Pension Fund Investment Sub-Committee

21 July 2014

Agenda

The Pension Fund Investment Sub-Committee will meet at **Northgate House Conference Room, Warwick** on **21 July 2014** at **10:00am**

1. General

(1) Appointment of Chairman

(2) Appointment of Vice Chairman

(3) 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.

(4) Minutes of the previous meeting and matters arising

2. Changes to the Local Government Pension Scheme – Policy discretions

3. Review of Investment Strategy

4. Funding Update

5. Rugby Borough Council Cleaning Contract

6. Governance

EXEMPT ITEMS

7. 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'.

8. (Exempt) minutes of the meeting held on 19 May 2014

9. Any other items

Which the Chair decides are urgent.

JIM GRAHAM
Chief Executive
Shire Hall
Warwick

Membership of the Pension Fund Investment Sub-Committee
Councillors John Appleton, Sara Doughty, Bill Gifford, John Horner, and Brian Moss

For general enquiries please contact Sally Baxter:
Tel: 01926 412323
Email: sallybaxter@warwickshire.gov.uk

Minutes of the Pension Fund Investment Sub-Committee meeting held on 19 May 2014

Present:

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

Officers
Sally Baxter, Democratic Services Officer
John Betts, Head of Finance
Neil Buxton, Pensions Services Manager
Mathew Dawson, Treasury and Pension Fund Manager
Vicki Forrester, Principal Accountant - Revenue
John Galbraith, Senior Solicitor, Pension Fund Services
Kate Hiller, Solicitor
Andrew Lovegrove, Head of Corporate Financial Services

Invitees
Robert Bilton, Hymans Robertson
Peter Jones, Independent Investment Advisor
Paul Potter, Investment Advisor, Hymans Robertson
Paul Hewitt, Manifest

1. General

(1) Apologies

None.

(2) Disclosures

Councillor Sara Doughty declared a non-pecuniary interest in items 11 – 13 in so far she was a Member of Nuneaton and Bedworth Borough Council.

(3) Minutes of the previous meeting

The minutes of the meeting held on 10 February 2013 were agreed as a true record.

Neil Buxton informed the committee that the membership had increased and there were now 16,300 active members of the Local Government Pension Scheme.

2. Infrastructure Managers

2.1 Mathew Dawson provided an overview of the process undertaken to identify and appoint infrastructure fund managers. Following the interviews held on 20 March 2014, it was decided that the infrastructure fund would be £55m and the fund would be split to invest in a fund of funds and a single manager.

2.2 The single fund selected was the Standard Life Capital Infrastructure which would run for an initial period of 12 years managing between 6-8 assets with Warwickshire investing £20m. The fund of funds manager selected was Partners Group Global Infrastructure 2014 which would be in place for 12 years, commencing from August 2014, and would invest in primary, secondary and direct investments. Warwickshire would invest £35m into this fund and Blackrock, the funds transition manager, would be asked to manage the transfer of assets.

2.3 Further consideration regarding the asset allocation would be presented to the committee in July as part of the Hymans review of the fund's investments.

2.4 Clarification as to the distinction of the two funds was provided and it was acknowledged that the committee had agreed that a 'hybrid' between the two would be implemented.

2.5 Resolved

That the Pension Fund Investment Sub-Committee approves the current position with regard to the ongoing fund manager appointment process.

3. Funding Strategy Statement

3.1 Richard Warden, Hymans, introduced the Funding Strategy Statement (FSS) and explained that in accordance with Local Government Pension Scheme Regulations, the FSS would be published and guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) would mean that a consultation with appropriate persons would be undertaken.

3.2 The FSS would provide an overview of all funding decisions made by the Fund within the valuation year. Richard Warden explained the contents of the FSS to the committee which included the funding objectives, the employer contribution rate setting and the risk and control mechanisms.

3.3 With regard to Community Admission Bodies (CAB), it was explained that the Administering Authority would be able to vary the discount rate applied to set the employers contribution rate. This aimed to protect other employers in the fund by helping the employer to achieve full funding before the agreement terminates or the last active member leaves.

3.4 It was acknowledged that by using a discount rate set equal to guilt yields which were currently repressed, it would be difficult for CAB's coming to the end of their agreements. In total, there was four CAB's that were members of the LGPS and each were treated separately.

3.5 Following a question from the committee, John Betts, Head of Finance, commented that the FSS provided a good overview of the funding process and would be invaluable when consulting employers in the fund.

3.6 It was identified that the numbers of School's converting to Academy status was increasing. Therefore the impact of deferred pensions before schools became academy status could potentially impact upon the fund due to the shared risk. This would need to be monitored.

3.7 Resolved

That the Pension Fund Investment Sub- Committee approves the Funding Strategy Statement.

4. The 2013 Actuarial Valuation

4.1 Andrew Lovegrove, Head of Corporate Financial Services, explained the final position of the 2013 Actuarial Valuation. All employers had agreed to pay the contribution rates contained in the report for the next three financial years.

4.2 It was identified that some confusion had been experienced with regard to the LGPS and Warwickshire County Council. Mechanisms such as different letter headed paper for LGPS correspondence were being considered to help employers understand the distinction between the fund and Warwickshire County Council.

4.3 Following discussions with employers, Warwickshire County Council were considering how employers could meet increased contribution rates in particular, those that were due to retire.

4.4 The committee was advised that a number of employers had indicated that they would struggle to meet the contribution rates therefore Warwickshire County Council would be providing assistance. Academies had accepted the contribution rates and were aware that they would be required to meet the rates. With regard to charitable organisations and Community Admission Bodies, it was acknowledged that a consistent approach should be taken and discussions in order to provide suitable support for community organisations should be undertaken with Heads of Service.

4.5 In response to questions from the committee it was confirmed that information and the contribution rates were published and available to view on the Warwickshire LGPS website. It was reported that the past service liability number had decreased therefore was an improvement to the fund and the liability number trend had also decreased in response to the improvement in gilt yields. Paul Potter, Hymans, explained that the expectation was that assets and gilt yields would increase and liabilities would decrease.

4.6 Resolved

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

5. Investment Performance

5.1 Mathew Dawson, Treasury and Pension Fund Manager, provided an overview of the fund value and investment performance for the fourth quarter in 2013/14 to 31 March 2014.

5.2 He reported that the fund value had increased by 1.2% on the previous quarter and was valued as £1,477.6m at 31 March 2014. Information regarding the fund asset allocation including allocation by manager, was explained and analysis of the Fund against its asset class benchmarks was discussed.

5.3 It was reported that the Fund performance had out-performed its overall benchmark by 0.32%. Overall, Fund Managers had provided a good annual performance and Equity Managers had increased their performance, against benchmarks, with value added per quarter since December 2010 – March 2014.

5.4 It was noted that the investments had performed well and this had been achieved by active targeting.

5.5 Resolved

That the Pension Fund Investment Sub-Committee notes the fund value and investment performance for the fourth quarter in 2013/14 to March 2014.

6. Review of Investment Strategy

6.1 Paul Potter, Hymans Robertson, introduced the review of the investment strategy and distributed copies of the presentation to the committee. Asset Liability Modelling (ALM) approach was used to review the high level investment strategy which involved considering the chances of the Fund achieving its long term objectives in conjunction with the associated risks.

6.2 In reviewing the high level investment strategy, the estimated liabilities of the Fund extracted from the latest actuarial valuation and projected forward to consider what the Fund’s assets and liabilities could look like, under various different scenarios. 5,000 simulations were tested which include a number of assumptions for the different asset classes, such as different levels of future inflation or deflation, interest rates and increase of salaries which would affect the contribution rates. This provides the basis that is considered when trying to ascertain the likelihood of different future funding levels and contributions.

6.3 A number of key assumptions were applied to the Fund’s which the committee required clarification. It was clarified that local authorities may be losing personnel but they may transfer to another employer within the Fund therefore would potentially remain in the LGPS therefore this had been applied as an assumption. Gilt yields had been assumed to increase to more ‘normal’ levels which implied higher funding levels over the next 20 years.

6.4 With regard to cash flow and access to income, it was explained that there was sufficient funds to meet demand between now and 2025 but this was only the case if new entrants to the Fund were admitted. The disposable of assets should be considered if no new entrants were admitted.

6.5 The contribution strategy was in place and would assist the funding objective within the 19 years’ time frame. The contribution rates had increased and agreement across the fund would provide stabilisation. New entrants would have the opportunity to look at the strategy therefore they would be required to be in agreement before entering into the Fund.

6.6 The current target asset allocation was discussed and the modelling of alternative investment strategies and the range of outcomes of the five models on the projection of funding levels at 2033. In conclusion, by increasing growth with the current contribution strategy, more risk was associated with the projection of funding levels for 2033. The probability of the Fund achieving its target at 2033 and assuming a fixed contribution rate decreased if 65% and above growth was used.

6.7 It was advised that the current investment strategy and current contribution strategy would give the Fund a good chance of reaching its target. Peter Jones, Independent Investment Advisor, suggested that by de-risking the Fund at 77% would have implications on the gilt yield because the analysis was based on the assumption that gilt yields would increase to 'normal' levels over a 20 year period. The advice would be provided to other authorities and this could lead to a 'ceiling' effect on gilt yields.

6.8 Other types of investments was discussed by the committee such as Infrastructure investment, to stabilise the Fund.

6.8 If the fund was to consider a strategy incorporating de-risking the Fund, consideration would need to be given to employers in the Fund that have lower levels of funding. Further analysis would be provided at the next meeting of the Pension Fund Investment Sub-Committee scheduled for July. The Chair advised the committee to consider potential issues with the strategy, in preparation for the next meeting.

6.9 Resolved

That the Pension Fund Investment Sub-Committee notes the strategic asset allocation of the fund based on the findings from Hymans Robertson and will receive more information at the next scheduled meeting of the committee.

7. Share Voting Policy

7.1 Paul Hewitt, Manifest, explained that since the implementation of the proxy voting system, provided by Manifest, additional regulatory and governance arrangements had been implemented therefore the policy would require updating to reflect these changes.

7.2 The policy was divided into seven principles;

- Shareholder rights and responsibilities,
- The Board of Directors,
- Shareholders' Capital,
- Audit and Accountability,
- Director Remuneration,
- Sustainability Reporting ; and
- Detailed Voting Procedures.

7.3 The new guidelines were relevant mainly to Shareholder rights and responsibilities in so far the policy allows for analysis of best practice and compliance. A specific policy vote regarding Director Remuneration allowed for greater transparency and accuracy when voting and greater detail of the remuneration arrangements.

7.4 Paul Hewitt explained that the share plan of 10% was over any rolling ten year period thus on average, the percentage was not that high. Employees would receive payment in the form of shares to align with shareholders. It was important to note that all means of obtaining shares was subject to shareholder approval.

7.5 Sustainability reporting in particular within a company was important to analyse management arrangements. Companies were encouraged to explain their approach to sustainability in the widest possible sense and explain how their policies align with long-term corporate strategy. This would include risk reporting and would also be incorporated into accounting. The committee noted that that there was now an expectation that that companies would take an active interest in civil society.

7.6 With regard to political donations, the committee suggested that the policy should state that political donations were not supported. However, it was explained that this was a general rule and was in place to cover all legal definitions.

7.7 The recommendation before committee was considered to be in line with the long-term objectives of the fund and the voting policy's general principles would work alongside these objectives and allow for flexibility.

7.8 The committee requested that a progress report on Share Voting be provided at a future meeting. It was clarified that the policy was in the public domain.

7.9 Manifest was asked to provide timely reports. It was acknowledged that the Share Voting Policy report had been deferred from a previous meeting of the committee because it was not made available in time for consideration.

7.10 Resolved

That the Pension Fund Investment sub-Committee approves the revised Share Voting Policy.

8. Directions Order/ Fair Deal

8.1 Neil Buxton, Pension Services Manager, explained that the Fair Deal Policy confirmed that staff employed by academies, police authorities and colleges of further education, would retain access to the Local Government Pension Service (LGPS) if their service was outsourced to a private contractor. It was noted that the provisions within the Directions Order had not changed.

8.2 The Directions Order, where applicable, provides that transferred staff should be provided with access to the LGPS (via an admission agreement) or access to a broadly comparable pension scheme, determined by the Government Actuary's Department or by the Fund's Actuary.

8.2 Resolved

i) That the Pension Fund Investment Sub-Committee notes 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 and;

ii) That the Pension Fund Investment Sub-Committee agrees to the admission of contractors to the Warwickshire County Council Pension Fund where support staff in the categories mentioned above, are transferred to an alternative provider and that the Strategic Director of Resources and the Head of Finance are satisfied that the appropriate guarantees for the admission of the contractor are in place.

9. Exempt Items – Reports containing Confidential or Exempt Information

9.1 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.

10. Exempt Minutes of the meeting of the Pension Fund Investment Sub Committee – 10 February 2014

10.1 The Pension Fund Investment Sub-Committee agreed the exempt minutes of the meeting held on 10 February 2014 as a true and accurate record.

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

11.1 Andrew Lovegrove, Head of Financial Services, presented the report and advice was provided by John Galbraith, Senior Solicitor, and Kate Hiller, Solicitor, as per the exempt minutes.

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

12.1 Andrew Lovegrove, Head of Financial Services, presented the report. Consideration was given to the report, as per the exempt minutes.

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

13.1 Andrew Lovegrove, Head of Financial Services, presented the report. Consideration was given to the report, as per the exempt minutes.

14. (Exempt) Warwickshire County Council Children's Centres

14.1 Neil Buxton, Pension Services Manager, presented the report. Consideration was given to the report, as per the exempt minutes.

15. Any other items

None.

The Sub Committee rose at 12.35pm

……………………………………….
Chair

Pension Fund Investment Sub-Committee

21 July 2014

Changes to the Local Government Pension Scheme - Policy discretions

Recommendation

That the Pension Fund Investment Sub- Committee approves the administration policies for the Pension Fund attached at Appendix A.

1.0 Background

1.1 The introduction of the Local Government Pension Scheme Regulations 2013 and the Local Government Pension Scheme Regulations (Transitional Provisions and Savings) Regulations 2013 both effective from 1 April 2014, make it necessary for the County Council, in its' capacity as the Administering Authority and Employing Authority (as defined in accordance with the pension scheme regulations) to review the policies in place for certain discretions allowed for by the regulations.

1.2 This report is specifically concerned with the discretions allowed for the Pension Fund.

2.0 Local Government Pension Scheme(LGPS) 2014

2.1 The 1st April 2014 saw the introduction of LGPS 2014 and a radical change to the provisions of the Local Government Pension Scheme.

2.2 These changes were brought about following the review of public sector pension schemes undertaken by Lord Hutton. The main changes are:

- The retention of a defined benefit pension scheme.
- For membership from 1 April 2014, the introduction of a career related pension scheme (CARE) with the benefit entitlement accrued based on pensionable pay received during the year rather than accrued service and final pay.
- An improved accrual rate of 1/49th of pay.
- Individual pension accounts to be adjusted annually in line with prices
- Saving provisions for membership accrued prior to the introduction of LGPS 2014.
- The introduction of a two year vesting period for an entitlement to a benefit.
- Saving provisions for members who on 1 April 2012 were within ten years of retirement.
- The retention of final salary for benefits accrued prior to 1 April 2014.

- The retention of the current ill-health provisions.
- The retention of immediate payment of a benefit on being made redundant or on business efficiency if the member has attained age 55.
- The ability for members to choose to retire from age 55 and receive payment of their benefit, albeit reduced.
- An alignment of the scheme's retirement age with state retirement age for benefits accrued under LGPS 2014.
- A review of contribution bandings which will see higher paid scheme members pay a higher contribution with lower paid members paying a lower contribution.
- Pensionable pay to include non-contractual payments (e.g. overtime) which were previously treated as non-pensionable.
- The ability for members to enhance their pension provision by purchasing up to an extra £6,500 per annum.
- The introduction of a 50/50 plan whereby members may elect to pay a reduced contribution (50%) and reduce their personal benefit for that period to 50% without affecting death in service or ill-health benefits.
- Protection for members who's service is transferred to an external provider.
- A costing umbrella to ensure that the future cost of the Scheme is maintained equitably between members and employers.
- Benefits in payment and deferred benefits to be increased in line with the consumer prices index (CPI).
- A review of the governance of the Scheme.

3.0 Discretions

3.1 Appendix A provides a full list of discretions and proposed policies. The schedule shows where there are current policies in place and where there is a new provision the proposed policy.

4.0 Communications

4.1 Treasury and Pensions is liaising with all Fund employers about the employer discretions and policies required by the Scheme regulations.

	Name	**Contact Information**
Report Author	Neil Buxton, Pension Services Manager	neilbuxton@warwickshire.gov.uk 01926 412195
Head of Service	John Betts, Head of Finance	johnbetts@warwickshire.gov.uk 01926 412441
Strategic Director	David Carter, Strategic Head of Resources	davidcarter@warwickshire.gov.uk 01926 412564

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

Regulation	Administering Authority Discretion	Pension Fund Policy
16(1).	Whether to turn down a request to pay Additional Pension Contributions / Shared Cost Additional Pension Contributions (APC / SCAPC) over a period of time where it would be impractical to allow such a request (e.g. where the sum being paid is very small and could be paid as a single payment).	**Proposed policy:** Payments of £50 or less the Pension Fund will require payment by way of a single payment.
16(10).	Whether to require a satisfactory medical before agreeing to an application to pay an APC / SCAPC. Whether to turn down an application to pay an APC / SCAPC if not satisfied that the member is in reasonably good health.	**Proposed policy:** a) The Pension Fund will not require a satisfactory medical where the APC / SCAPC is in respect of reinstating a period of unpaid leave. b) The Pension Fund will require the completion of a medical questionnaire by the member's GP where the APC / SCAPC is in respect of purchasing additional pension.
17(12).	Decide to whom any AVC / SCAVC monies (including life assurance monies) are to be paid on death of the member.	See **Trans Regs 17(5) to (8) & Reg 40(2), Reg 43(2) & Reg 46(2) & Reg 17(12) above.** below
Transitional Regs 10(9).	Decide, in the absence of an election from the member within 12 months of ceasing a concurrent employment, which ongoing employment benefits from the concurrent employment which has ceased should be aggregated (where there is more than one ongoing employment).	**Proposed policy:** Determine which is the most beneficial for the member.

PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

30(8)*	Whether to waive, in whole or in part, actuarial reduction on benefits paid on flexible retirement. (Policy required by the Administering Authority where the employer has become defunct)	**The Pension Fund's existing policy is:** Consideration will be given to waive the actuarial reduction to the benefits where the member had to give up work to provide for a chronically ill spouse or partner.
30(8)*	Whether to waive, in whole or in part, actuarial reduction on benefits which a member voluntarily draws before normal pension age. (Policy required by the Administering Authority where the employer has become defunct).	**The Pension Fund's existing policy is:** Consideration will be given to waive the actuarial reduction to the benefits where the member had to give up work to provide for a chronically ill spouse or partner
68(2)	Whether to require any strain on the Fund costs to be paid "up front" by employing authority following payment of benefits under Reg 30(6) (flexible retirement) Reg 30(7) (redundancy / business efficiency) or waiver (in whole or in part) under Reg 30(8) of any actuarial reduction that would otherwise have been applied to benefits which a member voluntarily draws before normal pension age or to benefits drawn on flexible retirement.	**Proposed policy:** In accordance with the Fund's existing Funding Strategy Statement, with the agreement of the Administering Authority can be spread as follows: • Major employing bodies – up to 5 years. • Community Admission Bodies and Designating Employers – payable immediately. • Academies – payable immediately. • Transfer Admission Bodies – payable immediately.

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

Trans Regs Sch2 para2(2)*	Whether as the 85 year rule does not automatically apply to members who would otherwise be subject to it and who choose to voluntarily draw their benefits on or after age 55 and before age 60, to switch the 85 year rule back on for such members. Where the employer does not do so if the member has already met the 85 year rule the members benefits are to be reduced in accordance with actuarial guidance issued by the Secretary of State (with benefits from any pre1 April 2008 membership for member who will not be 60 or more on 31 March 2016, and benefits from any pre 1 April 2016 for members who will be 60 or more on 31 March 2016 which would not normally be subject to an actuarial reduction nonetheless being subject to a reduction calculated by reference to the period between the date the benefits are drawn and age 60). If the member has not already met the 85 year rule the members benefits are to be reduced in accordance with actuarial guidance issued by the Secretary of State (with the reduction on that part of the members benefits subject to the 85 year rule being calculated by reference to the period between the date the benefits are drawn and age 60 or the date of attaining the 85 year rule, whichever is the later).	Under the current regulations, a member who benefits under the protections afforded under the rule of 85 cannot retire without the agreement of their employer. If the employer agrees to their retirement because there is no actuarial reduction (or a partial reduction depending the members age) and therefore the employer incurs a cost for allowing retirement between age 55 and 60. LGPS2014 allows a member protected by the rule of 85 to retire early and suffer a reduction of benefits previously protected. This discretion allows the employer to turn-on the 85 year rule and effectively have in place the protections currently afforded to these members. **Proposed policy:** To “switch on” the rule of 85 protections thereby retaining the pre 1 April 2014 position but to “switch off” the protection if a member wishes to retire early and suffer the actuarial reduction to their benefit entitlement.

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

Trans Regs Sch2 para2(3)*	Whether to waive on compassionate grounds, the actuarial reduction applied to benefits from pre 1 April 2014 membership where the employer has "switched on" the 85 year rule for a member voluntarily drawing benefits on or after age 55 and before age 60. (Policy required by the Administering Authority where the employer has become defunct).	**The Pension Fund's existing policy is:** Consideration will be given to waive the actuarial reduction to the benefits where the member had to give up work to provide for a chronically ill spouse or partner.
Trans Regs Sch2 para 2(5)	Whether to require any strain on Fund costs to be paid "up front" by employing authority following waiver of actuarial reduction under Trans Regs Sch 2 para 2(3)	**Proposed policy** Because the employer is releasing benefits on compassionate grounds (e.g. the member has had to give up work to care for a chronically ill spouse or partner) it seems perverse to require payment of actuarial strain up front and thereby introduce a financial aspect to the decision making. Therefore, the Pension Fund does not require payment up front and is prepared for the cost to be subsumed as part of the subsequent triennial valuation. However, where the employer is releasing the benefits for reasons other than those described above (e.g. for financial reasons) the Fund will require payment of the strain "up front".
34(1).	Whether to commute small pension.	**The Pension Fund's existing policy is:** To allow the commutation of small pensions provided the member satisfies HMRC requirements.

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

Trans Regs 17(5) to (8) & Reg 40(2), Reg 43(2) & Reg 46(2) & Reg 17(12) above.	Decide to whom death grant is paid.	**The Pension Fund's existing policy is:** That Treasury and Pensions make payment to the nominee unless it is apparent that the nomination may no longer be valid (i.e. that the nominee may have separated or divorced since the nomination was made or other exceptional circumstances). If no nomination has been made or the nomination is no longer valid payment is made as follows, (in this order of priority): • to the spouse or partner upon production of evidence of marriage or partnership or, • any person appearing to the authority to have been his (her) relative or dependant at any time or, • to their personal representatives or, • if there is no evidence of marriage or partnership or of any persons appearing to be a relative or a personal representative, payment will be made to the Estate. If the nominee is a minor, payment is made to a trust fund in respect of the nominee. In the event of a potential dispute, the Administering Authority will gather relevant information to present to the Director of Resources to make an informed decision regarding the distribution of the amount due.

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

49(1)(c)	Decide, in the absence of an election from the member, which benefit is to be paid where the member would be entitled to a benefit under 2 or more regulations in respect of the same period of Scheme membership.	**Proposed policy:** Determine which is the most beneficial for the member.
65.	Decide whether to obtain a new rates certificate if the Secretary of State amends the regulations as part of the "cost sharing" under Reg 63.	**Proposed policy:** The Pension Fund will discuss the implications of such an event with the Fund's Actuary.
69(1)	Decide frequency of payments to be made over to Fund by employers and whether to make an admin charge.	**The Pension Fund's existing policy:** The employing authority shall pay to the administering authority all (employee and employer) contributions due in respect of their employees (or former employees) by the 19th of the month following the end of the month in which the amount was deducted from pay.
71(1)	Whether to charge interest on payments by employers which are overdue	**Proposed policy:** The Fund reserves the right to charge employers interest on delayed payments under Reg 69(1).
82(2)	Whether to pay death grant due to personal representatives or anyone appearing to be beneficially entitled to the estate without need for grant of probate / letters of administration where payment is less than amount specified in S6 of the Administration of Estates (Small Payments) Act 1965	**Proposed policy:** Where the death grant due is less than the amount specified in S6 of the Administration of Estates (Small Payments) Act 1965, currently £5,000, payment will be made following completion of a Form of Indemnity. However, any apparent dispute as to who should receive payment and the Fund will refer to the policy under the payment of death grants above.

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

83	Whether, where a person (other than an eligible child) is incapable of managing their affairs, to pay the whole or part of that person's pension benefits to another person for their benefit.	**Proposed policy:** The Pension Fund will request Power of Attorney or in the absence of this satisfactory evidence that the person is managing the member's affairs (e.g. to whom DWP payments are being made).
100(6).	Extend normal time limit for acceptance of a transfer value beyond twelve months from joining the LGPS.	**The Pension Fund's current policy is:** To allow in exceptional circumstances where it is clear there has been an administrative delay by the employer or the scheme administrator This is now a joint policy with the Administering Authority to prevent scheme employers from accepting late applications without good reason.
100(7)	Allow transfer of pension rights into the Fund.	**Proposed policy:** Allowed
Sch 1 & Trans Regs 17(9)	Decide to treat child as being in continuous education or vocational training despite a break.	**The Pension Fund's existing policy is:** That the AA allow a break of up to eighteen months to allow the child of a deceased member to take "a year out" between further and higher education and for payment to be suspended during this period of suspension. This has long been the practice of the Authority.

APPENDIX A
PUBLIC SERVICE PENSIONS, ENGLAND AND WALES

Local Government Pension Scheme Regulations 2013

Sch 1 & Trans Regs 17(9)(b)	Decide evidence required to determine financial dependence of cohabiting partner on scheme member or financial interdependence of cohabiting partner and scheme member.	**The Pension Fund's existing policy is:** That Treasury and Pensions take reasonable steps to determine that a nomination is valid. A benefit will not be payable if the member has not completed a nomination form. The nominated beneficiary will produce on request relevant and valid documents to determine interdependency. For example, proof of joint mortgage or lease for a period in excess of two years, joint bank accounts, Council tax statements.
Trans Regs 3(13) & Admin Reg 70(1) (2008 regs) & Admin Reg 71(4)(c)	Decide policy on abatement of pre 1 April 2014 element of pensions in payment following re-employment.	**The Pension Fund's existing policy is:** "The County Council will no longer apply the abatement rule save in exceptional circumstances where it determines that not to abate the pension in payment could lead to a serious lack of confidence in the public service."
Trans Regs 15(1)(c) & Trans Regs Sch 1 & 83 (1997 regs)	Extend time period for capitalisation of added years contract.	**Proposed policy:** In exceptional circumstances

***These are matters about which the regulations require there must be a written policy.**

Pension Fund Investment Sub-Committee

21 July 2014

Review of Investment Strategy

Recommendation

That the Pension Fund Investment Sub- Committee discuss the proposals in 3.1 to 3.4 based on the findings from Hymans Robertson.

1 Introduction

1.1 At the sub-committee meeting, Hymans Robertson presented a high level strategy paper which used Asset Liability Modelling to assess longer term objectives, future risk, cash flow and the impact on contribution rates.

2. Outcomes Following May Meeting

2.1 The results showed that there was some scope to reduce risk within the investment strategy. However, reductions in risk would be more compelling when the fund had a higher funding level.

2.2 The decision was made that no immediate de-risking would take place. However, it was acknowledged that the concept and principles around de-risking is an area that the Committee should now be considering, particularly in terms of how the Committee might formulate and implement a de-risking strategy.

2.3 It was also agreed that the current level of diversification within the growth assets was appropriate and hence there was no requirement to further reduce equities in favour of alternative growth assets. There was however scope to improve the efficiency of the equity mandate structure

2.4 Given the recommendation in 2.3 there were subsequent discussions with officers and Hymans Robertson regarding the funds equity assets.

2.5 **Appendix A** details the findings of these discussions and the arising two proposals for discussion at this meeting.

3. Proposals for discussion

3.1 The Fund currently has over £400m of equities managed by three passive managers, namely L&G, BlackRock and State Street. Hymans rate each of these managers highly, with all three managers performing in line with their respective benchmarks. However there is scope to consolidate the mandates from three to two, with the aim of simplifying the structure and also potentially reducing management fees.

3.2 The funds passive equities are currently invested in index funds tracking market cap weighted indices. Over recent years, the effectiveness of the market cap approach has been challenged therefore **Appendix B** details alternative forms of methods of index tracking for discussion at this meeting.

3.3 No changes are proposed to the funds two active equity mandates. Both Threadneedle and MFS have outperformed their respective benchmarks over 1, 3, and 5-years.

3.4 No changes are proposed to the split between active and passive equities, particularly given the ongoing DCLG consultation of which one of the key areas is the use of active fund management.

	Name	**Contact Information**
Report Author	Mathew Dawson, Treasury and Pension Fund Manager	Mathewdawson@warwickshire.gov.uk 01926 412227
Head of Service	John Betts, Head of Finance	johnbetts@warwickshire.gov.uk 01926 412441
Strategic Director	David Carter, Strategic Director, Resources Group	davidcarter@warwickshire.gov.uk 01926 412564

Review of Asset Allocation

Introduction

This paper is addressed to the Investment Sub Committee ("the Committee") of the Warwickshire Pension Fund ("the Fund"). It should not be released or otherwise disclosed to any third party except with our prior written consent, in which case it should be released in its entirety. We accept no liability to any other party unless we have especially accepted such liability in writing.

Background

Further to the actuarial valuation carried out as at 31 March 2013, a formal review of the Fund's investment strategy was carried out. The review took into account up-to-date information on the Fund's membership, clarity on the details of the new LGPS Scheme and the revised contribution strategy recommended by the Actuary.

There were two components to the review of strategy:-

- **Setting 'high level' strategy** – agreeing the broad level of risk and expected return from the investments.
- Agreeing the **detailed asset allocation** and manager structure – this stage considers the individual allocations to specific asset classes and considers how best they should be managed.

The findings of the investment strategy review were presented to the Committee at the May 2014 meeting. The outcomes from the discussions were as follows:

- The results showed that there was some scope to reduce risk within the investment strategy. However, reductions in risk would be more compelling when the Fund had a higher funding level.
- The decision was made that no immediate de-risking would take place. However, it was acknowledged that the concept and principles around de-risking is an area that the Committee should now be considering, particularly in terms of how the Committee might formulate and implement a de-risking strategy.
- It was also agreed that the current level of diversification within the growth assets was appropriate and hence there was no requirement to further reduce equities in favour of alternative growth assets. There was however scope to improve the efficiency of the equity mandate structure.

For completeness, we are comfortable with the current line-up of bond mandates and do not believe that any immediate change is necessary within the 'low risk' component of the Fund. Therefore, the remainder of this paper sets out the current asset allocation, and looks in more detail at ways to improve the efficiency of the equity manager line-up.

We are mindful of the DCLG consultation currently in progress regarding the future structure of the LGPS. One of the key areas being considered under the consultation is the appropriateness of active management. Whilst the outcome of the consultation has yet to be confirmed, we are keen to not implement any changes which may subsequently be required to be unwound.

Current Asset Allocation

The table below sets out the current asset allocation including the allocations to private equity and infrastructure.

Asset class	Current Benchmark (showing current private equity investment) %		New Target (assumes full 4% private equity and infrastructure allocations) %	
Equities	56.5		49.5	
UK		26.5		21.0
Overseas Equities		30.0		28.5
Private Equity	1.0		4.0	
Total Equity	**57.5**		**53.5**	
Property	10.0		10.0	
Infrastructure	-		4.0	
Hedge Funds	5.0		5.0	
Multi-Asset Absolute Return	5.0		5.0	
Total 'return-seeking' assets	**77.5**		**77.5**	
Bonds	22.5		22.5	
Gilts		2.5		2.5
Index-Linked Gilts		5.0		5.0
Corporate Bonds		10.0		10.0
Absolute Return		5.0		5.0
Total	**100.0**		**100.0**	

We note the following key points from the above table:

- The infrastructure mandates are currently unfunded. We expect Standard Life to begin calling capital in Q3 2014.
- The private equity allocation is partially funded. Harbourvest will continue to make capital calls as opportunities arise.
- Currently, the Fund is overweight to quoted equities. However, this position is primarily offset by the underweight allocation to infrastructure and private equity, which will reduce over time as outlined above.

We are comfortable with the current target allocation of 49.5% in quoted equities and 4% allocation to private equity and infrastructure programmes. Furthermore, we do not believe that there is any need to further reduce the allocation to equity in favour of more diversification, as we consider the current mix of growth assets to be sufficiently diversified already. We believe that any benefits to be gained from further diversifying the growth assets will be outweighed by the increase in costs (both monetary and governance costs) as a result of the greater complexity.

Current Equity Manager Arrangements

Whilst we do not advise any change to the current mix of growth assets, we do believe there is scope within the quoted equity allocation to improve the structure of these mandates. The table below shows the current equity arrangements split by active and passive management.

		Manager	Actual Allocation (%)	Long Term Benchmark Allocation (%)
Active	UK	Threadneedle	16.0	-
	Overseas	MFS	16.2	-
	Total		**32.2**	**-**
Passive	UK	State Street	7.3	-
		BlackRock	4.0	-
	Overseas	L&G	9.3	-
		BlackRock	6.9	-
	Total		**27.5**	**-**
Total			**59.9**	**49.5**

As at 31 March 2014, the Fund was circa 10% overweight (59.9% v.s. 49.5%) to its long term target allocation to quoted equities. However, a target of 8% has been allocated (split equally) between private equity and infrastructure. The funding of the private equity mandate has already begun (c.1% of total Fund assets as at 31 March); however, capital has yet to be allocated to the infrastructure mandates.

Therefore, 7% of the 'overweight' equity position represents assets that have still to be invested in private equity and Infrastructure. Excluding these mandates which have not yet been fully been funded, the overweight to quoted equities is circa 3%, which is offset by small underweight positions in property, hedge funds, and absolute return funds.

The specific target allocations for individual managers going forward will be finalised in con junction with any changes made as part of this current review.

Active Equity Mandates

We are comfortable with the Fund's current active equity managers, and would not propose that any changes are made to these mandates. Both Threadneedle and MFS have outperformed their respective benchmarks over 1-, 3-, and 5-years. The table below shows the actual v.s. benchmark performance for the period to 31 March 2014, as provided by the investment managers.

Managers	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)
Threadneedle			
Actual	14.2	11.9	17.4
Benchmark	8.8	8.8	16.4
Relative	+5.0	+2.8	+0.9
MFS			
Actual	8.8	13.4	18.1
Benchmark	6.2	7.0	14.1
Relative	+2.4	+6.0	+3.5

Passive Equity Mandates

The Fund currently has over £400m of equities managed by three passive managers, namely L&G, BlackRock and State Street. We rate each of these managers highly, with all three managers performing in line with their respective benchmarks. We do however believe that there is scope to consolidate the mandates from three to two, with the aim of simplifying the structure and also potentially reducing management fees. In doing so, we would also recommend that the Committee consider alternative ways to passively manage equities.

Alternative ways of passive management

The Fund's passive equity assets are all invested in index funds tracking market cap weighted indices. These passive strategies are seen as providing low cost, low governance and therefore efficient access to equity returns. However, over recent years, the effectiveness of the market cap approach has been challenged, leading to the development of different index construction methodologies, for example, equal weighting, fundamentally weighted indices, risk efficient indices and low volatility indices.

Of these alternatives, our preferred approach is for assets to be managed passively against a fundamentally weighted index alongside traditional 'market cap' based funds. The remainder of this paper therefore considers the fundamental indexation approach. The training slides entitled "Alternative approaches to passive management" dated July 2014, provide some further details on the other approaches and will form the basis of a presentation at the forthcoming meeting.

Why consider an alternative to market cap weighted indices?

Market capitalisation weighted indices are the well-established default measure for the performance of equity markets and have been so for many years. For the overwhelming majority of equity managers these indices are their primary benchmark which they either track, in the case of passive managers, or try to beat, in the case of active managers. The positive attributes of market cap indices, set out below, cannot be dismissed lightly:

- easy to understand;
- accurate reflection of the supply and demand from investors;
- easy to monitor and replicate (track) as it offers good liquidity and transparency;
- essentially self-rebalancing;
- comparatively easy and cheap to access.

The major criticism for this price led index construction methodology is that it has a pro cyclical nature. As a stock's price increases relative to other index constituents, so does its weight in the index and vice versa. If companies' share prices accurately reflect their underlying financial performance then market cap weighted indices are behaving efficiently. However, stock prices are very erratic, driven by short term news and investors' behavioural drivers. There is much evidence to suggest that, even over extended periods, the relationship between share price and underlying fundamental value breaks down.

The link between pricing and index weight means there is a tendency for capital flows to be allocated to overvalued stocks and away from undervalued stocks; this is a key flaw of cap weighted indices. Further, although we typically regard the market index as style neutral, in fact the index construction methodology produces a bias to large cap growth style companies as investors are attracted to overtly successful businesses.

What are fundamentally weighted indices?

Fundamental weighting is a method of index construction that breaks the link between a stock's price and its weighting within an index. The intention is to remove the influence of future investor expectations by taking price out of the weighting calculation. Instead, the weighting of a company depends on a number of past and present financial factors taken from statutory financial accounting data.

In a fundamentally weighted index, the weight of each stock is determined by reference to directly observable, historic valuation measures / characteristics of the company. The aim is for a company's index weighting to be more representative of its economic footprint.

Clearly, there will still be a relationship between a company's size and these fundamental characteristics (larger companies tend to have higher revenues, they typically generate more cash, pay more dividends and employ more people). Importantly, however, the fundamental characteristics are all backward looking and thus reflective of the intrinsic "worth" of the company. There is some differentiation in the composition and time frame over which fundamental index providers assemble their value setting data. Nevertheless, the common feature is that the volatility associated with market sentiment and investor expectations of future profitability, which are automatically built into price-based indices, are eliminated.

Since fundamental indices are not price weighted, movements in share prices create drifts in actual index weights which require periodic re-balancing back to fundamentally determined weights. Rebalancing has a cost, so the trade-off between frequency of re-balancing (and thus cost) versus a pure, fundamental index tracking portfolio, needs to be considered.

Pros of fundamental indexation

- Fundamental indexation provides an element of diversification to market cap passive, for example:
    - a degree of protection against excessive, speculative over or under valuation of stocks;
    - an offset to the large cap growth bias of cap weighted indices;
- It provides the potential to outperform market cap indices over longer periods due to:
    - exploitation of the value premium;
    - the discipline of contrarian rebalancing;
- Access is straightforward, transparent and liquid;
- Governance requirements are low.

Cons of fundamental indexation

- Fundamental indices' performance may deviate markedly from that of market cap indices over shorter periods even though long run volatility will be similar; historically observed excess return may take several years to accrue;
- Fundamental indices and fundamental index tracking managers will not adapt their rules to changing market conditions; the mandate is effectively passive once the decision to follow a fundamental index approach is taken;
- There is a value bias, the environment for which may be hostile under certain macroeconomic conditions;
- There is higher transition cost drag than market cap indices and scale may eventually erode excess returns, though we believe this to be some considerable way off;
- Rebalancing exercises tend to be contrarian and may, therefore, be "uncomfortable" at times; for example, an increasing allocation to out of favour financial stocks has been a recent feature;
- At this stage, passive fundamental indexation is slightly higher cost and does not offer the same flexibility in terms of liquidity (transition etc) as passive market cap.
- More effective at a global level e.g. emerging markets, where pricing inefficiencies may prevail more.

Recommendations

In light of the results of the strategy modelling, and the more detailed analysis of the Fund's equity mandates, we propose the following recommendations:

- The composition of the overall mix of growth assets is sufficiently well diversified. As a result, we recommend making **no further changes to the current mix of growth assets**.
- We are comfortable with the current mix of 'low risk' assets given the Fund's liabilities. We therefore recommend that **no further changes be made to the 'low risk' assets in the immediate future**.
- In light of the ongoing DCLG consultation, and potential outcomes from it, we recommend that the **split between active and passive equities remains unchanged for the immediate future**.
- Within the Fund's passive equity allocation, we recommend that the Fund **introduces an allocation to fundamental indexation at a global equity level**, to be managed by one of the existing passive equity managers. We recommend leaving the passive UK equities to track a market cap index.
- In conjunction with the above change, the aim is to **consolidate the Fund's passive equity assets with two managers**.

We look forward to discussing these issues at the forthcoming meeting.

Prepared by:-

Paul Potter, Partner

Elaine Torry, Associate Consultant

June 2014

For and on behalf of Hymans Robertson LLP

General Risk Warning

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.

Alternative approaches to passive management

Warwickshire Pension Fund

- Paul Potter
- July 2014

Your current equity managers

		Manager	Valuation (£m)	Actual Allocation (%)
Active Equities	UK	Threadneedle	237.4	16.0
	Global	MFS	239.8	16.2
Total Active			477.2	32.2
Passive Equities	UK	State Street	108.7	7.3
		BlackRock	59.7	4.0
	Overseas	L&G	138.4	9.3
		BlackRock	102.3	6.9
Total Passive			409.1	27.5
Total Equities			**886.3**	**59.9**

Totals may not sum due to rounding.

Stock market indices

- Define the investment universe
- Set by strict rules
  - What's in, what's out ?
  - Weighting of each company ?
  - Frequency of rebalancing ?
- Used to measure
  - 'Market' return
  - Risk taken relative to the index (by active managers)
- Standard historical approach uses market capitalisation
- **Knowledge of index crucial for passive mandates**

Market capitalisation – industry benchmark of choice (currently)

- Three share universe (Companies A, B and C)
- Consider the ABC market cap index...

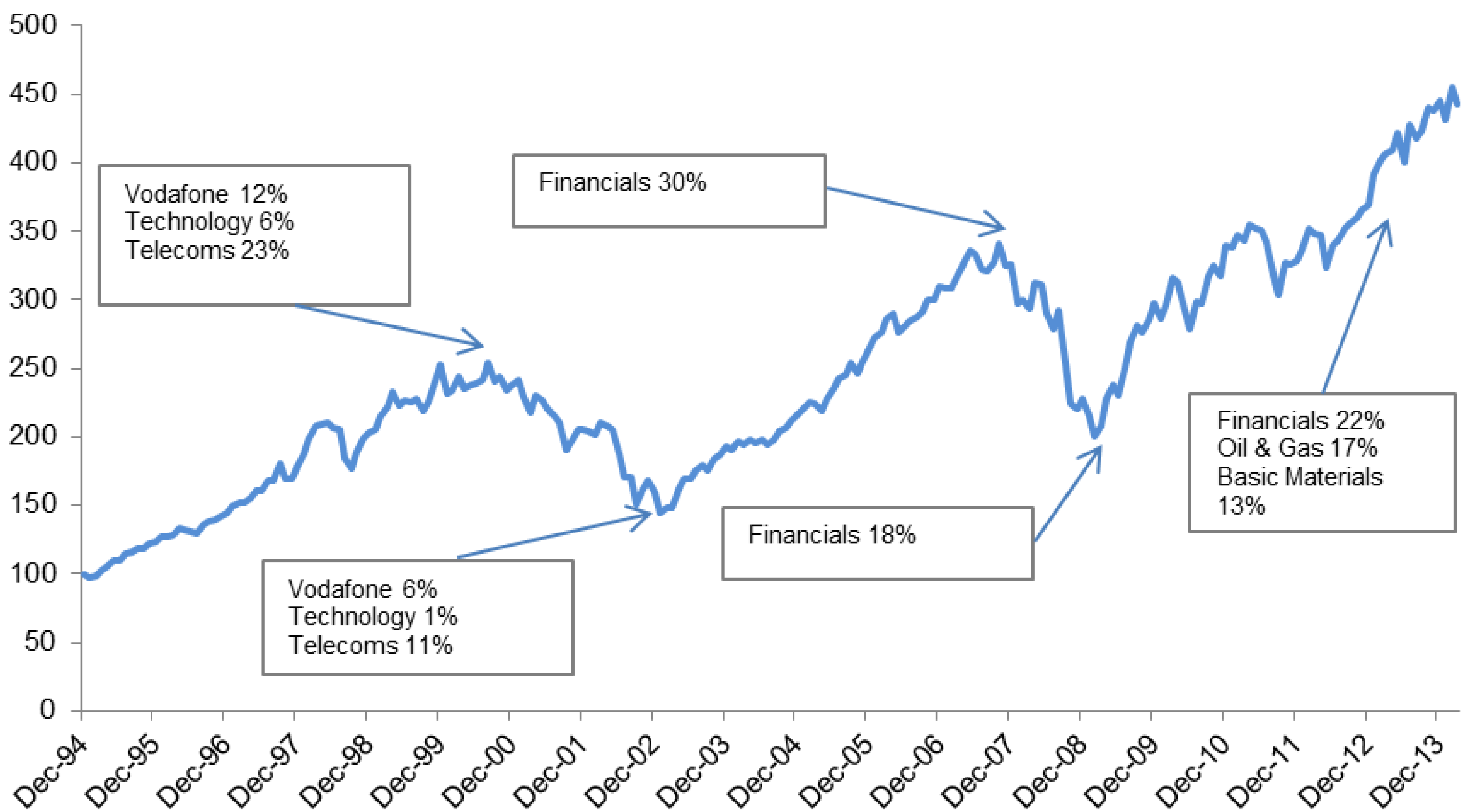
Company	Number of shares issued	Current share price	Market Capitalisation	Index weight
A	100	£1.00	£100	25%
B	200	£0.50	£100	25%
C	250	£0.80	£200	50%
Totals			£400	100%

Market capitalisation – changes to weightings

- Price changes drive weightings in index
- Portfolio rebalances along with benchmark

Company	Number of shares issued	Current share price	Market Capitalisation	Index weight
A	100	£2.00	£200	40%
B	200	£0.50	£100	20%
C	250	£0.80	£200	40%
Totals			£500	100%

Market capitalisation indices – chasing bubbles



- Weighting sensitive to price, price/earnings ratios etc

Market cap. weighted indices

- Likely to remain the default for equity access and benchmarking
  - transparent and objective
  - simple
  - liquid and relatively cheap to track
- … but challenges are emerging
  - excessive price speculation
  - continuing high volatility
  - rising allocations to passive equity

Three topical alternatives to market cap weighted indices

- Fundamental indices (e.g. RAFI, GWA)
  - weights based on real measures of a company's size
  - value tilt; 'contrarian' (sell high, buy low) rebalancing effect
- Low volatility / minimum variance indices (e.g. MSCI Minimum Volatility index)
  - weights based on constructing a lower / lowest risk stock portfolio
- Equally weighted indices
  - each stock has an equal weighting

Passive alternative index options

Index type	For	Against	Conclusion
Fundamental	Provides diversified, value tilted equity exposure. Rebalances from outperformers to underperformers Readily understandable and intuitively appealing. Good performance record versus market cap weighting	Slightly higher fees over market cap (e.g. 0.06% p.a. - licensing fee paid to RAFI). More rebalancing = higher transaction costs (RAFI c.0.08% p.a. vs. market cap c.0.02% p.a.) No long term reduction in volatility.	Suitable alongside market capitalisation index investment. Arguably an alternate to active value manager. ✓
Minimum variance	Supporting evidence of reduction in risk without reduction in return over historical period considered. Less ‘naive’ approach, considers correlations and risk factors.	Arguably more active than passive – potentially concentrated portfolios High tracking error vs. m. cap Turnover can be high.	Typically complex and methodology more subjective. ✗
Equal weighted	Avoids concentration issues. Simple and objective. Forms basis of several empirical studies.	Significant turnover and rebalancing costs. Higher weight to (riskier?) small cap stocks. Liquidity issues →universe limited.	Appealing but arbitrary and practical constraints. ✗

Fundamental equity indices

- Link broken between a company’s share price and its index weighting
  - Removes influence of future emotive investor expectations
  - Rebalances away from ‘excess speculation’ and hence bubbles (e.g. TMT bubble in late ‘90s)
- Weightings anchored by fundamental measures
  - Sales
  - Cashflow
  - Book value
  - Dividends

Like for like comparison: rules

Fundamental Index

Individual stock weights determined by share of:

- Sales
- Book value
- Cash flow
- Dividends

.... or some other combination of fundamental valuation measures

Market Cap Index

Individual stock weights determined by:

Issued shares x share price

Price determined by:

- shares in issue
- investor assessment of historical performance
- investor expectations of future returns

Like for like comparison: characteristics

Fundamental Index

- Value tilt (reflects ‘back to basics’ link with fundamental valuation measures)
- Rebalancing required
- Rebalancing turnover (c.15% p.a.; trading cost 0.06% - 0.10% p.a.)
- Modest tilt to small cap
- Volatility similar to market cap over long periods

Market Cap Index

- Style neutral (arguably behavioural tilt to large cap growth)
- Turnover c.2-3% p.a. (constituent change with trading cost c. 0.02% p.a.)
- Automatically rebalances

Like for like comparison: regional split

Fundamental Index

North America	43.9
Europe (ex-UK)	20.9
UK	9.3
Japan	10.2
Asia (ex-Japan)	6.5
Emerging Markets	9.2

Market Cap Index

North America	52.7
Europe (ex-UK)	17.1
UK	7.7
Japan	7.3
Asia (ex-Japan)	4.5
Emerging Markets	10.7

At 31 March 2014 Update.
Source: RAFI, MSCI World All Countries

Like for like comparison: sector split

Fundamental Index	
Basic Materials	8.6
Consumer Goods	11.2
Consumer Services	9.2
Energy	12.5
Financial	24.8
Health Care	6.4
Industrial	10.7
Technology	5.8
Telecoms	5.6
Utilities	5.4

Market Cap Index	
Basic Materials	5.6
Consumer Goods	13.9
Consumer Services	10.6
Energy	9.6
Financial	22.0
Health Care	8.6
Industrial	12.0
Technology	9.1
Telecoms	4.9
Utilities	3.8

At 31 March 2014 Update.
Source: RAFI, MSCI World All Countries

Like for like comparison: top 10 stocks

Fundamental Index

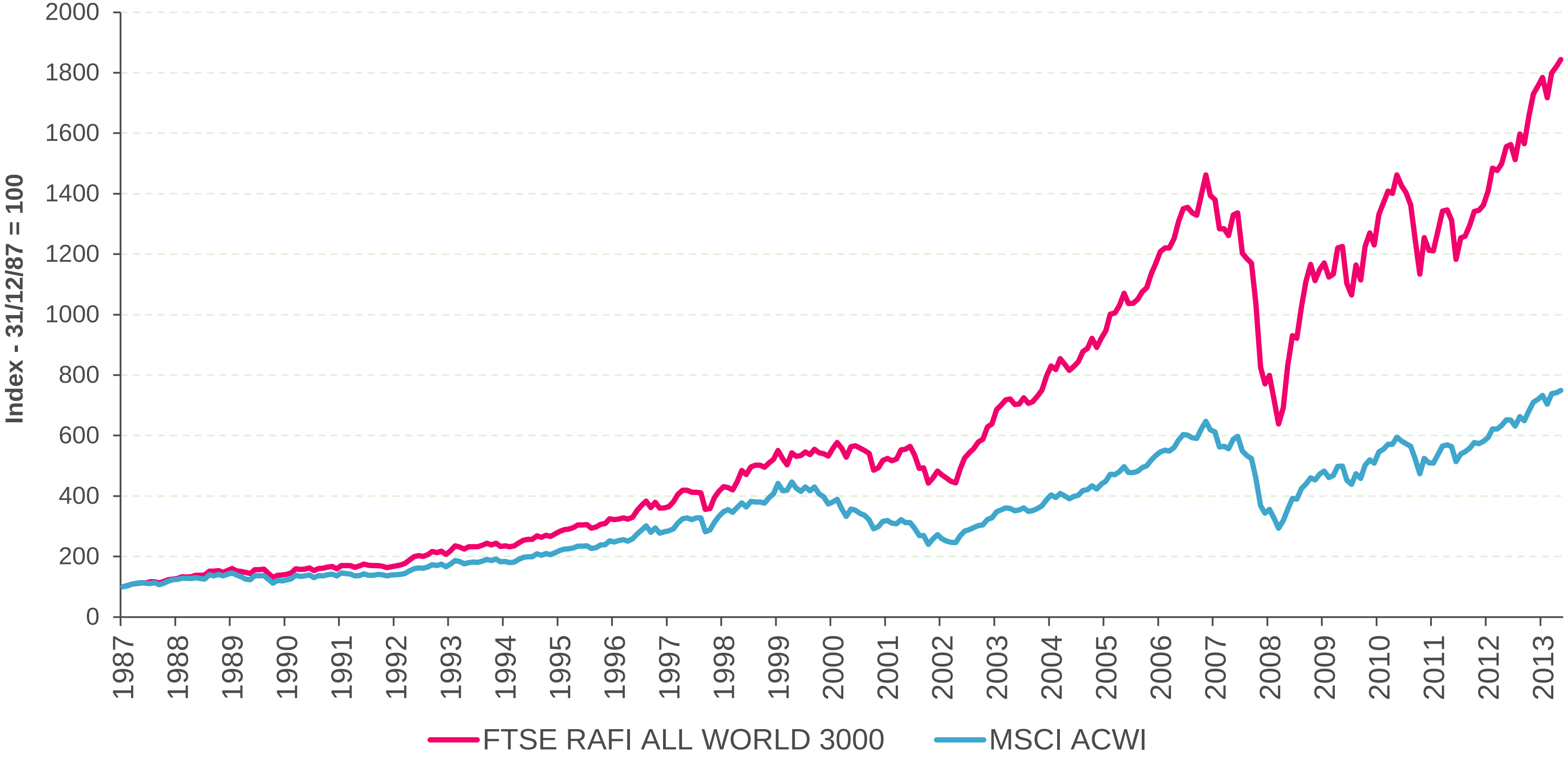
Exxon Mobil Corp.	1.2
AT&T	0.9
BP	0.8
Chevron	0.8
JP Morgan Chase	0.8
HSBC	0.7
Royal Dutch Shell	0.7
General Electric	0.7
Bank of America	0.7
Total France	0.7

Market Cap Index

Apple	1.1
Exxon Mobil	1.0
Microsoft	0.8
Google	0.7
Johnson & Johnson	0.6
Wells Fargo & Co	0.6
General Electric	0.6
Walmart Stores	0.6
Nestle	0.6
Royal Dutch Shell	0.5

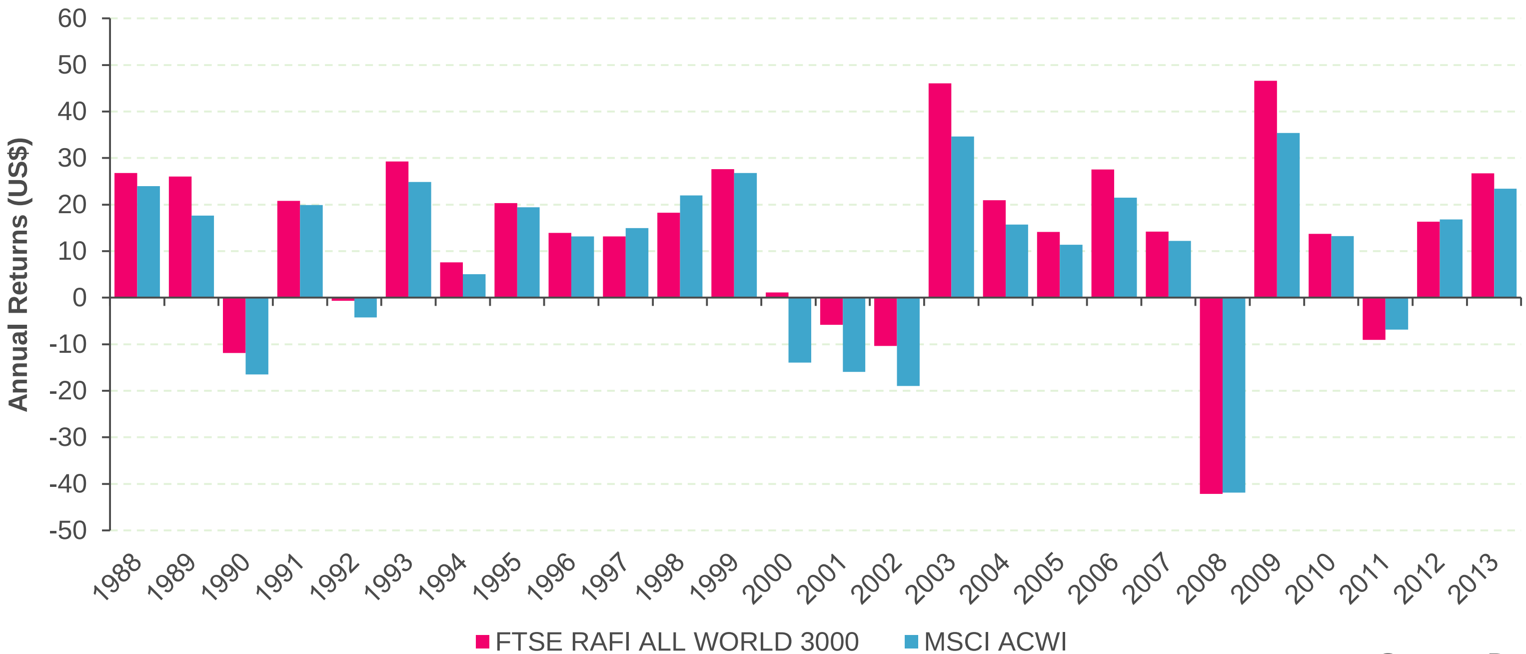
At 31 March 2014 Update.
Source: RAFI, MSCI World All Countries

Like for like: cumulative performance comparison



Source: Datastream

Like for like: annual performance comparison



Source: Datastream

Returns	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
FTSE RAFI	13.1	18.3	27.6	1.1	-5.8	-10.3	46.0	20.9	14.1	27.6	14.2	-42.1	46.6	13.7	-9.1	16.3	26.7
MSCI ACWI	15.0	22.0	26.8	-13.9	-15.9	-19.0	34.6	15.8	11.4	21.5	12.2	-41.8	35.4	13.2	-6.9	16.8	23.4

Implementation – passive fundamental equity

- Methodology providers:
  - RAFI; GWA; MSCI
- Index providers:
  - FTSE; Russell; MSCI
- Pooled (index tracking) fund providers:
  - L&G, BlackRock, State Street (RAFI global funds of £1bn+)
- Fees likely to be marginally higher than market cap passive + licence fee of methodology provider (e.g. RAFI 6 basis points)
- But still low cost relative to active management

Passive fundamental equity – Pros & Cons

Pros	Cons
Diversification to market cap passive	Deviations from market cap over short term
Protect against excessive, speculative over/under valuation of stocks	No scope to changes rules i.e. passive management
Value style bias offsets large cap growth bias	Environment for value investing can be hostile
Potential to outperform over the long term?	Ongoing rebalancing and one-off implementation costs
Access is straightforward, transparent and liquid	Slightly higher fees
Governance requirements are low	Lower liquidity and flexibility than market cap

Looking forward – passive fundamental equity

- Attractive compliment to current ‘market cap’ mandates.
- Implementation possible with existing managers (L&G, BlackRock, State Street).
- Recommend that allocation is introduced within passive equity component of the Fund.

General Risk Warning

This communication has been compiled by Hymans Robertson LLP, and is based upon their understanding of events as at June 2014 and therefore may be subject to change. This publication is designed to be a general summary of a topical investment issue and is not specific to the circumstances of any particular employer or pension scheme. The information contained herein is not to be construed as advice and should not be considered a substitute for specific advice in relation to individual circumstances. Where the subject of this note refers to legal matters please note that Hymans Robertson LLP is not qualified to give legal advice therefore we recommend that you seek legal advice. Hymans Robertson LLP accepts no liability for errors or omissions. Your Hymans Robertson LLP consultant will be pleased to discuss any issue in greater detail.

Please note the value of investments, and income from them, may fall as well as rise. This includes but is not limited to equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.

Thank you

Any questions?

Like for like: top stock comparison

Top RAFI 3000 holding

Exxon Mobil Corp.

RAFI 3000 (1.2%)

Book Value: c. $177bn
Cash Flow: c. $47bn*
Revenue: c. $372bn*
Dividends: c. $9.3bn*

MSCI World All Countries (1.0%)

Share Price: $45
No shares outstanding: c. 4.3bn
Market Cap: c. $440bn

Apple

RAFI 3000 (0.4%)

Book Value: c. $120bn
Cash Flow: c. $34bn*
Revenue: c. $109bn*
Dividends: c. $2.6bn*

MSCI World All Countries (1.1%)

Share Price: $92
No shares outstanding: c. 6bn
Market Cap: c. $560bn

Top MSCI World AC holding

* Average over last 5 years

Like for like: top ten comparison

HYMANS ROBERTSON
The Spirit of Independence

2008	
RAFI 3000	FTSE All-World
Exxon Mobil	Exxon Mobil
BP	Procter & Gamble
Wal-Mart Stores	Microsoft
JPMorgan Chase & Co	General Electric
Verizon Communications	AT&T
General Electric	Wal-Mart Stores
Chevron	Johnson & Johnson
HSBC	Nestle
Pfizer	Chevron
AT&T	BP

2009	
RAFI 3000	FTSE All-World
Bank of America	Exxon Mobil
ING Group CVA	Microsoft
Citigroup	HSBC
Exxon Mobil	Apple
BP	BP
HSBC	Johnson & Johnson
General Electric	Procter & Gamble
Ford Motor	Nestle
AT&T	International Bus Machns.
Vodafone Group	AT&T

2010	
RAFI 3000	FTSE All-World
Exxon Mobil	Exxon Mobil
General Electric	Apple
AT&T	Microsoft
Petrochina (H)	Nestle
ING Group CVA	General Electric
Vodafone Group	Chevron
Chevron	International Bus Machns.
BP	Procter & Gamble
Royal Dutch Shell A	HSBC
Citigroup	AT&T

2011	
RAFI 3000	FTSE All-World
Exxon Mobil	Exxon Mobil
AT&T	Apple
BP	Microsoft
Chevron	International Bus Machns.
General Electric	Chevron
Vodafone Group	Nestle
Royal Dutch Shell A	General Electric
Wal-Mart Stores	Procter & Gamble
Pfizer	Johnson & Johnson
Total	AT&T

2012	
RAFI 3000	FTSE All-World
Bank of America	Apple
Exxon Mobil	Exxon Mobil
Royal Dutch Shell	Microsoft
General Electric	Royal Dutch Shell
AT&T	General Electric
HSBC	IBM
BP	Chevron
Citigroup	Nestle
JPMorgan Chase & Co	Samsung
Chevron	BHP Billiton

2013	
RAFI 3000	FTSE All-World
Exxon Mobil Corp.	Apple
AT&T	Exxon Mobil
BP	Microsoft
Chevron	Google
JP Morgan Chase	Johnson & Johnson
HSBC	Wells Fargo & Co
Royal Dutch Shell	General Electric
General Electric	Walmart Stores
Bank of America	Nestle
Total France	Royal Dutch Shell

Item 4

Pension Fund Investment Sub-Committee

21 July 2014

Funding Update

Recommendation

That the Pension Fund Investment Sub-Committee takes no action as a result of the funding update, as recommended by the actuary and, continues to regularly monitor the funding position ahead of the next valuation.

1 Introduction

1.1.1 Over a year has passed since the formal actuarial valuation as at 31 March 2013. An estimated funding update was requested at the meeting of the Investment Sub-Committee dated 19 May 2014.

1.2 Following this meeting the fund actuary has calculated an estimated funding level at 31 May 2014.

1.3 **Appendix A** shows the full results.

2 Funding update results

Funding level

2.1 The results of this update show an increase in funding level from 76.7% in March 2013 to 82.6% in May 2014.

£m	**31 Mar 2013**	**31 May 2014**
Assets	1,379	1,507
Liabilities	1,798	1,823
Surplus/(deficit)	(419)	(317)
Funding Level	**76.7%**	**82.6%**

Whole Fund common contribution rate

2.2 This has fallen from 29.2% of pay to 26.0% of pay. Of this reduction, 0.7% of pay relates to the cost of future service benefits and 2.5% of pay to past service deficit recovery.

3 Commentary on results

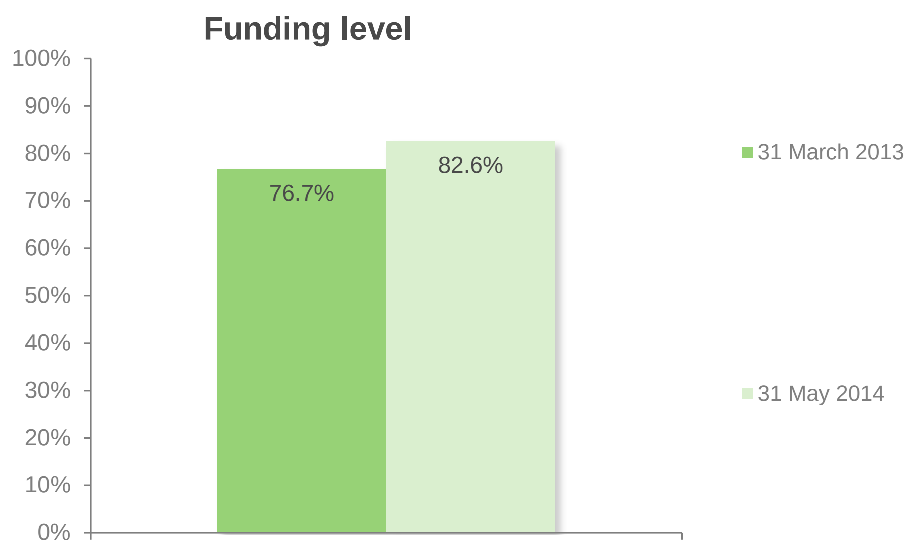
3.1 The rise in the funding level and corresponding fall in the deficit and contribution rate is clearly welcome. The main reason is that assets have returned about 10% during the period versus an “expected” return, as implied by the valuation discount rate, of about 5.5%. There has also been a small improvement of 0.15% pa in long term interest rates (net of inflation). This reduces the value placed on the liabilities and the cost of future service benefits.

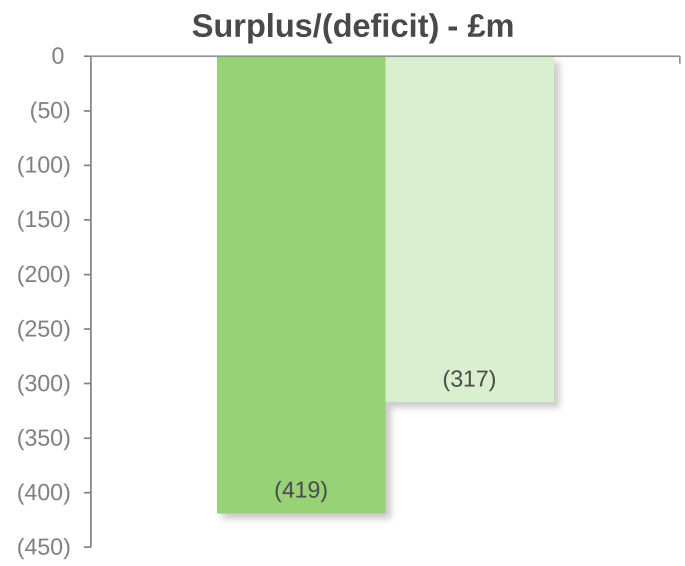
3.2 In practice, the major employers in the Fund pay stabilised contribution rates that are significantly below the Whole Fund rate quoted above. These stabilised rates were set in anticipation of long term asset returns being higher than the discount rate and allowed for gradual rises in interest rates over time. The results of this funding update suggest that that the Fund is slightly “ahead of schedule” at present in terms of meeting its long term objective of being fully funded.

3.3 These results are at Whole Fund level only. Individual employer funding positions may have changed to either a greater or less extent.

	Name	**Contact Information**
Report Author	Mathew Dawson, Treasury and Pension Fund Manager	mathewdawson@warwickshire.gov.uk 01926 412227
Head of Service	John Betts, Head of Finance	johnbetts@warwickshire.gov.uk 01926 412441
Strategic Director	David Carter, Strategic Director	davidcarter@warwickshire.gov.uk 01926 412564

Funding update as at 31 May 2014
Warwickshire County Council Pension Fund





HYMANS ROBERTSON

Summary

This funding update is provided to illustrate the estimated development of the funding position from 31 March 2013 to 31 May 2014, for the Warwickshire County Council Pension Fund ("the Fund"). It is addressed to Warwickshire County Council in its capacity as the Administering Authority of the Warwickshire County Council Pension Fund and has been prepared in my capacity as your actuarial adviser.

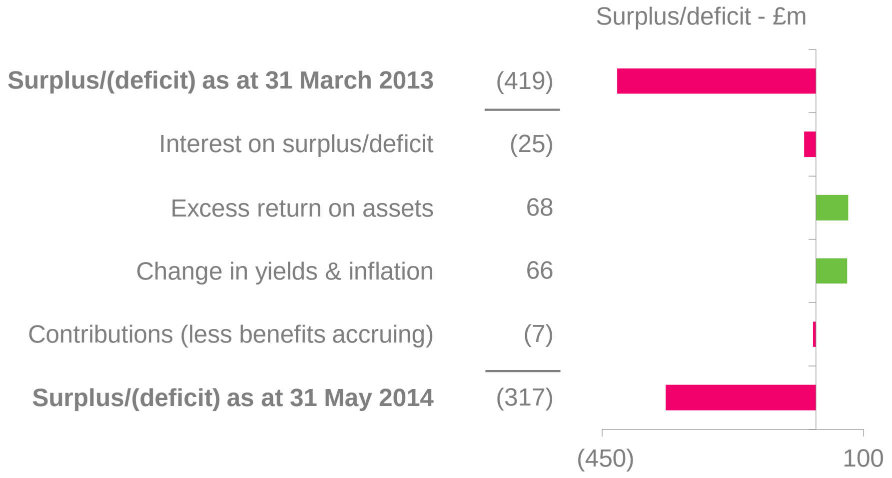
The funding level at the latest formal valuation was 76.7%. As at 31 May 2014 the funding level has increased to 82.6%. This is largely as a result of an increase in bond yields, and subsequent higher discount rate, which places a lower value on the Fund's liabilities. This has been offset by an increase in inflation and asset performance being less than expected.

This report has been produced exclusively for the Administering Authority. This report must not be copied to any third party without our prior written consent.

This report looks at the whole fund position and does not allow for the circumstances of individual employers. The results for individual employers can be quite different to the fund as a whole depending on their own experience and the profile of their liabilities. Differences in the relationship between the ratio of accrued liabilities and the payroll can have a large influence on changes in contributions.

Richard Warden
Fund Actuary

What's happened since the last update – ongoing funding basis



Differences between this funding update and a full actuarial valuation

The accuracy of this type of funding update calculation is expected to decline over time as the period since the last valuation increases. This is because this funding update does not allow for changes in individual members' data since the last valuation.

Details of the approach used in this funding update are given in the appendix.

The figures in tables throughout this document may not add up due to rounding.

HYMANS ROBERTSON LLP

Estimated financial position at 31 May 2014

Ongoing funding basis

£m	31 Mar 2013	31 May 2014
Assets	1,379	1,507
Liabilities	1,798	1,823
Surplus/(deficit)	**(419)**	**(317)**
Funding level	76.7%	82.6%

Gilts funding basis

£m	31 Mar 2013	31 May 2014
Assets	1,379	1,508
Liabilities	2,438	2,453
Surplus/(deficit)	**(1,059)**	**(945)**
Funding level	56.6%	61.5%

Basis summary

	31 Mar 2013	31 May 2014
Pre retirement discount rate		
Nominal	4.6%	4.9%
Real	1.3%	1.5%
Post retirement discount rate		
Nominal	4.6%	4.9%
Real	1.3%	1.5%
Salary increase rate	4.3%	4.5%

The assumptions underlying the funding bases are set out in the Funding Strategy Statement. They are those set for the 2013 valuation of the Fund updated for market conditions as at the calculation date.

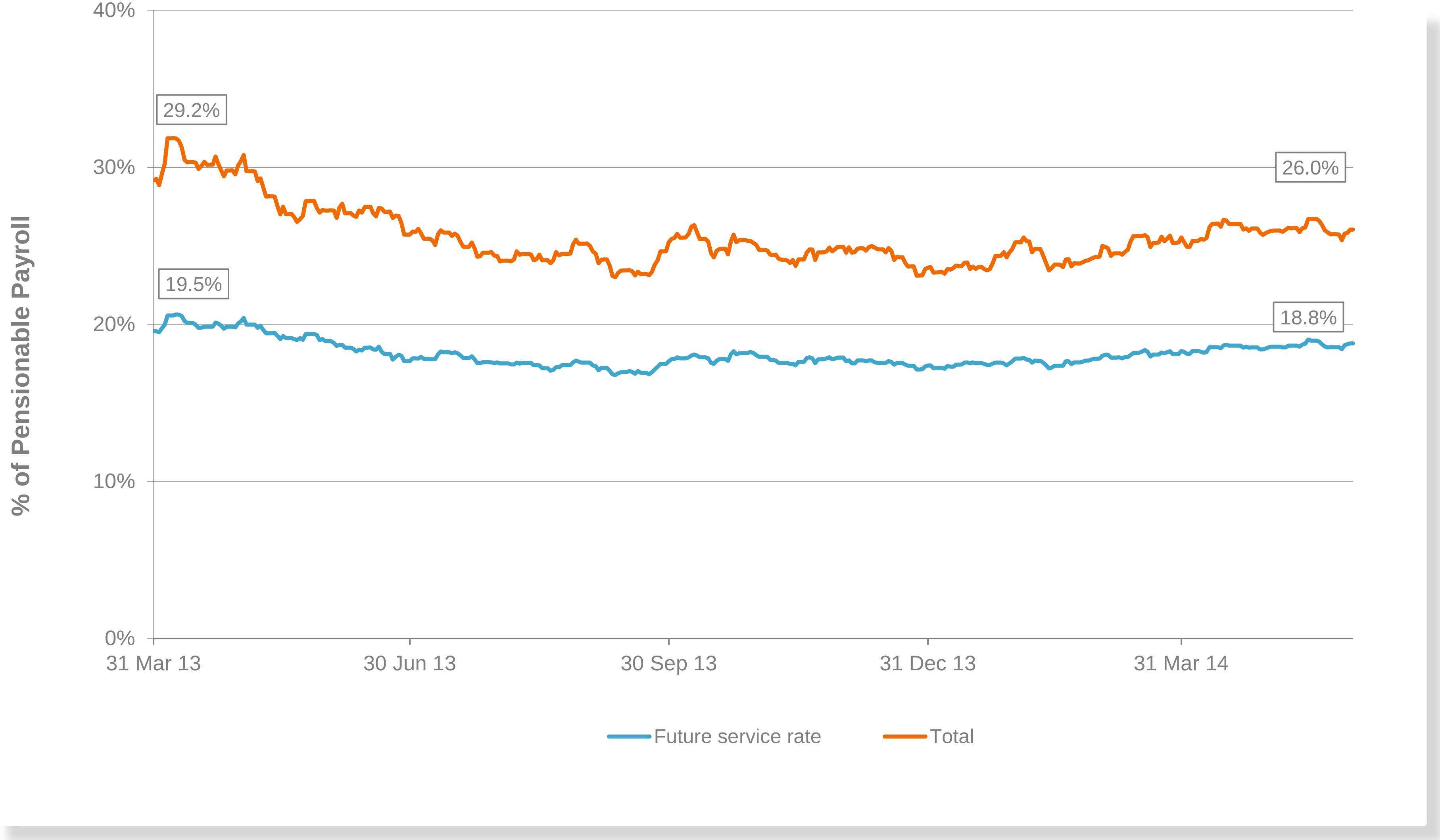
Market indicators

	31 Mar 2013	31 May 2014
Market yields (p.a.)		
Fixed interest gilts	3.04%	3.33%
Index linked gilts	-0.27%	-0.12%
Implied inflation (RPI)	3.33%	3.45%
Implied inflation (CPI)	2.55%	2.68%
AA corporate bonds	4.07%	4.11%
AA spread	1.03%	0.78%
AOA	1.60%	1.60%
Price indices		
FTSE All Share	3,381	3,655
FTSE 100	6,412	6,845

Change in funding level since last valuation

HYMANS ROBERTSON LLP

Change in contribution rate



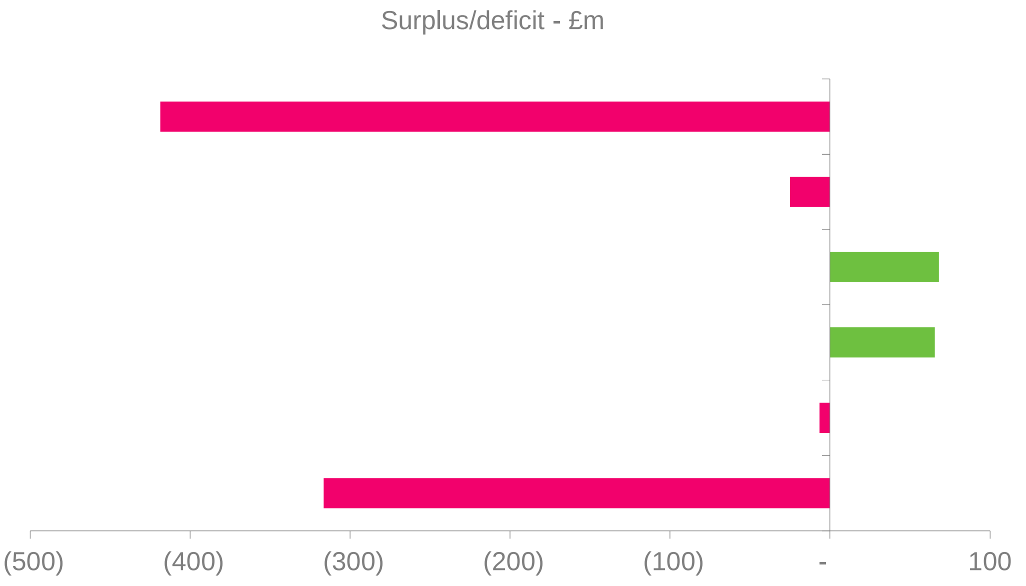
What's happened since last valuation? – ongoing funding basis

Assets		£m
Asset value as at 31 March 2013	1,379	
Contributions paid in:		60
Benefit payments:		(75)
Expected return on assets:		75
Excess return on assets:		68
Asset value as at 31 May 2014	1,507	

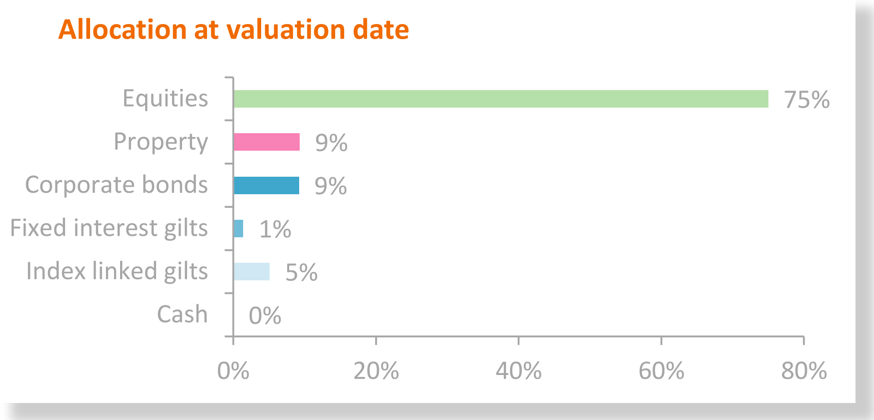
Liabilities		£m
Liability value as at 31 March 2013	1,798	
Cost of benefits accruing:		66
Interest on liabilities:		100
Change in yields & inflation:		(66)
Benefit payments:		(75)
Liability value as at 31 May 2014	1,823	

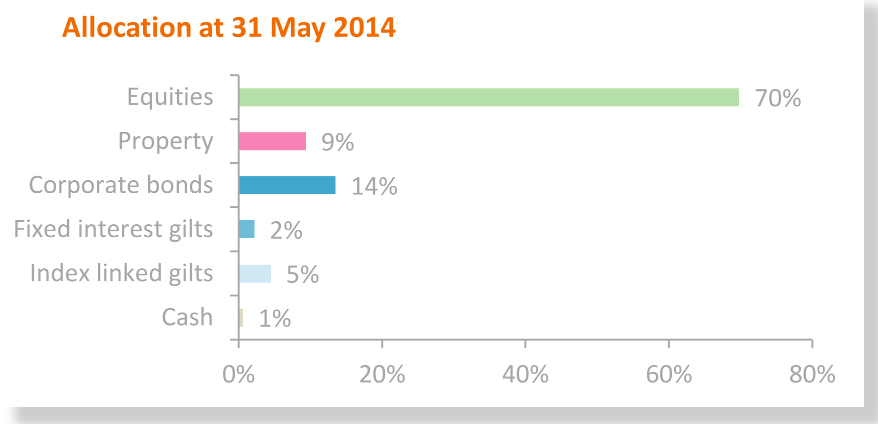
Overall effect

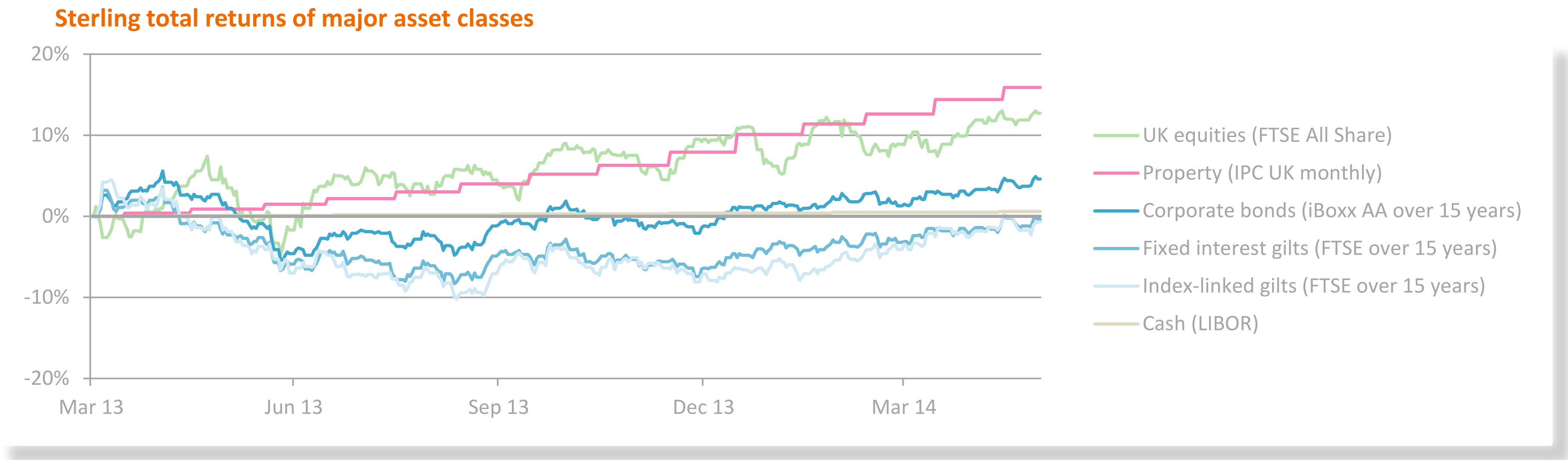
Surplus/(deficit) as at 31 March 2013	(419)
Interest on surplus/deficit	(25)
Excess return on assets	68
Change in yields & inflation	66
Contributions (less benefits accruing)	(7)
Surplus/(deficit) as at 31 May 2014	(317)



What caused your assets to change?







Sensitivity matrix – ongoing funding basis

Better outcomes →

Bond yields (% p.a.)							
3.94	68.5% (517)	75.8% (397)	83.0% (278)	90.3% (159)	97.6% (39)	104.9% 80	112.2% 199
3.73	66.6% (566)	73.7% (447)	80.7% (328)	87.7% (208)	94.8% (89)	101.8% 31	108.8% 150
3.53	64.8% (619)	71.6% (499)	78.4% (380)	85.2% (261)	92.0% (141)	98.7% (22)	105.5% 97
3.33	63.0% (675)	69.6% (555)	76.1% (436)	82.6% (317)	89.2% (197)	95.7% (78)	102.3% 42
3.12	61.2% (734)	67.5% (615)	73.8% (495)	80.1% (376)	86.4% (257)	92.8% (137)	99.1% (18)
2.92	59.4% (797)	65.5% (678)	71.6% (558)	77.7% (439)	83.7% (320)	89.8% (200)	95.9% (81)
2.72	57.7% (864)	63.5% (745)	69.4% (626)	75.2% (506)	81.1% (387)	86.9% (268)	92.7% (148)
	4,791	5,476	6,160	6,845	7,529	8,213	8,898

Equity level (using FTSE 100 Price Index as a proxy)

Better outcomes ↑

82.6%	Funding level
(317)	Surplus/(deficit) – £m

Appendix: Scope, methodology, reliances, limitations and market data

Scope

This funding update is provided to Warwickshire County Council as the Administering Authority of the Warwickshire County Council Pension Fund to illustrate the funding position as at 31 May 2014. It should not be used for any other purpose. It should not be released or otherwise disclosed to any third party except with Hymans Robertson LLP's prior written consent, in which case it is to be released in its entirety. Hymans Robertson LLP accepts no liability to any third party unless we have expressly accepted such liability in writing.

Compliance with professional standards

The method and assumptions used to calculate the updated funding position are consistent with those used in the latest formal actuarial valuation, although the financial assumptions have been updated to reflect known changes in market conditions. As such, the advice in this report is consistent with that provided for the last valuation, as set out in the:

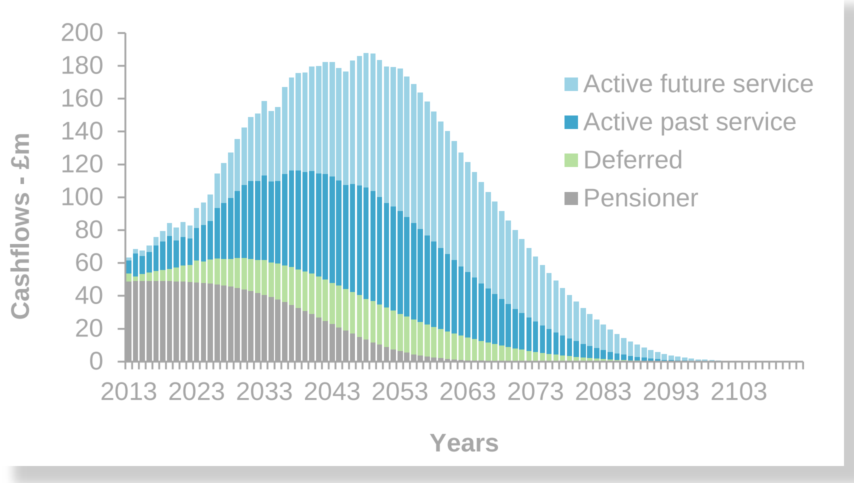
- Valuation Assumptions Briefing Note
- Funding Strategy Statement
- Valuation Report
- Rates and Adjustments Certificate

This update therefore complies with the following Technical Actuarial Standards (TASs):

- Reporting ("TAS R")
- Modelling ("TAS M")
- Data ("TAS D")
- Pensions TAS

How liabilities are calculated

- The future benefits that are payable from the Fund ("cash-flows") were calculated on a specific set of assumptions at the last valuation date.
- These cash-flows (on the ongoing funding basis) are shown below.
- These cash-flows were adjusted using available financial and Fund information to produce estimated cash-flows at post valuation dates.
- The specific information used for this update is set out on the next page.
- Market information is used to produce discount rates at these dates.
- The estimated cash-flows are discounted to produce the estimated liability value at a specific date.



How assets are calculated

Assets are projected from the valuation date allowing for actual or estimated Fund cash-flows and daily benchmark indices. Where available, asset values are recalibrated using known asset data.

The update allows for:

1 Movements in the value of the assets as measured by index returns and data from the administering authority where available.
2 Movements in liabilities as a result of changes in yields and hence inflation and discount rate assumptions.
3 Estimated cash-flows (contributions and benefit payments).
4 Expected accrual of benefits for employee members accrued since the last valuation (based on projected salary roll).
5 Demographic experience in line with assumptions.
6 Variations in liabilities arising from the changes in RPI since the valuation date differing relative to assumptions.
7 Benefit accrual in line with the 2014 scheme.

The update does not allow for:

1 Asset allocations differing from those assumed (other than when asset data is recalibrated based on available information).
2 The asset values as at the date of this report have not been based on audited Fund accounts.
3 Variations in liabilities arising from salary rises differing relative to assumptions.
4 Differences between estimated and actual salary roll of employees.
5 Variation between actual and expected demographic experience (e.g. early retirement or mortality).

Membership data

My calculations are based on the membership data provided for the most recent actuarial valuation. Details on the quality of this data and a data summary can be found in the last formal actuarial valuation report.

Limitations of this model

In the short term, the typical main contributors to funding position volatility are movements in the value of assets held, liability changes due to yield movements, benefit changes and deficit contributions to the Fund.

The accuracy of this type of funding update calculation is expected to decline over time. Differences between the position shown in this report and the position which a valuation would show can be significant; particularly if there have been volatile financial markets or material membership changes (these are more likely to occur in smaller Funds). It is not possible to fully assess the accuracy of this update without carrying out a full actuarial valuation.

If yield curves are not available at a funding update date this model uses approximate yield curves based on the movements in long-term gilt yields since the date of the last available yield curve. Liability calculations are performed on the valuation date, the funding update date, anniversaries of the valuation date and each month-end in between. Interpolation is used for other dates shown in graphs. Some asset classes are not easily tracked by the benchmark indices used in this model which can lead to significant differences between actual and projected asset values.

Indices used to update projected asset values

Some of the following indices have been used to update projected asset values in this funding update.

- FTSE 100
- FTSE 250
- FTSE Small Cap
- FTSE All Share
- FTSE All World Series North America (£)
- FTSE All World Series Japan (£)
- FTSE All World Series Developed Europe (£)
- FTSE All World Series Developed Asia Pacific (£)
- FTSE All World Series All World Developed Ex UK (£)
- FTSE All World Series All World Ex UK (£)
- FTSE All World Series All Emerging (£)
- UK Government Fixed Interest Gilts (Over 15 Years)
- UK Government Index-Linked Gilts (Over 5 Years)
- UK Government Index-Linked Gilts (Over 15 Years)
- iBoxx A rated UK Corporate Bonds (Over 15 Years)
- iBoxx AA rated UK Corporate Bonds (Over 15 Years)
- iBoxx AAA rated UK Corporate Bonds (Over 15 Years)
- iBoxx All Investment Grades rated UK Corporate Bonds (Over 15 Years)
- IPD Property
- Cash Indices LIBOR 1 Month

The indices are a standard list and are not necessarily the same indices that managers have been asked to track or beat. All indices used to estimate projected asset values are total return indices. However, the market indicators quoted in this report are price indices, as these are more widely recognised.

Market information used to update liability values

Some of the following market information has been used to update liabilities values in this funding update.

- Nominal gilt yield curves derived from Bank of England data
- RPI gilt inflation curve derived from Bank of England data
- Nominal swap curves derived from Bloomberg data
- Real swap curves derived from Bloomberg data
- Inflation volatilities derived from the swap market
- FTSE Actuaries UK Fixed Interest Gilts Yields (Over 15 Years)
- FTSE Actuaries Index-Linked Gilts (3% Inflation) Yields (Over 15 Years)
- iBoxx AA rated UK Corporate Bond Yields (Over 15 Years)

Note: Market yields displayed in the market indicators table are on an annual basis.

Pension Fund Investment Sub-Committee

21 July 2014

Rugby Borough Council Cleaning Contract

Recommendation

That the Pension Fund Investment Sub- Committee approves the retrospective admission of Superclean Services Wothorpe Limited as an employer to the Warwickshire Pension Fund in respect of the Rugby Borough Council Cleaning Contract.

1.0 Background

1.1 Rugby Borough Council (RBC) let a cleaning contract in June 2013 and the successful contractor is Superclean Services Wothorpe Limited (Superclean).

1.2 There is one member of the Local Government Pension Scheme (LGPS) affected by the letting of this contract.

1.3 The contract had previously been undertaken by another contractor who did not approach the Fund for an admission agreement.

2.0 Superclean Services Wothorpe Limited

2.1 Although Superclean had approached the Fund in 2013 for an admission agreement, no confirmation had been received from RBC that the contract had been awarded to Superclean.

2.2 Confirmation has now been received that RBC awarded the cleaning contract to Superclean with effect from 3 June 2013.

2.3 The Pension Fund's Actuary has been commissioned to calculate a Bond and contribution rate for this employer and once this is available officers will discuss this with Superclean and RBC concerning membership of the Fund and arrears due.

3.0 Next Steps

3.1 That the Sub - Committee approve the admission of Superclean provided officers have received satisfactory assurances concerning the payment of future and past contributions due.

3.2 The Pension Fund's legal advisers have commenced drafting an admission agreement.

	Name	Contact Information
Report Author	Neil Buxton, Pension Services Manager	neilbuxton@warwickshire.gov.uk 01926 412195
Head of Service	John Betts, Head of Finance	johnbetts@warwickshire.gov.uk 01926 412441
Strategic Director	David Carter, Strategic Head of Resources	davidcarter@warwickshire.gov.uk 01926 412564