total employer contribution rate (incl. expenses)	**17.6**	**29.2**
Employee contribution rate	6.4	6.1
Expenses	0.6	0.6

2.3 The employer contribution rate is a theoretical figure – an average across the whole Fund. In practice, each employer that participates in the Fund has its own circumstances and underlying funding position, giving rise to its own contribution rate requirement. **Appendix A** pages 27 and 28 detail individual employer contribution rates due.

3 Future Funding Plan

3.1 The Pensions Fund's funding plan is set out in the Funding Strategy Statement (FSS). The FSS will be presented at this Sub-Committee meeting.

4 Recommendation

4.1 That the Sub-Committee note the report.

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Item 5

Pension Fund Investment Sub Committee

19 May 2014

Investment Performance

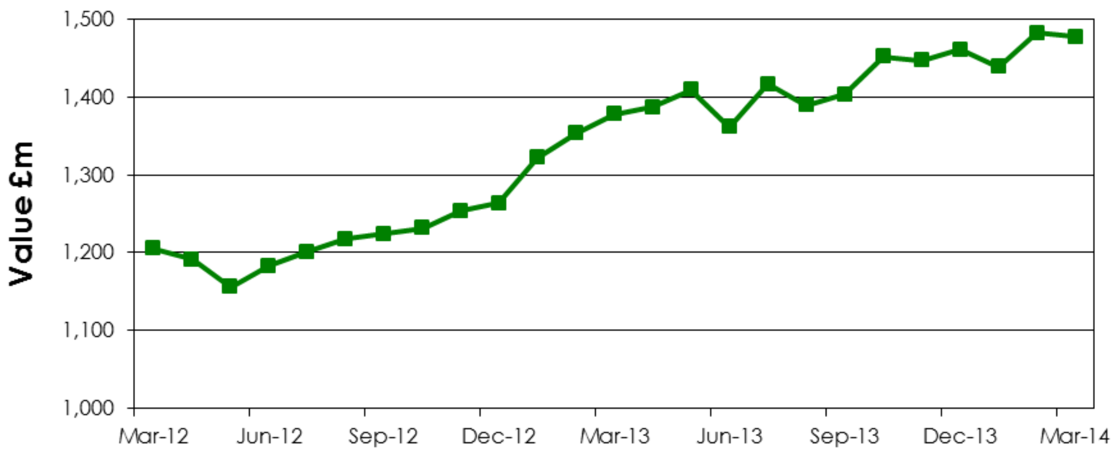
Recommendation

That the Committee notes the fund value and investment performance for the fourth quarter in 2013/14 to 31 March 2014.

1. Fund Value at 31 March 2014

1.1 The fund value was £1,477.6m at 31 March 2014 an increase of 1.2% on the previous quarter as shown in Figure 1.

Figure 1. Total Fund Value Since 30 March 2012



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2. Fund Asset Allocation

2.1 The performance of the Fund against its asset class benchmarks for the quarter ending 31 March 2014 is shown in Table 1.

Table 1: Fund Asset Allocation

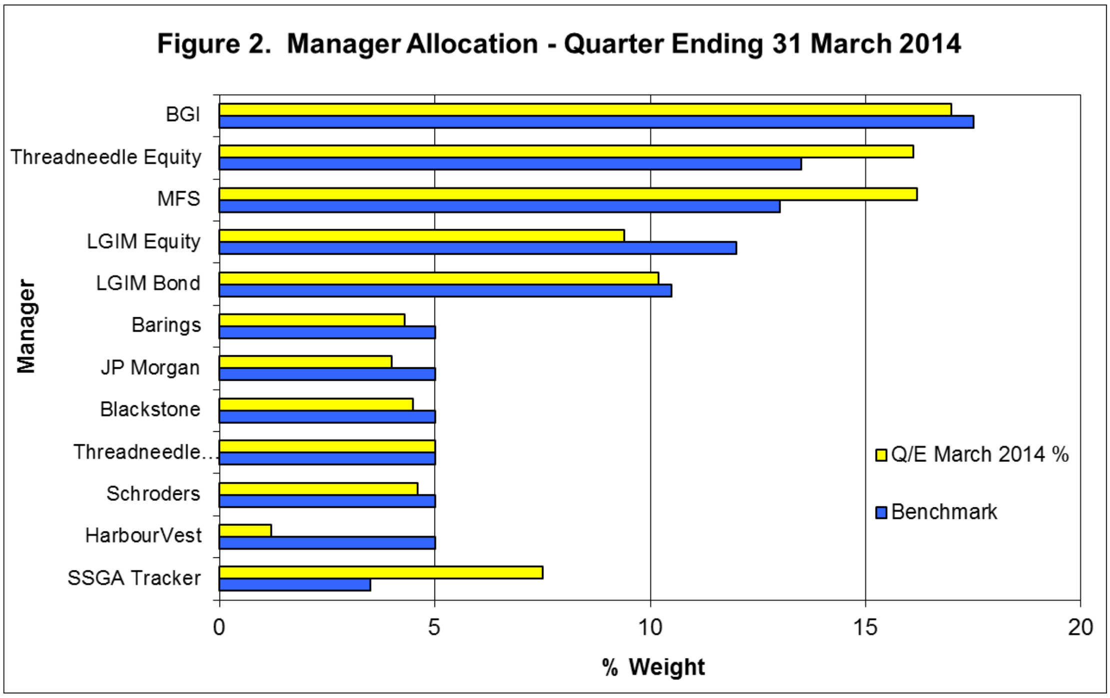
Asset Class		Q/E Mar 2014	Fund policy	Over/under weight
		%	%	%
Equity		**59.60**	**52.50**	**7.10**
	UK	28.70	22.50	6.20
	Overseas	30.90	30.00	0.90
Fixed Income		**16.20**	**17.50**	**-1.30**
	UK corporate bonds	9.40	10.00	-0.60
	UK government bonds	2.20	2.50	-0.30
	UK index linked bonds	4.60	5.00	-0.40
Hedge Funds		**4.50**	**5.00**	**-0.50**
Private Equity		**1.10**	**5.00**	**-3.90**
Property		**9.60**	**10.00**	**-0.40**
Multi Asset Absolute Return		**4.30**	**5.00**	**-0.70**
Absolute Return Bonds		**4.00**	**5.00**	**-1.00**
Cash		**0.70**	**0.00**	**0.70**
Total		**100.00**	**100.00**	**0.00**

2.2 The fund managers' asset allocation against the benchmark for the quarter ending 31 March 2014 is shown in Table 2.

Table 2: Fund Asset Allocation by Manager

Manager	**Q/E March 2014 %**	**Benchmark**	**Variance**
SSGA Tracker	7.5	3.5	4.0
HarbourVest	1.2	5.0	-3.8
Schroders	4.6	5.0	-0.4
Threadneedle Property	5.0	5.0	0.0
Blackstone	4.5	5.0	-0.5
JP Morgan	4.0	5.0	-1.0
Barings	4.3	5.0	-0.7
LGIM Bond	10.2	10.5	-0.3
LGIM Equity	9.4	12.0	-2.6
MFS	16.2	13.0	3.2
Threadneedle Equity	16.1	13.5	2.6
BGI	17.0	17.5	-0.5
Total	100.0	100.0	0.0

2.2 Fund asset allocation against each manager is shown in Figure 2.



3. Fund Performance

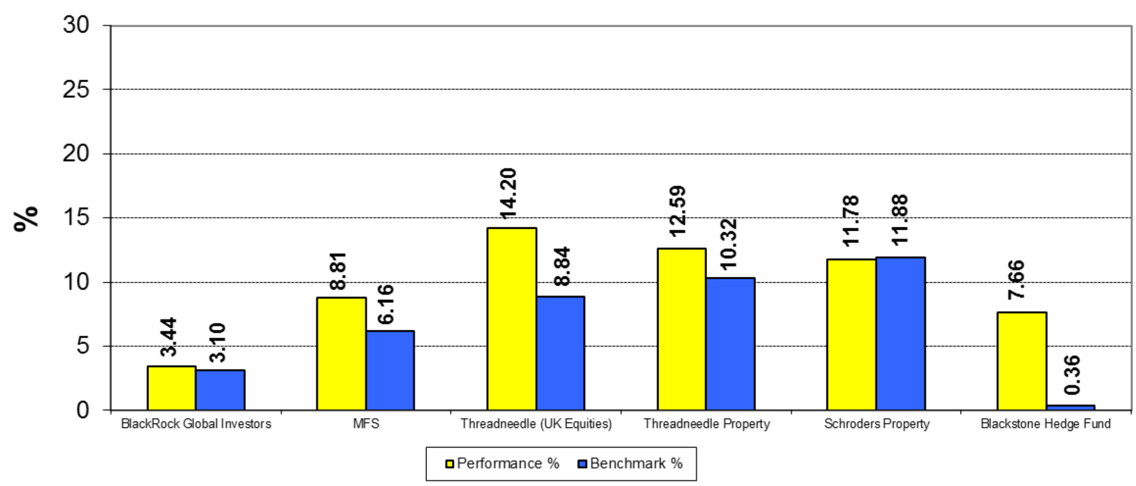
3.1 Overall the fund out-performed its overall benchmark by 0.32%. The performances of managers against their benchmarks for the quarter ending 31 March 2014 were:

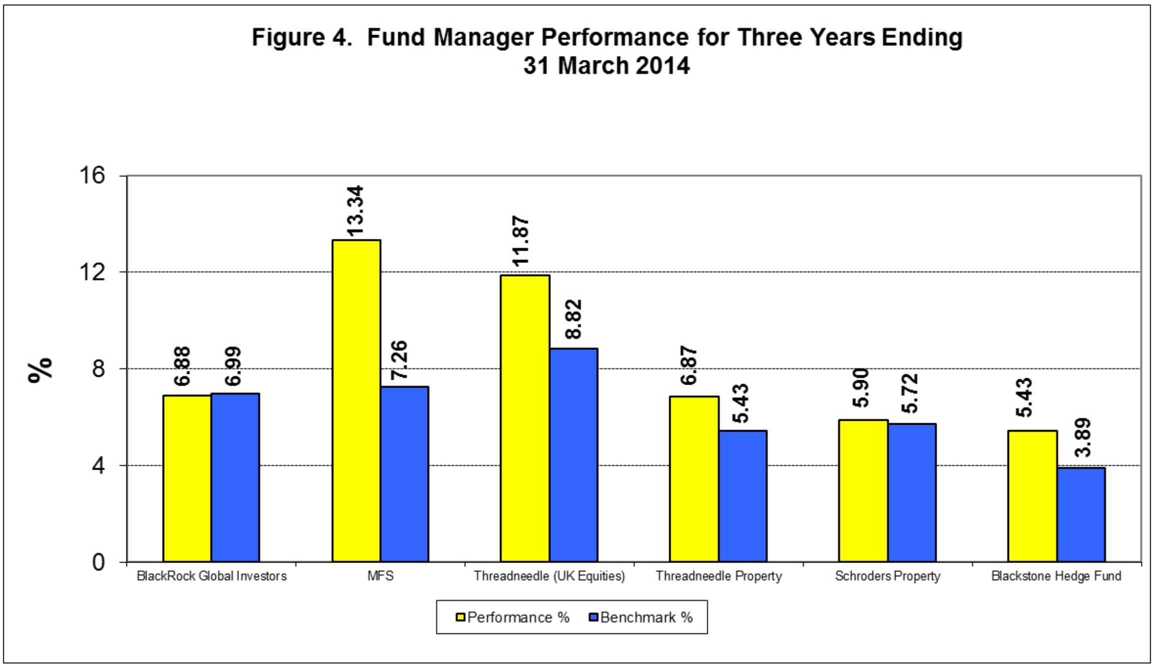
Table 3: Performance by Fund Manager

Manager	Benchmark Measure	Q/E Mar 2014	Benchmark	Variance
		%	%	%
BlackRock Global Investors		0.90		**-0.20**
	BlackRock Benchmark		1.10	
MFS		0.20		**-0.20**
	Global Equity Benchmark		0.40	
State Street Tracker		-0.63		**0.00**
	FTSE All-Share		-0.63	
Threadneedle		1.44		**2.06**
	FTSE All-Share		-0.62	
Legal and General (Global Equities)		1.72		**0.45**
	LGIM Benchmark		1.27	
Legal and General (Fixed Interest)		2.37		**0.00**
	LGIM Benchmark		2.37	
Threadneedle Property		3.39		**0.35**
	Customised Benchmark		3.04	
Schroders Property		2.73		**-0.55**
	Customised Benchmark		3.28	
Blackstone Hedge		1.68		**1.59**
	Customised Benchmark		0.09	
Barings Multi Asset		-0.52		**-0.64**
	Customised Benchmark		0.12	
JP Morgan Strategic Bond		1.69		**1.57**
	Customised Benchmark		0.12	
Total		**1.18**		**0.32**
	WCC Total Fund Benchmark		**0.86**	

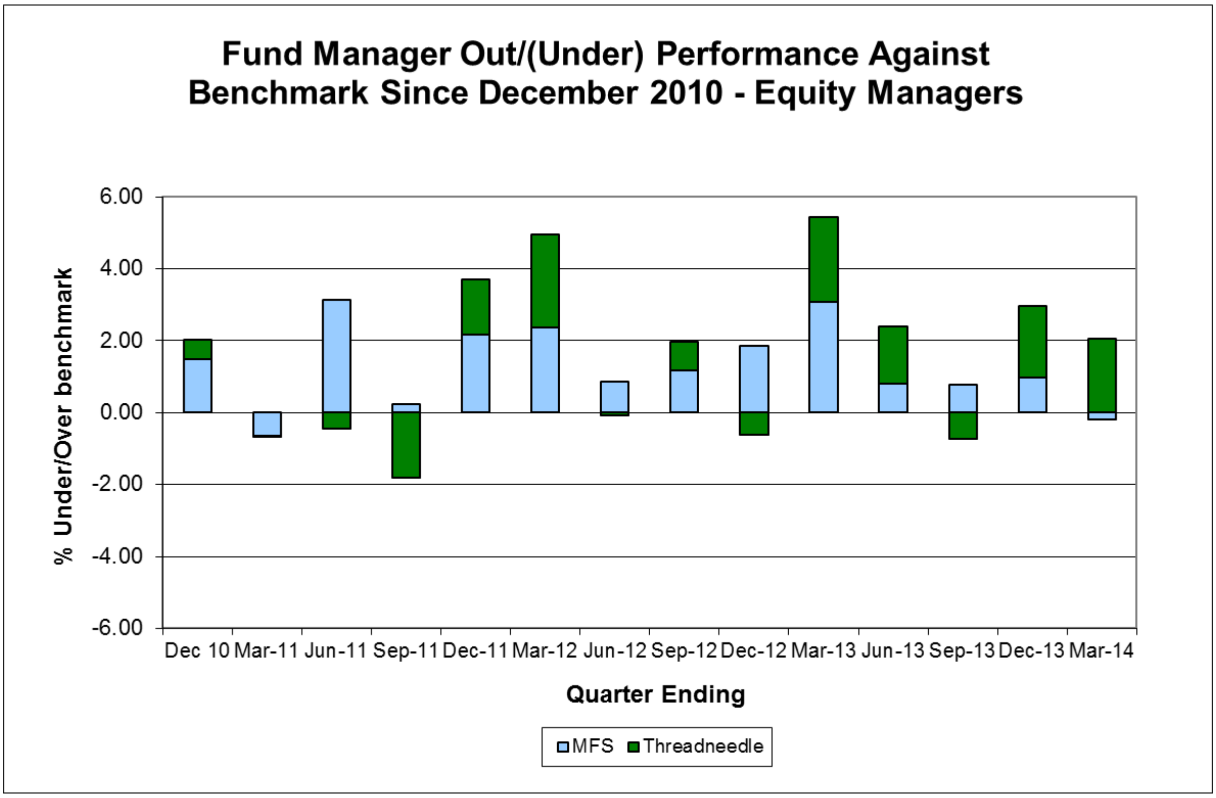
3.2 Annualised return for the fund managers to 31 March 2014 is summarised in Figure 3. The three year annualised return is summarised in Figure 4.

Figure 3. Fund Manager Performance for the Year Ending 31 March 2014





3.3 Equity Manager performances against their benchmarks are summarised in Figures 5.



Warwickshire County Council

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Pension Fund Investment Sub Committee

19 May 2014

Review of Investment Strategy

Recommendation

That the sub-committee discuss the strategic asset allocation of the fund based on the findings from Hymans Robertson.

1 Introduction

1.1 Further to the actuarial valuation carried out as at 31 March 2013, it was agreed that there would be a formal review of the Fund's investment strategy. This is an appropriate time to carry out such a review as the investment consultant has current information on the Fund's membership following the valuation, clarity on the details of the new LGPS Scheme, and confirmation of the contribution strategy being recommended by the actuary.

2. The High Level Strategy

2.1 In order to review the high level investment strategy, the approach known as Asset Liability Modelling (ALM) is used. This enables the consultant to consider the chances of the Fund achieving its long term objectives in conjunction with the associated risks.

2.2 In our modelling, the estimated liabilities of the Fund are taken from the latest actuarial valuation and projected forward the possible evolution of the Fund's assets and liabilities under a range of different scenarios. Within the 5,000 simulations tested, there are a wide range of assumptions around returns for each of the asset classes as well as different levels of future inflation and interest rates. This allows consideration of the likelihood of different funding levels and contribution rates in the future.

2.3 A detailed presentation will be distributed in advance of this meeting and will address the following issues as part of the exercise:-

- Given the combination of the current investment strategy and contribution strategy (with agreed stabilisation measures), what are the chances of meeting the Fund's long term objectives?
- How would those chances be affected by adopting a higher or lower risk investment strategy? What would be the implications for risk in either approach?

- What would be the impact on likely contribution rates should there be any change in the investment strategy?
- Is there a position where reductions in investment risk would be more compelling?
- What is the medium / long term outlook for the Fund's cash flow position?

3. Detailed asset allocation

3.1 Once the high level investment strategy has been agreed in 2.3, the next step will be to look at the asset allocation and investment manager arrangements at the July and November sub-committee meetings.

3.2 Broad areas for consideration will include:-

- The allocation of equities between active and passive management, including some of the newer alternative forms of passive management? Is the current number of managers optimal?
- The allocation to other 'diversifying growth assets' appropriate (infrastructure, hedge funds, multi-asset etc.) Are there other opportunities available to the Fund?
- The current split between fixed income active and passive management and between absolute return and traditional mandates appropriate in the current environment?

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Pension Fund Investment Sub-Committee

19 May 2014

Share Voting

Recommendation

That the Sub-Committee approve the recommendation in 4.1

1 Introduction

1.1 At the meeting of 4 August 2008 it was decided that the Pension Fund approve a policy in respect of shareholder activism and the implementation of a proxy voting system to vote on the Fund's shares. Since this time the funds officers have used this voting system and approved policy to vote on the shares held in our segregated mandates held with Threadneedle Investments (UK equities) and MFS Investment Management (Global equities).

1.2 Our provider for the proxy voting system, Manifest, drafted the best practice governance and voting policy that used recommendations from the Higgs and Smith Reports. There have been subsequent regulatory developments and governance, therefore the original policy needs to be revised to reflect these changes.

2 Changes to the Voting Policy

2.1 The policy has been redrafted to include the new regulations around director's remuneration and the quality of company narrative reporting. Further amendments have been made to the policy to ensure compliance with the UK Governance Code. Also, the Pension Fund signed the Stewardship Code in 2013 which encompasses principles that should also be reflected in the policy.

3 The Proposed Voting Policy

3.1 Officers have engaged with Manifest and drawn up a revised share voting policy for the sub-committee approval. The draft voting policy is shown in **Appendix A**.

4 Recommendation

4.1 That the sub-committee approve the revised share voting policy as attached.

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Appendix A

1 ABOUT THIS DOCUMENT

This document is an executive summary of Warwickshire County Council Pension Fund's approach to investor stewardship and in particular its views on key governance and corporate sustainability issues. These issues include: capital and board structure; board evaluation and refreshment; director remuneration, audit and accountability, and narrative reporting matters.

These high-level principles are underpinned by detailed market-by-market guidelines, which are used as a basis for voting the fund's shares at general meetings.

The fund has appointed a proxy voting agency to assist the fund in the implementation of its policies. Final vote decisions are determined by Fund officers using independent research to support their decision-making. The exception to this is case-by-case investment resolutions, for example take-overs, where the investment manager is consulted before a final decision is made.

Unless otherwise specified, the Fund seeks to adopt a highest common denominator standard to its global voting. Although we recognise that local market standards may vary, our objective is to hold management accountable to the highest possible standards on a consistent basis. The only exception will be where local laws contradict.

2 SHAREHOLDER RIGHTS & RESPONSIBILITIES

2.1 One Share- One Vote

The Fund fully supports the concept of “One share- One Vote” and is not supportive of the creation of share capital with differential voting rights. Companies should therefore disclose the share structure, voting rights and any other rights or limitations attached to each class of shares.

2.2 Shareholder Engagement & Wider Stewardship Activities

The Fund is a signatory to the Stewardship Code and is also a member of the Local Authority Pension fund Forum.

While the fund undertakes its own voting, we seek to involve our fund managers in our stewardship activities and expect them to include stewardship considerations as part of their investment strategy.

As a Code signatory we believe that proper disclosure of our voting records will help companies and other stakeholders including Fund members understand our approach. These records are updated regularly and can be found at www.warwickshire.gov.uk/pensions

3 THE BOARD OF DIRECTORS

3.1 Board Composition, Diversity & Succession

When assessing the quality of investee company boards, WPF takes a balanced approach to understanding board composition which takes account of overall board size, director skills, background and experience.

Diversity brings substantial benefits to companies in terms of skills and competencies. We therefore expect to see a structured and well-articulated approach to board refreshment and succession planning. Diversity is more than simply gender; while not supporting specific gender quotas, we encourage boards to voluntarily achieve a target of at least 30% women on the board and in senior positions and to provide clear explanations of how they are achieving diversity goals.

All companies should have a succession plan and explain their approach towards to the use of executive search firms or “Head-hunters” versus internal talent or “Pipeline” development.

3.2 Director Independence & Commitment

Director independence is generally assessed against the standards set by the UK Corporate Governance Code (‘the Code’), however there are times when a case-by-case approach is required.

Independence on its own is not a sufficient characteristic for a successful appointee, directors should be able to devote the necessary time to the company's affairs. We therefore expect to see full disclosure of directors other outside appointments together with a record of attendance and explanations for non-attendance, which will be considered on a case-by-case basis.

3.3 Board Evaluation

Boards should undertake a formal evaluation of its performance every two to three years under the guidance of an external, independent facilitator. A statement about the results of the evaluation should be included as a separate item in the annual report.

3.4 Chair/CEO

We support the separation of the roles of Chairman and Chief Executive.

Except in rare circumstances, former Chief Executives should not be appointed to the position of Chair. We would expect to see a clear explanation of the reasons and what time horizon the company is looking to for a replacement. The position may be temporary, due to unexpected circumstances, such as illness.

3.5 Director Re-election

Directors are expected to submit themselves for re-election on a regular basis and that boards should not insulate individual candidates.

3.6 Directors' Service Contracts

Companies should fully disclose directors' service contracts or terms of appointment; all contracts should include a notice period of no longer than one year and any exit payments should be clearly disclosed. In particular:

- Severance payments relating to poor corporate performance should not extend beyond basic salary. There should be no entitlement to discretionary payments in these circumstances.

- Contracts should not provide additional compensation for severance as a result of change of control;

- The duty to mitigate should be made a specific contract provision and remuneration committees should consider phased payments in order to fulfil compensation commitments on early termination.

4 SHAREHOLDERS' CAPITAL

Pre-emption rights are a basic shareholder right which can be easily eroded without careful monitoring. We support the principles of the UK's Pre-Emption Group guidelines on dilution which permit up to 5% of share capital to be offered for cash rather than on a rights basis. Existing shareholders should be offered the right of first refusal when a company issues shares exceeding 5% of the existing shares in issue or exceeding a 7.5% threshold in any three-year rolling period, as set out in the Pre-Emption Group's document "Disapplying Pre-Emption Rights: A Statement of Principles", issued in 2006.

Companies should provide explicit assurance that share buybacks will only be exercised in the best interests of all shareholders. This is particularly important where incentive pay may be linked to Earnings per Share performance.

5 AUDIT & ACCOUNTABILITY

5.1 Audit & Accountability

Sound audit and reporting standards are an essential investor protection. Clear presentation of material risks to the business and how they are mitigated is a core requirement. Explanations in relation to changes to accounting practices, restatements or matters of emphasis must be prominent and transparent.

5.2 Audit Committee

Boards should ensure that the relationship with the auditor is appropriately focussed on the protection of the company and not of management. The audit committee, which should be composed of suitably qualified individuals, with a least one designated "Financial Expert", is responsible for ensuring that the auditors offer independent and effective services. Non-audit related work should be minimised to avoid unnecessary conflicts of interest.

5.3 Internal Controls

Oversight and management of risk can be enhanced by the use of an internal audit function. Financial institutions should operate a separate risk committee.

5.4 Audit Partner, Audit Firm Rotation

We encourage competitive tendering for audit every 5-7 years and mandatory rotation after no more than 15 years. Retendering alone is unlikely to safeguard auditor independence. We do not support "Big 4 only" restrictions in tenders or any such requirements by lenders.

6 DIRECTOR REMUNERATION

6.1 Remuneration Committee

The UK Corporate Governance Code provisions on the role and composition of remuneration committees, serves as a benchmark for our approach to committee composition for our UK and global holdings. Remuneration committees should have access to their own independent advice which is not connected with any other services provided to management e.g. audit, HR, board evaluation etc. Non-executive fees and any associated policies, including share ownership policies should also be disclosed.

In their reporting to shareholders, committees are encouraged to explain their approach to the discretionary powers they exercise over the various components of executive pay. Blanket discretion is not supported.

6.2 Remuneration Policy & Disclosure

Remuneration policies should be clear and straightforward so as to facilitate understanding of how management is incentivised to achieve long term shareholder value and support the success of the company.

- Pay for Performance

We expect to see a significant proportion of executive pay linked to corporate performance which is clearly and meaningfully aligned with strategy and positive shareholder value. Financial metrics and ratios such as earnings per share or total shareholder return on their own are unlikely to be sufficient measures of strategy. We therefore we wish to understand the relationship between pay and Key Performance Indicators (KPI's); business and market risk; and how these support long-term, sustainable returns. Sustainability or "extra-financial" criteria which have a material business impact are encouraged as part of the KPI's.

- Variable or Performance-Related Pay

Companies should clearly disclose the performance targets used in any variable pay plans (Annual Bonus, Short-Term Incentives or Long-term Incentives). Where commercial sensitivity prevents forward disclosures, we expect to see retrospective disclosure. The technical analysis of variable pay schemes is provided by our research provider and takes account of global and market best practices.

- Recruitment Payments

We recognise that companies may need flexibility in order to be able to recruit new executive directors. We expect to see clear disclosure relating to the maximum variable pay which can be paid to incoming directors. Such payments should exclude compensation for variable pay forgone at the previous employer. Transaction related payments should be subject to demanding performance conditions.

- Change of Control

There should be no automatic waiving of performance conditions for either change of control or capital reorganisations. Any consequential early vesting should be time pro-rated.

- Dilution

Share-based remuneration plans have the potential to dilute shareholders. For this reason share plans should not exceed 10% of the ordinary issued share capital in any rolling 10 year period.

- Claw-backs

The remuneration policy should disclosure clearly what claw-back provisions have been made and in particular their scope. The remuneration committee should have sufficient flexibility to operate the policy rather than simply tying clawback to specific events such as financial restatements, for example.

7 SUSTAINABILITY REPORTING

7.1 Responsibility & Disclosure

There is strong evidence that demonstrates that companies with a long-term sustainable approach to their management outperform their peers. We therefore encourage our companies to describe their approach to sustainability in the widest possible sense and explain how their policies align with long- term corporate strategy. The board of directors should be directly responsible for sustainability considerations.

7.2 Sustainability Risk Reporting

We strongly support transparent and understandable sustainability risk reporting in the context of how relevant and material risk impact their business strategy.

7.3 Employment, Health and Safety

Poor employment practices present significant operational and investment risks for companies. We expect management to develop good employment practices across their organisation that are linked to sustainable corporate prosperity and thus investment value.

7.4 Political Donations

Political donations are considered on a case-by-case basis according to jurisdiction, however as a general rule we do not support shareholders’ funds being used for party political donations.

8 DETAILED VOTING PROCEDURES

In addition to these high level principles, the Fund maintains detailed voting procedures on a market by market and issue by issue basis. These are maintained by our service provider on behalf of the fund and are reviewed on a regular basis, at least annually to ensure that our procedures are consistent with local laws and best practices.

The fund aims to cast its votes on an informed and pragmatic basis having given due consideration to the specific circumstances of the company and the disclosures given to shareholders. Companies are encouraged to provide transparent explanations which explain and justify their reasons for non-compliance with standards. In cases where there is insufficient information or unduly harsh voting deadlines, the fund reserves the right to withhold votes on all resolutions.

Pension Fund Sub-Committee

19 May 2014

Directions Order / Fair Deal

Recommendations

(1) That the Sub-Committee note that support staff at academies, the police authority (crime commission) and colleges of further education are now protected with regard to LGPS membership if their service is outsourced to a private contractor.

(2) The Sub-Committee agree to the admission of contractors to the WCC Pension Fund where support staff in the categories mentioned in Recommendation 1, are transferred to an alternative provider and that the Strategic Director of Resources and Head of Finance are satisfied that the appropriate guarantees for the admission of the contractor are in place.

1.0 Background

1.1 At the May 2012 meeting of the Board, it was noted that support staff employed by an academy were not protected for future membership of the Local Government Pension Scheme (LGPS) if the service they provided was outsourced to a private contractor. This was because academies are not considered to be a Best Value Authority and therefore not covered by the provisions of the Directions Order issued under Section 101 of the Local Government Act 2003, which protects the pension rights of staff who are outsourced from the service of a best value authority.

1.2 Although the provisions of the Directions Order has not been changed the Government, by way of the Fair Deal Policy, has now confirmed that staff employed by academies, police authorities and colleges of further education should now retain access to the LGPS if their service is outsourced to a private contractor.

2.0 The Directions Order

2.1 Where the Directions Order applies, the transferred staff should be provided with continued access to the LGPS (via an admissions agreement) or access to a broadly comparable pension scheme.

2.2 A broadly comparable pension scheme is usually determined by the Government Actuary's Department or by the Fund's Actuary and will offer transferred LGPS members with a pension scheme with benefits broadly comparable to those in the LGPS.

3.0 Fair Deal

3.1 The original Fair Deal policy, Staff Transfers from Central Government: A Fair Deal for Staff Pensions, was published by HM Treasury in June 1999 and covered staff who were compulsorily transferred from the public sector, the new employer (the contractor) was to give access to an occupational pension scheme broadly comparable to the public sector scheme they were leaving or continued access to that public sector scheme.

3.2 Importantly, staff employed by local authorities (best value authorities), were covered by the Directions Order which did not cover academies, police authorities and colleges.

3.3 Fair Deal has now been extended to cover the above organisations and although Fair Deal is not compulsory there is an expectation that support staff employed at academies, police authorities and colleges to receive the same protection as those employed by a local authority.

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