TOWER HAMLETS

PENSIONS COMMITTEE

Wednesday, 25 November 2015 at 7.00 p.m.

Room MP701, 7th Floor, Town Hall, Mulberry Place, 5 Clove Crescent, London E14 2BG

This meeting is open to the public to attend.

Members:
Chair: Councillor Andrew Cregan
Vice Chair: Councillor Clare Harrisson

Councillor Abdul Mukit MBE, Councillor Candida Ronald, Councillor Suluk Ahmed, Councillor Harun Miah and Councillor Mohammed Mufti Miah

Co-opted Members:
Kehinde Akintunde (Unions Representative)
Tony Childs (Admitted Bodies Representative)

Deputies:
Councillor Abdul Asad, Councillor Shafiqul Haque, Councillor John Pierce, Councillor Rajib Ahmed and Councillor Rachel Blake

[The quorum for this body is 3 voting Members].

Contact for further enquiries:
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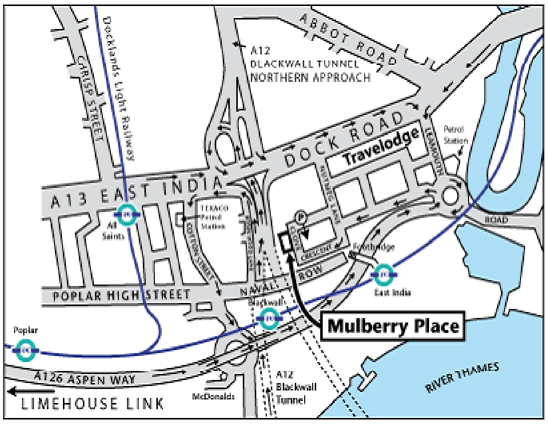

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APOLOGIES FOR ABSENCE

1. DECLARATIONS OF DISCLOSABLE PECUNIARY INTEREST — 1 - 4

To note any declarations of interest made by Members, including those restricting Members from voting on the questions detailed in Section 106 of the Local Government Finance Act, 1992. See attached note from the Monitoring Officer.

2. MINUTES OF THE PREVIOUS MEETING(S)

To confirm as a correct record the minutes of the meeting of the Committee held on 17 September 2015. (To follow)

3. PETITIONS

To receive any petitions relating to matters for which the Committee is responsible.

4. TRAINING - OVERVIEW OF THE PENSIONS REGULATOR CODE OF PRACTICE FOR PUBLIC SECTOR PENSIONS

Overview of the Pensions Regulator Code of Practice for Public Sector Pensions

5. REPORTS FOR CONSIDERATION

5 .1 The Pensions Regulator Code of Practice for Public Sector Pensions — 5 - 76

To consider the code of practice for the management of public sector pension schemes.

5 .2 Knowledge and Skills Audit

To receive a presentation from B Tobun, Investment and Treasury Manager.

6. ANY OTHER BUSINESS CONSIDERED TO BE URGENT

7. EXCLUSION OF THE PRESS AND PUBLIC

In view of the contents of the remaining items on the agenda the Committee is recommended to adopt the following motion:

“That, under the provisions of Section 100A of the Local Government Act 1972, as amended by the Local Government (Access to Information) Act 1985, the press and public be excluded from the remainder of the meeting for the consideration of the Section Two business on the grounds that it contains information defined as Exempt in Part 1 of Schedule 12A to the Local Government Act, 1972.”

EXEMPT SECTION (Pink Papers)

The exempt committee papers in the agenda will contain information, which is commercially, legally or personally sensitive and should not be divulged to third parties. If you do not wish to retain these papers after the meeting, please hand them to the Committee Officer present.

PAGE NUMBER(S)

7 .1 Update on Fixed Income Investment - Exempt Report

(Report to follow.)

Next Meeting of the Committee:

Thursday, 10 March 2016 at 7.00 p.m. to be held in Room MP702, 7th Floor, Town Hall, Mulberry Place, 5 Clove Crescent, London E14 2BG

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DECLARATIONS OF INTERESTS - NOTE FROM THE MONITORING OFFICER

This note is for guidance only. For further details please consult the Members' Code of Conduct at Part 5.1 of the Council's Constitution.

Please note that the question of whether a Member has an interest in any matter, and whether or not that interest is a Disclosable Pecuniary Interest, is for that Member to decide. Advice is available from officers as listed below but they cannot make the decision for the Member. If in doubt as to the nature of an interest it is advisable to seek advice **prior** to attending a meeting.

Interests and Disclosable Pecuniary Interests (DPIs)

You have an interest in any business of the authority where that business relates to or is likely to affect any of the persons, bodies or matters listed in section 4.1 (a) of the Code of Conduct; and might reasonably be regarded as affecting the well-being or financial position of yourself, a member of your family or a person with whom you have a close association, to a greater extent than the majority of other council tax payers, ratepayers or inhabitants of the ward affected.

You must notify the Monitoring Officer in writing of any such interest, for inclusion in the Register of Members' Interests which is available for public inspection and on the Council's Website.

Once you have recorded an interest in the Register, you are not then required to declare that interest at each meeting where the business is discussed, unless the interest is a Disclosable Pecuniary Interest (DPI).

A DPI is defined in Regulations as a pecuniary interest of any of the descriptions listed at **Appendix A** overleaf. Please note that a Member's DPIs include his/her own relevant interests and also those of his/her spouse or civil partner; or a person with whom the Member is living as husband and wife; or a person with whom the Member is living as if they were civil partners; if the Member is aware that that other person has the interest.

Effect of a Disclosable Pecuniary Interest on participation at meetings

Where you have a DPI in any business of the Council you must, unless you have obtained a dispensation from the authority's Monitoring Officer following consideration by the Dispensations Sub-Committee of the Standards Advisory Committee:-

- not seek to improperly influence a decision about that business; and
- not exercise executive functions in relation to that business.

If you are present at a meeting where that business is discussed, you must:-

- Disclose to the meeting the existence and nature of the interest at the start of the meeting or when the interest becomes apparent, if later; and
- Leave the room (including any public viewing area) for the duration of consideration and decision on the item and not seek to influence the debate or decision

When declaring a DPI, Members should specify the nature of the interest and the agenda item to which the interest relates. This procedure is designed to assist the public's understanding of the meeting and to enable a full record to be made in the minutes of the meeting.

Where you have a DPI in any business of the authority which is not included in the Member's register of interests and you attend a meeting of the authority at which the business is considered, in addition to disclosing the interest to that meeting, you must also within 28 days notify the Monitoring Officer of the interest for inclusion in the Register.

Further advice

For further advice please contact:-

Melanie Clay, Director of Law Probity and Governance 2017 364 4800

APPENDIX A: Definition of a Disclosable Pecuniary Interest

(Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012, Reg 2 and Schedule)

Subject	Prescribed description
Employment, office, trade, profession or vacation	Any employment, office, trade, profession or vocation carried on for profit or gain.
Sponsorship	Any payment or provision of any other financial benefit (other than from the relevant authority) made or provided within the relevant period in respect of any expenses incurred by the Member in carrying out duties as a member, or towards the election expenses of the Member. This includes any payment or financial benefit from a trade union within the meaning of the Trade Union and Labour Relations (Consolidation) Act 1992.
Contracts	Any contract which is made between the relevant person (or a body in which the relevant person has a beneficial interest) and the relevant authority— (a) under which goods or services are to be provided or works are to be executed; and (b) which has not been fully discharged.
Land	Any beneficial interest in land which is within the area of the relevant authority.
Licences	Any licence (alone or jointly with others) to occupy land in the area of the relevant authority for a month or longer.
Corporate tenancies	Any tenancy where (to the Member's knowledge)— (a) the landlord is the relevant authority; and (b) the tenant is a body in which the relevant person has a beneficial interest.
Securities	Any beneficial interest in securities of a body where— (a) that body (to the Member's knowledge) has a place of business or land in the area of the relevant authority; and (b) either— (i) the total nominal value of the securities exceeds £25,000 or one hundredth of the total issued share capital of that body; or (ii) if the share capital of that body is of more than one class, the total nominal value of the shares of any one class in which the relevant person has a beneficial interest exceeds one hundredth of the total issued share capital of that class.

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Non-Executive Report of the: **Pensions Committee** 25 November 2015	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
The Pensions Regulator Code of Practice for Public Sector Pensions	

Originating Officer(s)	Bola Tobun, Investment and Treasury Manager
Wards affected	All wards

Summary

In the past the Pensions Regulator (TPR) had very little responsibility in relation to oversight of public service pension schemes. Recently he has been provided with a range of oversight powers as well as a requirement to put in place codes of practice for public service pension schemes covering a number of areas relating to the management of schemes. The new Code of Practice for Public Service Pension Schemes comes into force from 1st April 2015 and all schemes must now consider whether they comply with the Code.

Recommendations:

The Pensions Committee is recommended to:

- Note the contents of the Code of Practice
- Note that a Compliance Checklist is being created which will be brought back to the February 2016 Pensions Committee.

1. REASONS FOR THE DECISIONS

1.1 There has been much greater focus on whether the governance of LGPS pension funds is appropriate. The introduction of Local Pension Boards and focus on increased training are just two areas which we have seen. TPR's greater legal powers of oversight extend this further and the Code of Practice is a useful means to understand what good practice looks like in these areas.

1.2 A good standard of governance is crucial in minimising the key risks involved in managing the Pension Fund. Although there are clear benefits for many schemes of the greater oversight powers that have been given to TPR, ensuring compliance with these areas and the much greater focus on governance results in additional work for officers and advisers of the Fund. Any costs associated with delivering the requirements of this Code and the related legal changes are immaterial in the context of the Pension Fund and any such costs are recharged to the Pension Fund.

2. ALTERNATIVE OPTIONS

2.1 There are no alternative options.

3. DETAILS OF REPORT

3.1 The Pension Regulator (TPR) finalised its 14th Code of Practice in January 2015 following a consultation with interested parties on the original draft and the Regulator's new powers under the Public Services Pensions Act 2013 (the 2013 Act). The new Code of Practice for Public Service Pension Schemes come into force in April 2015 and is attached as Appendix X.

3.2 Although following the code itself is not a regulatory requirement, should TPR identify a situation where the legal requirements are being breached, he will use the code as a core reference document when deciding appropriate action.

3.3 The matters covered by Code 14 are:
- knowledge and understanding for members of pension boards;
- conflicts of interest;
- publication of information about pension boards, governance and administration;
- internal controls;
- record-keeping;
- late payment of employer and employee contributions;
- information about member benefits and disclosure of information to members;
- internal dispute resolution, and
- reporting breaches of the law.

3.4 In light of the legal powers that have now been placed on TPR and the increasing focus on the governance of public service pension schemes, it is appropriate to consider whether the management of the London Borough of Tower Hamlets Pension Fund meets the overriding legal requirements and the recommended ways of working outlined in TPR's Code of Practice.

3.5 A compliance checklist is being developed which will allow the Pensions Committee and Pension Board to quickly identify any areas where improvements should be made. In the period between now and the February

2016 Pensions Committee, officers will produce this document to identify any areas which require attention.

3.6 Training will be provided at this meeting in relation to governance matters and this will include some elements of the Code, in particular the requirement to report breaches of the law.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 The comments of the Corporate Director of Resources have been incorporated into the report.

5. LEGAL COMMENTS

The Pensions Regulator Code of Practice for Public Sector Pensions came force on the 1st April 2015. The Code introduces the framework for the governance and administration of public service pension schemes and provides an extended regulatory oversight by the regulator. Codes of practice provide practical guidance in relation to the exercise of functions under relevant pensions legislation and set out the standards of conduct and practice expected of those who exercise the functions. The regulator is required under section 90(2) of the Pensions Act 2004, to issue one or more codes of practice covering specific matters relating to public service pension scheme. The Code is not a statement of the law and there are no penalties for failure to comply with its provisions. However the Authority must ensure that it complies with the underlying legal duties in respect of those matters specified in section 90(2). It is possible to adopt an alternative approach to that set out in the Code, however any such approach must meet any underlying legal duties of the scheme manager. Failure to do so may result in a penalty being imposed and the regulator also has the power to issue an improvement notice under section 13 of the Pensions Act 2004. The notice may be drafted with reference to the code of practice.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The Pension Fund Accounts demonstrate financial stewardship of the fund's assets. A financially viable and stable pension fund is a valuable recruitment and retention incentive for the Council.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The monitoring arrangement for the Pension Fund and the work of the officers, advisers and consultants should ensure that the Fund optimises the use of its resources in achieving the best returns for members of the Fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 Accounts provide an effective mechanism to safeguard the Council's assets and assess the risks associated with its activities.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no any Crime and Disorder Reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- NONE

Appendices

- Appendix X : The new Code of Practice for Public Service Pension Schemes

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report
The new Code of Practice for Public Service Pension Schemes

Officer contact details for documents:
Bola Tobun(Investment & Treasury Manager) x4733

Code of practice no. 14

Governance and administration of public service pension schemes

April 2015

The Pensions Regulator

The Pensions Regulator

Code of practice no. 14

Governance and administration of public service pension schemes

Presented to Parliament pursuant to Section 91(5) of the Pensions Act 2004
Draft to lie before Parliament for forty days, during which time either House may resolve that the code be not made.

Presented to the Northern Ireland Assembly pursuant to Article 86(5) of the Pensions (Northern Ireland) Order 2005
Draft to lie before the Northern Ireland Assembly for ten days on which the Assembly has sat or thirty calendar days whichever period is the longer, during which time the Assembly may resolve that the code be not made.

12 January 2015

Code of practice no. 14
Governance and administration of public service pension schemes

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Contents

Introduction

1. This code of practice is issued by The Pensions Regulator ('the regulator'), the body that regulates occupational and personal pension schemes provided through employers.

2. The regulator's statutory objectives[1] are to:

   - protect the benefits of pension scheme members
   - reduce the risks of calls on the Pension Protection Fund (PPF)
   - promote, and improve understanding of, the good administration of work-based pension schemes
   - maximise compliance with the duties and safeguards of the Pensions Act 2008
   - minimise any adverse impact on the sustainable growth of an employer (in relation to the exercise of the regulator's functions under Part 3 of the Pensions Act 2004 only).

3. The regulator has a number of regulatory tools, including issuing codes of practice, to enable it to meet its statutory objectives.

4. Codes of practice provide practical guidance in relation to the exercise of functions under relevant pensions legislation and set out the standards of conduct and practice expected from those who exercise those functions[2].

Status of codes of practice

5. Codes of practice are not statements of the law and there is no penalty for failing to comply with them. It is not necessary for all the provisions of a code of practice to be followed in every circumstance. Any alternative approach to that appearing in the code of practice will nevertheless need to meet the underlying legal requirements, and a penalty may be imposed if these requirements are not met. When determining whether the legal requirements have been met, a court or tribunal must take any relevant provisions of a code of practice into account[3].

6. If there are grounds to issue an improvement notice[4], the regulator may issue a notice directing a person to take, or refrain from taking, such steps as are specified in the notice. These directions may be worded by reference to a code of practice issued by the regulator[5].

This code of practice

7. The Public Service Pensions Act 2013 (the 2013 Act) introduces the framework for the governance and administration of public service pension schemes and provides an extended regulatory oversight by the regulator.

1
Section 5(1) of the Pensions Act 2004.

2
Section 90A(1), ibid.

3
Section 90A(5), ibid.

4
Where the regulator considers that legal requirements are not being met, or have been contravened in circumstances which make it likely that the breach will continue or be repeated, it may issue an improvement notice under s13 of the Pensions Act 2004.

5
Section 13(3) of the Pensions Act 2004.

8. The regulator is required to issue one or more codes of practice covering specific matters relating to public service pension schemes[6]. This code of practice sets out the legal requirements for public service pension schemes in respect of those specific matters. It contains practical guidance and sets out standards of conduct and practice expected of those who exercise functions in relation to those legal requirements.

9. The practical guidance sections in this code are not intended to prescribe the process for every scenario. They do, however, provide principles, examples and benchmarks against which scheme managers and members of pension boards can consider whether or not they have understood their duties and obligations and are reasonably complying with them.

10. If scheme managers and the members of pension boards are, for any reason, unable to act in accordance with the guidance set out in this code, or an alternative approach that meets the underlying requirements, they should consider their statutory duty under section 70 of the Pensions Act 2004 to assess and if necessary report breaches of the law[7]. For further information, see the section of this code on 'Reporting breaches of the law'.

At whom is this code directed?

11. This code relates to public service pension schemes within the meaning of the Pensions Act 2004[8]. These are schemes established under the 2013 Act, new public body pension schemes and other statutory pension schemes which are connected to those schemes. It does not apply to schemes in the wider public sector, nor to any scheme which is excluded from being a public service pension scheme within the meaning of the Pensions Act 2004.

12. This code is particularly directed at scheme managers and the members of pension boards of public service pension schemes and connected schemes. Scheme managers must comply with various legal requirements relating to the governance, management and administration of public service pension schemes. Pension boards must also comply with certain legal requirements, including assisting scheme managers in relation to securing compliance with scheme regulations and other legislation relating to the governance and administration of the scheme, any requirements of the regulator and with any other matters specified in scheme regulations. The role, responsibilities and duties of pension boards will vary. Where pension boards are not directly responsible for undertaking particular activities, they remain accountable for assisting the scheme manager in securing compliance with the scheme regulations and other legislation relating to the governance and administration of the scheme, any requirements of the regulator and with any other matters for which they are responsible under the scheme regulations[9].

6
Section 90A(2) of the Pensions Act 2004.

7
Section 70, ibid.

8
Section 318, ibid.

9
Section 5 of the Public Service Pensions Act 2013.

13. In addition, the legal requirement to report breaches of the law under section 70 of the Pensions Act 2004 applies to other persons involved in public service pension schemes, so this code is also directed at them.

14. Scheme managers and pension boards (where relevant) may be able to delegate some activities to others, or outsource them, although they will not be able to delegate their accountability for complying with a legal requirement imposed on them. This code should therefore be followed by anyone to whom activities relating to the legal requirements covered by this code have been delegated or outsourced.

15. Employers participating in public service pension schemes will also find the code a useful source of reference. The role and actions of employers can be critical in enabling scheme managers to meet certain legal requirements[10].

16. Public service pension schemes are established primarily as defined benefit (DB) schemes. Some of these schemes also enable members to make additional voluntary contributions (AVCs) on either a DB basis or to a separate defined contribution (DC) scheme. There are also some DC schemes which are offered as alternatives to the DB schemes. This code applies to any DC scheme which is a public service pension scheme within the meaning of the Pensions Act 2004.

Terms used in this code

17. **The 2013 Act** – the Public Service Pensions Act 2013, which sets out the arrangements for the creation of schemes for the payment of pensions and other benefits. It provides powers to ministers to create such schemes according to a common framework of requirements.

18. **Public service pension schemes**[11] – these are (a) new public service pension schemes set up under section 1 of the 2013 Act (including any scheme which has effect as such a scheme[12]); (b) new public body pension schemes (within the meaning of the 2013 Act) and (c) any statutory pension schemes connected with a scheme described in (a) or (b). Substantially, these are the schemes providing pension benefits for civil servants, the judiciary, local government workers, teachers, health service workers, fire and rescue workers, members of police forces and the armed forces. Except where specified otherwise, the legal requirements and practical guidance set out in this code apply to any kind of public service pension scheme within the meaning of the Pensions Act 2004, whether it is a scheme established under section 1 of the 2013 Act, a new public body scheme or a connected scheme.

10
Employers participating in occupational public service pension schemes are under a statutory duty to report breaches of the law under s70 of the Pensions Act 2004.

11
As defined in s318 of the Pensions Act 2004. Under s318(6) of that Act, a scheme which would otherwise fall within the definition of 'public service pension scheme' in the Pensions Act 2004 does not do so if it is a scheme providing only for injury or compensation benefits (or both), or if it is specified in an order made under that section.

12
Section 28 of the 2013 Act.

19. **Connected scheme** – a scheme established under section 1 of the 2013 Act and another statutory pension scheme, or a new public body pension scheme and another statutory pension scheme are connected if and to the extent that the schemes make provision in relation to persons of the same description. Scheme regulations may specify exceptions[13].

20. **Responsible authority** – the 2013 Act identifies secretaries of state/ministers, each being the responsible authority for their schemes, who have power to make the scheme regulations for the relevant schemes[14]. The responsible authority may also be the scheme manager[15]. In relation to a public body pension scheme, references in the code to the responsible authority are to be read as references to the public authority which established the scheme.

21. **Scheme regulations** – each new scheme made under section 1 of the 2013 Act has scheme regulations which set out the detail of the membership and benefits to be provided under the scheme[16]. The regulations must identify scheme managers and provide for the establishment of pension boards and scheme advisory boards. These regulations constitute the main rules of the scheme. In addition to the scheme regulations, the rules of a scheme include:

    - certain legislative provisions, to the extent that they override provisions of the scheme regulations, or which have effect in relation to a scheme and are not otherwise reflected in the scheme regulations, and
    - any provision which the scheme regulations do not contain but which the scheme rules must contain if it is to conform with the requirements of Chapter 1 of Part 4 of the Pension Schemes Act 1993 (preservation of benefit under occupational pension schemes)[17].

    Some connected schemes and new public body pension schemes will not be established by regulations, so references in the code to scheme regulations should be read as references to the rules of the scheme in these cases.

22. **Scheme manager** – each public service pension scheme has one or more persons responsible for managing or administering the scheme[18]. Public service pension schemes can have different persons acting as scheme manager for different parts of the pension scheme. For the locally administered schemes[19], the scheme managers may be the local administering authorities or a person representing an authority or police force.

13
Section 4(6) and (7) of the 2013 Act.

14
Section 2 and Schedule 2, ibid.

15
Section 4(3), ibid.

16
Section 3 and Schedule 3, ibid.

17
Section 318(2) of the Pensions Act 2004.

18
Section 4 and s30 of the 2013 Act.

19
Locally administered schemes include the schemes for England, and Wales, and Scotland for local government workers, and England and Wales for fire and rescue workers and members of police forces.

23. **Pension board** – the scheme manager (or each scheme manager) for a scheme has a pension board[20] with responsibility for assisting the scheme manager to comply with the scheme regulations and other legislation relating to the governance and administration of the scheme and any requirements imposed by the regulator. The pension board must also assist the scheme manager with such other matters as the scheme regulations may specify. It will be for scheme regulations and the scheme manager to determine precisely what the pension board's role, responsibilities and duties entail.

24. **Scheme advisory board** – each DB public service pension scheme has a scheme advisory board[21] with responsibility for providing advice on the desirability of changes to the scheme, when requested to do so by the responsible authority (or otherwise, in accordance with scheme regulations). Where there is more than one scheme manager the scheme regulations may also provide for the scheme advisory board to provide advice (on request or otherwise) to the scheme managers or the scheme's pension boards on the effective and efficient administration and management of the scheme or any pension fund of the scheme.

25. **Schemes** – in this code the term 'schemes' is used throughout where actions to comply with a legal requirement, standard or expectation may be carried out by the scheme manager, pension board or by another person(s) including those to whom activities have been delegated or outsourced. The scheme manager or pension board will be ultimately accountable, depending upon to whom the legal obligation applies under the legislation.

26. **Must** – in this code the term 'must' is used where there is a legal requirement.

27. **Should** – in this code the term 'should' is used to refer to practical guidance and the standards expected by the regulator.

How to use this code

28. The code is structured as a reference for scheme managers and pension boards to use to inform their actions in four core areas of scheme governance and administration: governing your scheme, managing risks, administration and resolving issues.

29. Each core section includes practical guidance to help scheme managers and pension boards to discharge their legal duties. The regulator recognises that there may be alternative and justifiable actions or approaches that scheme managers or pension boards may wish to adopt, provided these meet the minimum legal requirements.

30. Schemes will need to consider and apply the practical guidance to suit their own particular characteristics and arrangements.

20
Section 5 and s30(1) of the 2013 Act (in the case of new public body schemes, if the scheme has more than one member).

21
Section 7, ibid. This requirement only applies to schemes set up under s1 of the 2013 Act.

Northern Ireland

31. References to the law that applies in Great Britain should be taken to include corresponding legislation in Northern Ireland. References to HM Treasury directions should be taken to be directions by the Department of Finance and Personnel. The responsible authority for each scheme is the relevant government department[22].

32. The appendix to this code lists the corresponding references to Northern Ireland legislation.

22 Section 2 and Schedule 2 of the Public Service Pensions Act (Northern Ireland) 2014.

Governing your scheme

33. This part of the code covers:

- knowledge and understanding required by pension board members
- conflicts of interest and representation, and
- publishing information about schemes.

Knowledge and understanding required by pension board members

Legal requirements

34. A member of the pension board of a public service pension scheme must be conversant with:

- the rules of the scheme[23], and
- any document recording policy about the administration of the scheme which is for the time being adopted in relation to the scheme.

35. A member of a pension board must have knowledge and understanding of:

- the law relating to pensions, and
- any other matters which are prescribed in regulations.

36. The degree of knowledge and understanding required is that appropriate for the purposes of enabling the individual to properly exercise the functions of a member of the pension board[24].

Practical guidance

37. The legislative requirements about knowledge and understanding only apply to pension board members. However, scheme managers should take account of this guidance as it will support them in understanding the legal framework and enable them to help pension board members to meet their legal obligations.

38. Schemes[25] should establish and maintain policies and arrangements for acquiring and retaining knowledge and understanding to support their pension board members. Schemes should designate a person to take responsibility for ensuring that a framework is developed and implemented.

39. However, it is the responsibility of individual pension board members to ensure that they have the appropriate degree of knowledge and understanding to enable them to properly exercise their functions as a member of the pension board.

23
See paragraph 21 for the definition of the 'rules of the scheme'.

24
Section 248A of the Pensions Act 2004.

25
See paragraph 25 for the definition of 'schemes'.

Areas of knowledge and understanding required

40. Pension board members must be conversant with their scheme rules, which are primarily found in the scheme regulations[26], and documented administration policies currently in force for their pension scheme[27]. Being 'conversant' means having a working knowledge of the scheme regulations and policies, so that pension board members can use them effectively when carrying out their duties.

41. They must also have knowledge and understanding of the law relating to pensions (and any other matters prescribed in legislation) to the degree appropriate for them to be able to carry out their role, responsibilities and duties.

42. In terms of documented administration policies, specific documents recording policy about administration will vary from scheme to scheme. However, the following are examples of administration policies which the regulator considers to be particularly pertinent and would expect to be documented where relevant to a pension scheme, and with which pension board members must therefore be conversant where applicable[28]. This list is not exhaustive and other documented policies may fall into this category:

- any scheme-approved policies relating to:
  - conflicts of interest and the register of interests
  - record-keeping
  - internal dispute resolution
  - reporting breaches
  - maintaining contributions to the scheme
  - the appointment of pension board members
- risk assessments/management and risk register policies for the scheme
- scheme booklets, announcements and other key member and employer communications, which describe scheme policies and procedures
- the roles, responsibilities and duties of the scheme manager, pension board and individual pension board members
- terms of reference, structure and operational policies of the pension board and/or any sub-committee
- statements of policy about the exercise of discretionary functions

26
See paragraph 21 for the definition of the 'rules of the scheme'.

27
Section 248A(2) of the Pensions Act 2004.

28
Section 248A(2)(b) of the Pensions Act 2004.

- statements of policy about communications with members and scheme employers
- the pension administration strategy, or equivalent[29], and
- any admission body (or equivalent) policies.

43. For pension board members of funded pension schemes, documents which record policy about the administration of the scheme will include those relating to funding and investment matters. For example, where relevant they must be conversant with the statement of investment principles and the funding strategy statement[30].

44. Pension board members must also be conversant with any other documented policies relating to the administration of the scheme. For example, where applicable, they must be conversant with policies relating to:

    - the contribution rate or amount (or the range/variability where there is no one single rate or amount) payable by employers participating in the scheme
    - statements of assurance (for example, assurance reports from administrators)
    - third party contracts and service level agreements
    - stewardship reports from outsourced service providers (for example, those performing outsourced activities such as scheme administration), including about compliance issues
    - scheme annual reports and accounts
    - accounting requirements relevant to the scheme
    - audit reports, including from outsourced service providers, and
    - other scheme-specific governance documents.

45. Where DC or DC AVC options are offered, pension board members should also be familiar with the requirements for the payment of member contributions to the providers, the principles relating to the operation of those arrangements, the choice of investments to be offered to members, the provider's investment and fund performance report and the payment schedule for such arrangements.

46. Schemes should prepare and keep an updated list of the documents with which they consider pension board members need to be conversant. This will enable them to effectively carry out their role. They should make sure that both the list and the documents are available in accessible formats.

29
For the local government pension schemes, this might include information about the setting of performance targets or making agreements about levels of performance.

30
Section 248A(2)(b) of the Pensions Act 2004.

Degree of knowledge and understanding required

47. The roles, responsibilities and duties of pension boards and their individual members will vary between pension schemes. Matters for which the pension board is responsible will be set out in scheme regulations[31]. Clear guidance on the roles, responsibilities and duties of pension boards and the members of those boards should be set out in scheme documentation.

48. Schemes should assist individual pension board members to determine the degree of knowledge and understanding that is sufficient for them to effectively carry out their role, responsibilities and duties as a pension board member.

49. Pension board members must have a working knowledge of their scheme regulations and documented administration policies. They should understand their scheme regulations and policies in enough detail to know where they are relevant to an issue and where a particular provision or policy may apply.

50. Pension board members must have knowledge and understanding of the law relating to pensions (and any other prescribed matters) sufficient for them to exercise the functions of their role. Pension board members should be aware of the range and extent of the law relating to pensions which applies to their scheme, and have sufficient understanding of the content and effect of that law to recognise when and how it impacts on their responsibilities and duties.

51. Pension board members should be able to identify and where relevant challenge any failure to comply with:
    - the scheme regulations
    - other legislation relating to the governance and administration of the scheme
    - any requirements imposed by the regulator, or
    - any failure to meet the standards and expectations set out in any relevant codes of practice issued by the regulator.

52. Pension board members' breadth of knowledge and understanding should be sufficient to allow them to understand fully and challenge any information or advice they are given. They should understand how that information or advice impacts on any issue or decision relevant to their responsibilities and duties.

31 Section 5(2) of the 2013 Act.

53. Pension board members of funded pension schemes should ensure that they have the appropriate degree of knowledge and understanding of funding and investment matters relating to their scheme to enable them to effectively carry out their role. This includes having a working knowledge of provisions in their scheme regulations and administration policies that relate to funding and investment, as well as knowledge and understanding of relevant law relating to pensions.

54. All board members should attain appropriate knowledge so that they are able to understand the relevant law in relation to their scheme and role. The degree of knowledge and understanding required of pension board members may vary according to the role of the board member, as well as the expertise of the board member. For example, a board member who is also a pensions law expert (for instance, as a result of their day job) should have a greater level of knowledge than that considered appropriate for board members without this background.

Acquiring, reviewing and updating knowledge and understanding

55. Pension board members should invest sufficient time in their learning and development alongside their other responsibilities and duties. Schemes should provide pension board members with the relevant training and support that they require. Training is an important part of the individual's role and will help to ensure that they have the necessary knowledge and understanding to effectively meet their legal obligations.

56. Newly appointed pension board members should be aware that their responsibilities and duties as a pension board member begin from the date they take up their post. Therefore, they should immediately start to familiarise themselves with the scheme regulations, documents recording policy about the administration of the scheme and relevant pensions law. Schemes should offer pre-appointment training or arrange for mentoring by existing pension board members. This can also ensure that historical and scheme-specific knowledge is retained when pension board members change.

57. Pension board members should undertake a personal training needs analysis and regularly review their skills, competencies and knowledge to identify gaps or weaknesses. They should use a personalised training plan to document and address these promptly.

58. Learning programmes should be flexible, allowing pension board members to update particular areas of learning where required and to acquire new areas of knowledge in the event of any change. For example, pension board members who take on new responsibilities will need to ensure that they gain appropriate knowledge and understanding relevant to carrying out those new responsibilities.

59. The regulator will provide an e-learning programme to help meet the needs of pension board members, whether or not they have access to other learning. If schemes choose alternative learning programmes they should be confident that those programmes:

- cover the type and degree of knowledge and understanding required
- reflect the legal requirements, and
- are delivered within an appropriate timescale.

Demonstrating knowledge and understanding

60. Schemes should keep appropriate records of the learning activities of individual pension board members and the board as a whole. This will help pension board members to demonstrate steps they have taken to comply with legal requirements and how they have mitigated risks associated with knowledge gaps. A good external learning programme will maintain records of the learning activities of individuals on the programme or of group activities, if these have taken place.

Conflicts of interest and representation

Legal requirements

61. A conflict of interest is a financial or other interest which is likely to prejudice a person's exercise of functions as a member of the pension board. It does not include a financial or other interest arising merely by virtue of that person being a member of the scheme or any connected scheme for which the board is established[32].

62. In relation to the pension board, scheme regulations must include provision requiring the scheme manager to be satisfied:

- that a person to be appointed as a member of the pension board does not have a conflict of interest and
- from time to time, that none of the members of the pension board has a conflict of interest[33].

32
Section 5(5) of the 2013 Act defines a conflict of interest in relation to pension board members and s7(5) of that Act in relation to scheme advisory board members.

33
Section 5(4)(a), ibid.

63. Scheme regulations must require each member or proposed member of a pension board to provide the scheme manager with such information as the scheme manager reasonably requires for the purposes of meeting the requirements referred to above[34].

64. Scheme regulations must include provision requiring the pension board to include employer representatives and member representatives in equal numbers[35].

65. In relation to the scheme advisory board, the regulations must also include provision requiring the responsible authority to be satisfied:

- that a person to be appointed as a member of the scheme advisory board does not have a conflict of interest and
- from time to time, that none of the members of the scheme advisory board has a conflict of interest[36].

66. Scheme regulations must require each member of a scheme advisory board to provide the responsible authority with such information as the responsible authority reasonably requires for the purposes of meeting the requirements referred to above[37].

Practical guidance

67. This guidance is to help scheme managers to meet the legal requirement to be satisfied that pension board members do not have any conflicts of interest. The same requirements apply to responsible authorities in relation to scheme advisory boards, (apart from the requirement regarding employer and member representatives), but the regulator does not have specific responsibility for oversight of scheme advisory boards.

68. Actual conflicts of interest are prohibited by the 2013 Act and cannot, therefore, be managed. Only potential conflicts of interest can be managed.

69. A conflict of interest may arise when pension board members:

- must fulfil their statutory role[38] of assisting the scheme manager in securing compliance with the scheme regulations, other legislation relating to the governance and administration of the scheme and any requirements imposed by the regulator or with any other matter for which they are responsible, whilst
- having a separate personal interest (financial or otherwise), the nature of which gives rise to a possible conflict with their statutory role.

34
Section 5(4)(b) of the 2013 Act.

35
Section 5(4)(c), ibid.

36
Section 7(4)(a), ibid.

37
Section 7(4)(b), ibid.

38
Section 5(2), ibid.

70. Some, if not all, of the 'Seven principles of public life' (formerly known as the 'Nolan principles')[39] will already apply to people carrying out roles in public service pension schemes, for example through the Ministerial code, Civil Service code or other codes of conduct. These principles should be applied to all pension board members in the exercise of their functions as they require the highest standards of conduct. Schemes should incorporate the principles into any codes of conduct (and across their policies and processes) and other internal standards for pension boards.

71. Other legal requirements relating to conflicts of interest may apply to pension board members and/or scheme advisory board members[40]. The regulator may not have specific responsibility for enforcing all such legal requirements, but it does have a particular role in relation to pension board members and conflicts of interest. While pension board members may be subject to other legal requirements, when exercising functions as a member of a pension board they must meet the specific requirements of the 2013 Act and are expected to satisfy the standards of conduct and practice set out in this code.

72. It is likely that some pension board members will have dual interests, which may include other responsibilities. Scheme managers and pension board members will need to consider all other interests, financial or otherwise, when considering interests which may give rise to a potential or actual conflict. For example, a finance officer appointed as a pension board member can offer their knowledge and make substantial contributions to the operational effectiveness of the scheme, but from time to time they may be involved in a decision or matter which may be, or appear to be, in opposition to another interest. For instance, the pension board may be required to take or scrutinise a decision which involves the use of departmental resources to improve scheme administration, while the finance officer is at the same time tasked, by virtue of their employment, with reducing departmental spending. A finance officer might not be prevented from being a member of a pension board, but the scheme manager must be satisfied that their dual interests are not likely to prejudice the pension board member in the exercise of any particular function.

39
The Committee on Standards in Public Life has set out seven principles of public life which apply to anyone who works as a public office holder or in other sectors delivering public services: **www.gov.uk/government/publications/the-7-principles-of-public-life**.

40
For example, local government legislation applicable to English local authorities contains legal requirements relating to certain people about standards of conduct, conflicts of interest and disclosure of certain interests.

73. Scheme regulations will set out matters for which the pension board is responsible[41]. Schemes[42] should set out clear guidance on the roles, responsibilities and duties of pension boards and the members of those boards in scheme documentation. This should cover, for example, whether they have responsibility for administering or monitoring the administration of the scheme; developing, delivering or overseeing compliance with requirements for governance and/or administration policies; and taking or scrutinising decisions relating to governance and/or administration. Regardless of their remit, potential conflicts of interest affecting pension board members need to be identified, monitored and managed effectively.

74. Schemes should consider potential conflicts of interest in relation to the full scope of roles, responsibilities and duties of pension board members. It is recommended that all those involved in the management or administration of public service pension schemes take professional legal advice when considering issues to do with conflicts of interest.

A three-stage approach to managing potential conflicts of interest

75. Conflicts of interest can inhibit open discussions and result in decisions, actions or inactions which could lead to ineffective governance and administration of the scheme. They may result in pension boards acting improperly, or lead to a perception that they have acted improperly. It is therefore essential that any interests, which have the potential to become conflicts of interest or be perceived as conflicts of interest, are identified and that potential conflicts of interest (including perceived conflicts) are monitored and managed effectively.

76. Schemes should ensure that there is an agreed and documented conflicts policy and procedure, which includes identifying, monitoring and managing potential conflicts of interest. They should keep this under regular review. Policies and procedures should include examples of scenarios giving rise to conflicts of interest, how a conflict might arise specifically in relation to a pension board member and the process that pension board members and scheme managers should follow to address a situation where board members are subject to a potential or actual conflict of interest.

41
Section 5(2) of the 2013 Act.

42
See paragraph 25 for the definition of 'schemes'.

77. Broadly, schemes should consider potential conflicts of interest in three stages:

- identifying
- monitoring, and
- managing.

Identifying potential conflicts

78. Schemes should cultivate a culture of openness and transparency. They should recognise the need for continual consideration of potential conflicts. Disclosure of interests which have the potential to become conflicts of interest should not be ignored. Pension board members should have a clear understanding of their role and the circumstances in which they may find themselves in a position of conflict of interest. They should know how to manage potential conflicts.

79. Pension board members, and people who are proposed to be appointed to a pension board, must provide scheme managers with information that they reasonably require to be satisfied that pension board members and proposed members do not have a conflict of interest[43].

80. Schemes should ensure that pension board members are appointed under procedures that require them to disclose any interests, including other responsibilities, which could become conflicts of interest and which may adversely affect their suitability for the role, before they are appointed.

81. All terms of engagement, for example appointment letters, should include a clause requiring disclosure of all interests, including any other responsibilities, which have the potential to become conflicts of interest, as soon as they arise. All interests disclosed should be recorded. See the section of this code on 'Monitoring potential conflicts'.

82. Schemes should take time to consider what important matters or decisions are likely to be considered during, for example, the year ahead and identify and consider any potential or actual conflicts of interest that may arise in the future. Pension board members should be notified as soon as practically possible and mitigations should be put in place to prevent these conflicts from materialising.

43
Section 5(4)(b) of the 2013 Act and scheme regulations.

Monitoring potential conflicts

83. As part of their risk assessment process, schemes should identify, evaluate and manage dual interests which have the potential to become conflicts of interest and pose a risk to the scheme and possibly members, if they are not mitigated. Schemes should evaluate the nature of any dual interests and assess the likely consequences were a conflict of interest to materialise.

84. A register of interests should provide a simple and effective means of recording and monitoring dual interests and responsibilities. Schemes should also capture decisions about how to manage potential conflicts of interest in their risk registers or elsewhere. The register of interests and other relevant documents should be circulated to the pension board for ongoing review and published, for example on a scheme's website.

85. Conflicts of interest should be included as an opening agenda item at board meetings and revisited during the meeting, where necessary. This provides an opportunity for those present to declare any interests, including other responsibilities, which have the potential to become conflicts of interest, and to minute discussions about how they will be managed to prevent an actual conflict arising.

Managing potential conflicts

86. Schemes should establish and operate procedures which ensure that pension boards are not compromised by potentially conflicted members. They should consider and determine the roles and responsibilities of pension boards and individual board members carefully to ensure that conflicts of interest do not arise, nor are perceived to have arisen.

87. A perceived conflict of interest can be as damaging to the reputation of a scheme as an actual conflict of interest. It could result in scheme members and interested parties losing confidence in the way a scheme is governed and administered. Schemes should be open and transparent about the way they manage potential conflicts of interest.

88. When seeking to prevent a potential conflict of interest becoming detrimental to the conduct or decisions of the pension board, schemes should consider obtaining professional legal advice when assessing any option.

Examples of conflicts of interest

89. Below are some examples of potential or actual conflicts of interest which could arise, or be perceived to arise, in relation to public service pension schemes. These will depend on the precise role, responsibilities and duties of a pension board. The examples provided are for illustrative purposes only and are not exhaustive. They should not be relied upon as a substitute for the exercise of judgement based on the principles set out in this code and any legal advice considered appropriate, on a case-by-case basis.

    a. Investing to improve scheme administration versus saving money
    An employer representative, who may be a Permanent Secretary, finance officer or local councillor, is aware that system X would help to improve standards of record-keeping in the scheme, but it would be costly to implement. The scheme manager, for instance a central government department or local administering authority, would need to meet the costs of the new system at a time when there is internal and external pressure to keep costs down. In order to meet the costs of the new system, the scheme manager would need to find money, perhaps by using a budget that was intended for another purpose. This decision could prove unpopular with taxpayers. A conflict of interest could arise where the employer representative was likely to be prejudiced in the exercise of their functions by virtue of their dual interests.

    b. Outsourcing an activity versus keeping an activity in-house
    In an extension of the previous example, a member representative, who is also an employee of a participating employer, is aware that system X would help to improve standards of record-keeping in the scheme, but it would mean outsourcing an activity that is currently being undertaken in-house by their employer. The member representative could be conflicted if they were likely to be prejudiced in the exercise of their functions by virtue of their employment.

    c. Representing the breadth of employers or membership versus representing narrow interests
    An employer representative who happens to be employed by the administering authority and is appointed to the pension board to represent employers generally could be conflicted if they only serve to act in the interests of the administering authority, rather than those of all participating employers. Equally, a member representative, who is also a trade union representative, appointed to the pension board to represent the entire scheme membership could be conflicted if they only act in the interests of their union and union membership, rather than all scheme members.

d. Assisting the scheme manager versus furthering personal interests

i. A pension board member, who is also a scheme adviser, may recommend the services or products of a related party, for which they might derive some form of benefit, resulting in them not providing, or not being seen to provide, independent advice or services

ii. A pension board member who is involved in procuring or tendering for services for a scheme administrator, and who can influence the award of a contract, may be conflicted where they have an interest in a particular supplier, for example, a family member works there.

e) Sharing information with the pension board versus a duty of confidentiality to an employer

An employer representative has access to information by virtue of their employment, which could influence or inform the considerations or decisions of the pension board. They have to consider whether to share this information with the pension board in light of their duty of confidentiality to their employer. Their knowledge of this information will put them in a position of conflict if it is likely to prejudice their ability to carry out their functions as a member of the pension board.

Representation on pension boards

90. While scheme regulations must require pension boards to have an equal number of employer and member representatives[44], there is flexibility to design arrangements which best suit each scheme.

91. Arrangements should be designed with regard to the principles of proportionality, fairness and transparency, and with the aim of ensuring that a pension board has the right balance of skills, experience and representation (for example, of membership categories and categories of employers participating in the scheme). Those responsible for appointing members to a pension board should also consider the mix of skills and experience needed on the pension board in order for the board to operate effectively in light of its particular role, responsibilities and duties.

44
Section 5(4)(c) of the 2013 Act.

Publishing information about schemes

Legal requirements

92. The scheme manager for a public service scheme must publish information about the pension board for the scheme(s) and keep that information up-to-date[45].

93. The information must include:

- who the members of the pension board are
- representation on the board of members of the scheme(s), and
- the matters falling within the pension board's responsibility[46].

Practical guidance

Publication of pension board information

94. Scheme members will want to know that their scheme is being efficiently and effectively managed. Public service pension schemes should have a properly constituted, trained and competent pension board, which is responsible for assisting the scheme manager to comply with the scheme regulations and other legislation relating to the governance and administration of the scheme and requirements imposed by the regulator.

95. Scheme managers must publish the information required about the pension board and keep that information up-to-date[47]. This will ensure that scheme members can easily access information about who the pension board members are, how pension scheme members are represented on the pension board and the responsibilities of the board as a whole.

96. When publishing information about the identity of pension board members, the representation of scheme members and matters for which the board is responsible, schemes[48] should also publish useful related information about the pension board such as:

- the employment and job title (where relevant) and any other relevant position held by each board member
- the pension board appointment process
- who each pension board member represents
- the full terms of reference for the pension board, including details of how it will operate, and
- any specific roles and responsibilities of individual pension board members.

45
Section 6(1) of the 2013 Act.

46
Section 6(2), ibid.

47
Section 6(1), ibid.

48
See paragraph 25 for the definition of 'schemes'.

97. Schemes should also consider publishing information about pension board business, for example board papers, agendas and minutes of meetings (redacted to the extent that they contain confidential information and/or data covered by the Data Protection Act 1998). They should consider any requests for additional information to be published, to encourage scheme member engagement and promote a culture of transparency.

98. Scheme managers must ensure that information published about the pension board is kept up-to-date[49]. Schemes should have policies and processes to monitor all published data on an ongoing basis to ensure it is accurate and complete.

Other legal requirements

99. Scheme managers (or any other person specified in legislation) must comply with any other legal requirements relating to the publication of information about governance and administration. In particular, HM Treasury directions may require the scheme manager or responsible authority of a public service pension scheme to publish scheme information, including information about scheme administration and governance and may specify how and when information is to be published[50].

49
Section 6(1) of the 2013 Act.

50
Section 15, ibid.

Managing risks

100. This part of the code covers the requirement for scheme managers to establish and operate adequate internal controls.

Internal controls

Legal requirements

101. The scheme manager of a public service pension scheme must establish and operate internal controls. These must be adequate for the purpose of securing that the scheme is administered and managed in accordance with the scheme rules and in accordance with the requirements of the law.

102. For these purposes 'internal controls' means:

- arrangements and procedures to be followed in the administration and management of the scheme
- systems and arrangements for monitoring that administration and management, and
- arrangements and procedures to be followed for the safe custody and security of the assets of the scheme[51].

Practical guidance

103. Internal controls are systems, arrangements and procedures that are put in place to ensure that pension schemes are being run in accordance with the scheme rules (which for most public service pension schemes are set out in the scheme regulations) and other law. They should include a clear separation of duties, processes for escalation and decision making and documented procedures for assessing and managing risk, reviewing breaches of law and managing contributions to the scheme.

104. Good internal controls are an important characteristic of a well-run scheme and one of the main components of the scheme manager's role in securing the effective governance and administration of the scheme. Internal controls can help protect pension schemes from adverse risks, which could be detrimental to the scheme and members if they are not mitigated.

105. Scheme managers must establish and operate internal controls[52]. These should address significant risks which are likely to have a material impact on the scheme. Scheme managers should employ a risk-based approach and ensure that sufficient time and attention is spent on identifying, evaluating and managing risks and developing and monitoring appropriate controls. They should seek advice, as necessary.

51
Section 249A(5) and s249B of the Pensions Act 2004.

52
Section 249B, ibid.

Identifying risks

106. Before implementing an internal controls framework, schemes[53] should carry out a risk assessment. They should begin by:

- setting the objectives of the scheme
- determining the various functions and activities carried out in the running of the scheme, and
- identifying the main risks associated with those objectives, functions and activities.

107. An effective risk assessment process will help schemes to identify a wide range of internal and external risks, which are critical to the scheme and members. When identifying risks, schemes should refer to relevant sources of information, such as records of internal disputes and legislative breaches, the register of interests, internal and external audit reports and service contracts.

108. Once schemes have identified risks, they should record them in a risk register and review them regularly. Schemes should keep appropriate records to help scheme managers demonstrate steps they have taken to comply, if necessary, with legal requirements.

Evaluating risks and establishing adequate internal controls

109. Not all risks will have the same potential impact on scheme operations and members or the same likelihood of materialising. Schemes should consider both these areas when determining the order of priority for managing risks and focus on those areas where the impact and likelihood of a risk materialising is high.

110. Many pension schemes will already have adequate internal controls in place, some of which may apply to a variety of the functions of the administering authority. Schemes should review their existing arrangements and procedures to determine whether they can prevent and detect errors in scheme operations and help mitigate pension scheme-related risks. For example, schemes could obtain assurance about their existing controls through direct testing or by obtaining reports on controls. Any such review should be appropriate to the outcome of the risk evaluation.

111. Schemes should consider what internal controls are appropriate to mitigate the main risks they have identified and how best to monitor them. For example, the scheme manager(s) for a funded scheme should establish and operate internal controls that regularly assess the effectiveness of investment-related decision making. Scheme managers for all pension schemes should establish and operate internal controls that regularly assess the effectiveness of data management and record-keeping.

53
See paragraph 25 for the definition of 'schemes'.

Managing risks by operating internal controls

112. Schemes should consider a number of issues when designing internal controls to manage risks. The examples provided are for illustrative purposes only and are not exhaustive. They should not be relied upon as a substitute for the exercise of judgement, based on the principles set out in this code and any advice considered appropriate, particularly in light of any problems experienced in the past.

a. How the control is to be implemented and the skills of the person performing the control
For example, schemes should ensure that new employers participating in the scheme understand what member data are required and the process for supplying it. Where employers fail to supply the correct data or do not follow the correct process, schemes should ensure that the employer identifies the cause of the error and that appropriate action is taken to avoid recurrence, for example remedying a systemic error or providing the relevant training.

b. The level of reliance that can be placed on information technology solutions where processes are automated
For example, where scheme administration processes use an automated system, internal or external auditors could audit the system on an annual basis to assess whether it is capable of performing a required function and report any issues that are identified.

c. Whether a control is capable of preventing future recurrence or merely detecting an event that has already happened
For example, schemes should ensure that their systems support the maintenance and retention of good member records. This includes implementing procedures and controls which identify where systems are not fit for purpose, there are gaps in the data, the data are of a poor quality and/or there has been a loss of data.

d. The frequency and timeliness of a control process
For example, schemes should ensure that data are complete. They should undertake a data-cleansing or member-tracing exercise and review this on a regular basis (at least annually or at regular intervals that they consider appropriate for the scheme).

e. How the control will ensure that data are managed securely
For example, schemes should ensure that all staff, including temporary or contract staff, complete information management training before they are given access to sensitive data.

f. The process for flagging errors or control failures, and approval and authorisation controls
For example, schemes should ensure that member communications such as member information booklets are reviewed regularly, particularly where there are changes to the scheme. All relevant parties should be aware of how they should flag errors and the authorisation required before any changes are made to the communications.

Monitoring controls effectively

113. Risk assessment is a continual process and should take account of a changing environment and new and emerging risks, including significant changes in or affecting the scheme and employers who participate in the scheme.

114. For example, where relevant, schemes should put in place systems and processes for making an objective assessment of the strength of an employer's covenant (which should include analysis of their financial position, prospects and ability to pay the necessary employer contributions).

115. An effective risk assessment process will provide a mechanism to detect weaknesses at an early stage. Schemes should periodically review the adequacy of internal controls in:

- mitigating risks
- supporting longer-term strategic aims, for example relating to investments
- identifying success (or otherwise) in achieving agreed objectives, and
- providing a framework against which compliance with the scheme regulations and legislation can be monitored.

116. Internal or external audits and/or quality assurance processes should ensure that adequate internal controls are in place and being operated effectively. Reviews should take place when substantial changes take place, such as changes to pension scheme personnel, implementation of new administration systems or processes, or where a control has been found to be inadequate.

117. A persistent failure to put in place adequate internal controls may be a contributory cause of an administrative breach. Where the effect and wider implications of not having in place adequate internal controls are likely to be 'materially significant', the regulator would expect to receive a whistleblowing report that outlines relevant information relating to the breach. For more information, see the 'Reporting breaches of the law' section of this code.

118. Ultimately, the legal responsibility for establishing and operating adequate internal controls rests with the scheme manager[54]. Scheme regulations or other documents may delegate responsibilities to pension board members or others – for example identifying, evaluating and managing risks, developing and maintaining appropriate controls and providing assurance to the scheme manager about any controls in place. However, accountability for those controls and the governance of policies, procedures and processes will reside with the scheme manager.

Outsourcing services

119. The legal requirements relating to internal controls apply equally where schemes outsource services connected with the running of the scheme. Providers should be required to demonstrate that they will have adequate internal controls in their tenders for delivering services. The requirements should be incorporated in the terms of engagement and contract between the scheme and service provider. Outsourced services may include, for example, the maintenance of records and data, calculation of benefits and investment management services. Where services are outsourced, scheme managers should be satisfied that internal controls associated with those services are adequate and effective.

120. An increasing number of service providers are obtaining independent assurance reports to help demonstrate their ability to deliver quality administration services. Schemes should ask their service providers to demonstrate that they have adequate internal controls relating to the services they provide. It is vital that schemes ensure they receive sufficient assurance from service providers. For example, the information from providers should be sufficiently detailed and comprehensive and the service level agreements should cover all services that are outsourced. Schemes should also consider including provisions in contracts for outsourced services requiring compliance with appropriate standards. This should help to ensure effective administration.

54
Section 249B of the Pensions Act 2004.

Administration

121. This part of the code covers:

- scheme record-keeping
- maintaining contributions, and
- providing information to members.

Scheme record-keeping

Legal requirements

122. Scheme managers must keep records of information relating to:

- member information[55]
- transactions[56], and
- pension board meetings and decisions[57].

123. The legal requirements are set out in the Public Service Pensions (Record Keeping and Miscellaneous Amendments) Regulations 2014 ('the Record Keeping Regulations').

Practical guidance

124. Failure to maintain complete and accurate records and put in place effective internal controls to achieve this can affect the ability of schemes[58] to carry out basic functions. Poor record-keeping can result in schemes failing to pay benefits in accordance with scheme regulations, processing incorrect transactions and ultimately paying members incorrect benefits. For funded schemes, it may lead to schemes managing investment risks ineffectively. There is also the potential for the maladministration of members' contributions and failure to identify any misappropriation of assets. Schemes should be able to demonstrate to the regulator, where required, that they keep accurate, up-to-date and enduring records to be able to govern and administer their pension scheme efficiently.

125. Scheme managers must establish and operate adequate internal controls[59], which should include processes and systems to support record-keeping requirements and ensure that they are effective at all times.

55
Regulation 4 of the Record Keeping Regulations.

56
Regulation 5, ibid.

57
Regulation 6, ibid.

58
See paragraph 25 for the definition of 'schemes'.

59
Section 249B of the Pensions Act 2004.

Records of member information

126. Scheme managers must ensure that member data across all membership categories specified in the Record Keeping Regulations is complete and accurate[60]. Member data should be subject to regular data evaluation.

127. Scheme managers must keep specific member data[61], which will enable them to uniquely identify a scheme member and calculate benefits correctly. This is particularly important with the establishment of career average revalued earnings (CARE) schemes. Scheme managers must be able to provide members with accurate information regarding their pension benefits (accrued benefits to date and their future projected entitlements) in accordance with legislative requirements[62], as well as pay the right benefits to the right person (including all beneficiaries) at the right time.

128. Schemes should require participating employers to provide them with timely and accurate data in order for the scheme manager to be able to fulfil their legal obligations. Schemes should seek to ensure that processes are established by employers which enable the transmission of complete and accurate data from the outset. Processes will vary from employer to employer, depending on factors such as employee turnover, pay periods, number of employees who are members and the timing and number of payroll processing systems.

129. Schemes should seek to ensure that employers understand the main events which require information about members to be passed from the employer to the scheme and/or another employer, such as when an employee:

- joins or leaves the scheme
- changes their rate of contributions
- changes their name, address or salary
- changes their member status, and
- transfers employment between scheme employers.

130. Schemes should ensure that appropriate procedures and timescales are in place for scheme employers to provide updated information when member data changes, for checking scheme data against employer data and for receiving information which may affect the profile of the scheme. If an employer fails to act according to the procedures set out above, meaning that they and/or scheme managers may not be complying with legal requirements, those under a statutory duty to report breaches of the law to the regulator under section 70 of the Pensions Act 2004 should assess whether there has been a relevant breach and take action as necessary.

60
Section 16 and s30 of the 2013 Act. Regulation 4 of the Record Keeping Regulations specifies member records which must be kept. The Data Protection Act 1998 requires personal data to be accurate and up-to-date.

61
Regulation 4 of the Record Keeping Regulations.

62
Legislative requirements include s14 of the 2013 Act, HM Treasury directions made under that section, and the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013.

Records of transactions

131. Schemes should be able to trace the flow of funds into and out of the scheme and reconcile these against expected contributions and scheme costs. In doing so, they will have clear oversight of the core scheme transactions and should be able to mitigate risks swiftly.

132. Scheme managers must keep records of transactions made to and from the scheme and any amount due to the scheme which has been written off[63]. They should be able to demonstrate that they do so.

Records of pension board meetings and decisions

133. Scheme managers must keep records of pension board meetings including any decisions made[64]. Schemes should also keep records of key discussions, which may include topics such as compliance with policies relating to administration of the scheme.

134. Scheme managers must also keep records relating to any decision taken by members of the pension board other than at a pension board meeting, or taken by a committee/sub-committee, which has not been ratified by the pension board. The records must include the date, time and place of the decision and the names of board members participating in that decision[65]. This will ensure that there is a clear and transparent audit trail of the decisions made in relation to the scheme.

Retention of scheme records

135. Schemes should retain records for as long as they are needed. It is likely that data will need to be held for long periods of time and schemes will need to retain some records for a member even after that individual has retired, ensuring that pension benefits can be properly administered over the lifetime of the member and their beneficiaries. Schemes should have in place adequate systems and processes to enable the retention of records for the necessary time periods.

Ongoing monitoring of data

136. Schemes should have policies and processes that monitor data on an ongoing basis to ensure it is accurate and complete, regardless of the volume of scheme transactions. This should be in relation to all membership categories, including pensioner member data where queries may arise once the pension is being paid.

137. Schemes should adopt a proportionate and risk-based approach to monitoring, based on any known or historical issues that may have occurred in relation to the scheme's administration. This is particularly important for the effective administration of CARE pension schemes, which requires schemes to hold significantly more data than needed for final salary schemes.

63
Regulation 5 of the Record Keeping Regulations.

64
Regulation 6, ibid.

65
Ibid.

Data review exercise

138. Schemes should continually review their data and carry out a data review exercise at least annually. This should include an assessment of the accuracy and completeness of the member information data held. Schemes should decide the frequency and nature of the review in light of factors such as the level of data quality, any issues identified and key scheme events.

139. Where the management of scheme data has been outsourced, it is vital that schemes understand and are satisfied that the controls in place will ensure the integrity of scheme member data. They should ensure that the administrator has assessed the risks that poor or deficient member records may present to the scheme and has taken the necessary steps to mitigate them, where applicable.

140. Where there has been a change of administrator or the administration system/platform, schemes should review and cleanse data records and satisfy themselves that all data are complete and accurate.

Data improvement plan

141. Where schemes identify poor quality or missing data, they should put a data improvement plan in place to address these issues. The plan should have specific data improvement measures which schemes can monitor and a defined end date within a reasonable timeframe when the scheme will have complete and accurate data.

Reconciliation of member records

142. Schemes should ensure that member records are reconciled with information held by the employer, for example postal address or electronic address (email address) changes and new starters. Schemes should also ensure that the numbers of scheme members is as expected based on the number of leavers and joiners since the last reconciliation. Schemes should be able to determine those members who are approaching retirement, those who are active members and those who are deferred members.

Data protection and internal controls

143. Schemes must ensure that processes that are created to manage scheme member data meet the requirements of the Data Protection Act 1998 and the data protection principles.

144. Schemes should understand:

- their obligations as data controllers and who the data processors are in relation to the scheme
- the difference between personal data and sensitive personal data (as defined in the Data Protection Act 1998)
- how data are held and how they should respond to data requests from different parties
- the systems which need to be in place to store, move and destroy data, and
- how data protection affects member communications.

Other legal requirements

145. In addition to the requirements set out in the Record Keeping Regulations, there are various other legal requirements that relate to record-keeping in public service pension schemes. Those requirements apply variously to managers, administrators and employers. Not all requirements apply to all public service pension schemes, but some of the key requirements are set out under the following legislation:

- Pensions Act 1995 and 2004
- Pensions Act 2008 and the Employers' Duties (Registration and Compliance) Regulations 2010[66]
- Occupational Pension Schemes (Scheme Administration) Regulations 1996
- Registered Pension Schemes (Provision of Information) Regulations 2006
- Data Protection Act 1998, and
- Freedom of Information Act 2000.

146. Where applicable, schemes should be able to demonstrate that they keep records in accordance with these and any other relevant legal requirements. Schemes should read the relevant legislation and any guidance in conjunction with this code where applicable.

66
See the regulator's guidance about automatic enrolment for more information about record-keeping requirements under this legislation.

Maintaining contributions

Legal requirements

147. Employer contributions must be paid to the scheme in accordance with any requirements in the scheme regulations. Where employer contributions are not paid on or before the date they are due under the scheme and the scheme manager has reasonable cause to believe that the failure is likely to be of material significance to the regulator in the exercise of any of its functions, the scheme manager must give a written report of the matter to the regulator as soon as reasonably practicable[67].

148. Where employee contributions are deducted from a member's pay, the amount deducted must be paid to the managers of the scheme at the latest by the 19th day of the month following the deduction, or by the 22nd day if paid electronically (the 'prescribed period')[68], or earlier if required by scheme regulations. References to 'days' means all days. References to 'working days' do not include Saturdays, Sundays or Bank Holidays.

149. Where employee contributions are not paid within the prescribed period, if the scheme manager[69] has reasonable cause to believe that the failure is likely to be of material significance to the regulator in the exercise of any of its functions, they must give notice of the failure to the regulator and the member within a reasonable period after the end of the prescribed period[70]. Where there is a failure to pay employee contributions on an earlier date in accordance with scheme regulations, schemes should also consider their statutory duty under section 70 of the Pensions Act 2004 to assess and if necessary report breaches of the law. For more information about reporting breaches of the law, see this section of the code.

Practical guidance

150. As part of the requirement to establish and operate adequate internal controls, scheme managers should ensure that there are effective procedures and processes in place to identify payment failures that are – and are not – of material significance to the regulator. A 'payment failure' is where contribution payments are not paid to the scheme by the due date(s), or within the prescribed period and a 'materially significant payment failure' refers to a payment failure which is likely to be of material significance to the regulator in the exercise of its functions.

151. Schemes[71] should monitor pension contributions, resolve payment issues and report payment failures, as appropriate, so that the scheme is administered and managed in accordance with the scheme regulations and other legal requirements.

67
Section 70A of the Pensions Act 2004.

68
Section 49(8) of the Pensions Act 1995 and regulation 16 of the Occupational Pension Schemes (Scheme Administration) Regulations 1996.

69
The legal requirement to report late payments of employee contributions is imposed on the 'managers' of a scheme, which the regulator generally takes to be the 'scheme manager' identified in scheme regulations in accordance with the 2013 Act.

70
Section 49(9) of the Pensions Act 1995.

71
See paragraph 25 for the definition of 'schemes'.

152. Adequate procedures and processes are likely to involve:

- developing a record to monitor the payment of contributions
- monitoring the payment of contributions
- managing overdue contributions, and
- reporting materially significant payment failures.

153. These procedures and processes should help scheme managers to meet their statutory duty to report materially significant payment failures to the regulator, as well as ensuring the effective management of scheme contributions and payment of the right pension.

Developing a record for monitoring the payment of contributions

154. There are legislative requirements for managers of DB schemes to keep a schedule of contributions; and for DC schemes, a payment schedule, which allows managers to monitor contributions to their scheme. There are various exemptions from these requirements including for DB and DC schemes which are established by or under an enactment and which are guaranteed by a Minister of the Crown or other public authority, and for DB schemes which are pay-as-you-go schemes[72].

155. Public service pension schemes which meet these exemptions should nonetheless develop a record for monitoring the payment of contributions to the scheme (a contributions monitoring record, which must reflect any requirements in scheme regulations where relevant). Schemes should prepare the contributions monitoring record in consultation with employers.

156. A contributions monitoring record will enable schemes to check whether contributions have been paid on time and in full, and, if they have not, provide a trigger for escalation for schemes to investigate the payment failure and consideration of whether scheme managers need to report to the regulator and, where relevant, members.

157. A contributions monitoring record should include the following information:

- contribution rates
- the date(s) on or before which employer contributions are to be paid to the scheme
- the date by when, or period within which, the employee contributions are to be paid to the scheme
- the rate or amount of interest payable where the payment of contributions is late.

72
Exemptions from the requirement to secure a schedule of contributions in respect of DB schemes under s227 of the Pensions Act 2004 are in regulation 17 of the Occupational Pension Schemes (Scheme Funding) Regulations 2005. Exemptions from the requirement to secure a payment schedule in respect of DC schemes under s87 of the Pensions Act 1995 is in regulation 17 of the Occupational Pension Schemes (Scheme Administration) Regulations 1996.

158. The date when employer contributions must be paid is the date on or before which they are due under the scheme in accordance with the scheme regulations (or other scheme documentation). Schemes should assess the timing of payments against the date specified.

159. While there is a legal requirement for employee contributions to be paid to the scheme by the 19th day of the month following deduction, or by the 22nd day if paid electronically, this does not override any earlier time periods required by the scheme regulations. There are special rules for the first deduction of contributions on automatic enrolment under the Pensions Act 2008[73].

160. A contributions monitoring record should help schemes to identify any employers who are not paying contributions on time and/or in full, support schemes to ensure that contributions are paid and employers to develop and implement new processes, as appropriate. The contributions monitoring record should provide schemes with information to maintain records of money received and will be useful for schemes to ensure that their member records are kept up-to-date.

Monitoring the payment of contributions

161. Schemes should monitor contributions on an ongoing basis for all the membership categories within the scheme. Schemes should regularly check payments due against the contributions monitoring record.

162. Schemes should apply a risk-based and proportionate approach to help identify employers and situations which present a higher risk of payment failures occurring and which are likely to be of material significance and require the scheme manager to intervene.

163. Schemes should be aware of what is to be paid in accordance with the contributions monitoring record or other scheme documentation, which may be used by the pension scheme. Schemes should also have a process in place to identify where payments are late or have been underpaid, overpaid or not paid at all.

164. For schemes to effectively monitor contributions they will require access to certain information. Employers will often provide the payment information that schemes need to monitor contributions at the same time as they send the contributions to the scheme, which may be required under the scheme regulations. Payment information may include:

- the employer and employee contributions due to be paid, which should be specified in the scheme regulations and/or other scheme documentation
- the pensionable pay that contributions are based upon (where required), and
- due date(s) on or before which payment of contributions and other amounts are to be made.

73
Regulation 16 of the Occupational Pension Schemes (Scheme Administration) Regulations 1996.

165. Schemes should have adequate internal controls in place to monitor the sharing of payment information between the employer, pension scheme and member. Where the necessary payment information is not automatically available or provided by employers, schemes should request the additional information they need. Schemes may not need to obtain payment information as a matter of course, only where it is required for effective monitoring.

166. Scheme managers must record and retain information on transactions, including any employer and employee contributions received and payments of pensions and benefits[74], which will support them in their administration and monitoring responsibilities.

167. Where the administration of scheme contributions is outsourced to a service provider, schemes should ensure that there is a process in place to obtain regular information on the payment of contributions to the scheme and a clear procedure in place to enable them to identify and resolve payment failures which may occur.

Managing overdue contributions

168. When schemes identify or are notified of a problem, they should assess whether a payment failure has occurred before taking steps to resolve and, if necessary, report it. During their assessment, schemes should take into account:

- legitimate agreed payments made directly by an employer for scheme purposes, ie where the scheme has agreed that a contributions payment can be made late due to exceptional circumstances
- legitimate agreed payment arrangements made between an employee and employer, ie where the employer has agreed that a contribution payment can be made late due to exceptional circumstances
- contributions paid directly to a pension provider, scheme administrator or investment manager
- any AVCs included with an employer's overall payment.

169. Where schemes identify a payment failure, they should follow a process to resolve issues quickly. This should normally involve the following steps:

a. Investigate any apparent employer failure to pay contributions in accordance with the contributions monitoring record or legal requirements.

b. Contact the employer promptly to alert them to the payment failure and to seek to resolve the overdue payment.

74
Regulation 5 of the Record Keeping Regulations.

c. Discuss it further with the employer as soon as practicable to find out the cause and circumstances of the payment failure.

d. Ask the employer to resolve the payment failure and take steps to avoid a recurrence in the future.

170. Schemes should maintain a record of their investigation and communications between themselves and the employer. Recording this information will help to provide evidence of schemes' effective monitoring processes and could help to demonstrate that the scheme manager has met the legal requirement to establish and operate adequate internal controls. It will also form part of the decision of whether or not to report a payment failure to the regulator and, where relevant, members.

171. The regulator recognises that a monitoring process based on information provided by employers may not be able to confirm deliberate underpayment or non-payment, or fraudulent behaviour by an employer. Schemes should review current processes or develop a new process which is able to detect situations where fraud may be more likely to occur and where additional checks may be appropriate.

172. Ultimately, schemes have flexibility to design their own procedures so that they can obtain overdue payments and rectify administrative errors in the most effective and efficient way for their particular scheme.

Reporting payment failures which are likely to be of material significance to the regulator

173. Scheme managers must report payment failures which are likely to be of material significance to the regulator within a reasonable period, in the case of employee contributions; and as soon as reasonably practicable in the case of employer contributions[75].

174. Where schemes identify a payment failure, they should attempt to recover contributions within 90 days from the due date or prescribed period having passed without full payment of the contribution.

175. While schemes are not expected to undertake a full investigation to establish materiality or investigate whether an employer has behaved fraudulently, schemes should ask the employer:

- the cause and circumstances of the payment failure
- what action the employer has taken as a result of the payment failure, and
- the wider implications or impact of the payment failure.

75
Section 49(9)(b) of the Pensions Act 1995 and s70A of the Pensions Act 2004.

176. When reaching a decision about whether to report, schemes should consider these points together and establish whether they have reasonable cause to report.

177. Having reasonable cause means more than merely having a suspicion that cannot be substantiated. Schemes should investigate the payment failure and use their judgement when deciding whether to report to the regulator.

178. Schemes may choose to take an employer's response to their enquiries at face value if they have no reason to believe it to be untrue or where their risk-based process indicates that there is a low risk of continuing payment failure. Where they receive no response, schemes may infer that an employer is unwilling to pay the contributions due.

179. Examples of payment failures that are likely to be of material significance to the regulator include:

- where schemes have reasonable cause to believe that the employer is neither willing nor able to pay contributions, for example in the event of a business failure or where an employer becomes insolvent and is unable to make pension payments
- where there is a payment failure involving possible dishonesty or a misuse of assets or contributions, for example where schemes have concerns that an employer is retaining and using contributions to manage cash flow difficulties or where schemes have become aware that the employer has transferred contributions elsewhere other than to the pension scheme, which may be misappropriation
- where the information available to schemes may indicate that the employer is knowingly concerned with fraudulently evading their obligation to pay employee contributions
- where schemes become aware that the employer does not have adequate procedures or systems in place to ensure the correct and timely payment of contributions due and the employer does not appear to be taking adequate steps to remedy the situation, for example where there are repetitive and regular payment failures, or
- any event where contributions have been outstanding for 90 days from the due date, unless the payment failure was a one-off or infrequent administrative error that had already been corrected on discovery or is thereafter corrected as soon as possible.

180. Examples of payment failures which are not likely to be of material significance to the regulator include:

- where a payment arrangement is being met by an employer for the recovery of outstanding contributions, or
- where there are infrequent one-off payment failures or administrative errors such as where employees leave or join the scheme and those occasional failures or errors have been corrected within 90 days of the due date.

181. Schemes should identify and report to the regulator, as appropriate, any payment failures that may not be of material significance taken individually, but which could indicate a systemic problem. For example, an employer consistently failing to pay contributions by the due date or within the prescribed period, but paying within 90 days, may be due to inefficient scheme systems and processes. Schemes may also need to report payment failures that occur repeatedly and are likely to be materially significant to the regulator, depending on the circumstances.

182. Reporting payment failures of employer contributions as soon as 'reasonably practicable' means within a reasonable period from the scheme manager having reasonable cause to believe that the payment failure is likely to be of material significance to the regulator. Schemes should also consider whether it may be appropriate to report a payment failure of employer contributions to scheme members.

183. A reasonable period for reporting would be within ten working days from having reasonable cause to believe that the payment failure is likely to be of material significance. This will depend upon the seriousness of the payment failure and impact on the scheme. A written report should be preceded by a telephone call, if appropriate.

184. In the case of an employer failing to pay employee contributions to the pension scheme, if the scheme manager has reasonable cause to believe that the payment failure is likely to be of material significance to the regulator, the failure must be reported to the regulator[76] and members within a reasonable period after the end of the prescribed period[77]. A reasonable period for reporting to the regulator would be within ten working days and to members within 30 days of having reported to the regulator.

185. Reports relating to payment failures of employer contributions must be made in writing (preferably using our Exchange online service)[78]. In exceptional circumstances the scheme manager could make a telephone report.

76
Reporting to the regulator does not affect any responsibility to report to another person or organisation.

77
S49(8) and (9) of the Pensions Act 1995 and regulation 16 of the Occupational Pension Schemes (Scheme Administration) Regulations 1996. Where there is a failure to pay employee contributions on an earlier date in accordance with scheme regulations, schemes should also consider their statutory duty under s70 of the Pensions Act 2004 to assess and if necessary report breaches of the law.

78
Section 70A of the Pensions Act 2004.

186. The regulator has standardised reporting procedures and expectations regarding content, format and channel. For more information, see the section of this code on 'Reporting breaches of the law'.

Providing information to members

Legal requirements

187. The law requires schemes[79] to disclose information about benefits and scheme administration to scheme members and others. This section summarises the legal requirements relating to benefit statements and certain other information which must be provided and should be read alongside the requirements in the 2013 Act, HM Treasury directions[80] and the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 ('the Disclosure Regulations 2013'). In addition to these duties, there are other legal requirements relating to the provision of information to members and others under other legislation. See paragraph 211 for further details.

Benefit statements

For active members of DB schemes under the 2013 Act

188. Scheme regulations must require scheme managers to provide an annual benefit information statement to each active member of a DB scheme established under the 2013 Act or new public body scheme[81]. The statement must include a description of the benefits earned by a member in respect of their pensionable service[82].

189. The first statement must be provided no later than 17 months after the scheme regulations establishing the scheme come into force. Subsequent statements must be provided at least annually after that date[83].

190. Statements must also comply with HM Treasury directions in terms of any other information which must be included and the manner in which they must be provided to members[84].

For active, deferred or pension credit members of any DB public service pension scheme under the Disclosure Regulations 2013

191. Managers[85] of a scheme must also provide a benefit statement following a request by an active, deferred or pension credit member of a DB scheme if the information has not been provided to that member in the previous 12 months before that request[86].

79
See paragraph 25 for the definition of 'schemes'.

80
Section 14 of the 2013 Act.

81
Section 14(1) and s30(1) of the 2013 Act.

82
Section 14(2)(a), ibid.

83
Section 14(4) and (5), ibid.

84
Section 14(2)(b) and (6), ibid.

85
The Occupational Pension Schemes (Managers) Regulations 1986 specify who is to be treated as the 'manager' (in certain occupational public service pension schemes) for the purpose of providing information under specified legislation, including the Disclosure Regulations 2013, which may differ from the person who is the 'scheme manager'.

86
Regulation 16 of the Disclosure Regulations 2013.

192. These benefit statements must include information about the amount of benefits by reference to a particular date and how they are calculated[87]. The full details depend on the type of member making the request.

193. The information must be given as soon as practicable but no more than two months after the date the request is made[88].

For members of a DC public service pension scheme under the Disclosure Regulations 2013

194. Managers of a scheme must provide a benefit statement to a member of a DC public service pension scheme, who is not an 'excluded person', within 12 months of the end of the scheme year[89]. An 'excluded person' is a member or beneficiary whose present postal address and email address is not known to the scheme because the correspondence has been returned (in the case of postal correspondence) or has not been delivered (in the case of electronic correspondence)[90].

195. The information which must be provided includes the amount of contributions (before any deductions are made) credited to the member during the immediately preceding scheme year[91], the value of the member's accrued rights under the scheme at a date specified by the managers of the scheme[92] and a statutory money purchase illustration[93]. The full detail of the information that must be provided is set out in the Disclosure Regulations 2013.

Other information about scheme administration

196. Under the Disclosure Regulations 2013, managers of a scheme must provide other information to members and others in certain circumstances (for example, on request). The Regulations set out the information which must be given, the timescales for providing such information and the methods that may be used. Not all information must be provided in respect of all public service pension schemes (there are some exemptions for specified public service schemes or according to the type of benefit offered), but information which scheme managers may need to provide includes:

- basic scheme information
- information about the scheme that has materially altered
- information about the constitution of the scheme
- annual report (this requirement will generally not apply to unfunded DB public service pension schemes and DB schemes for local government workers[94])

87
Regulation 16 and Schedule 5 of the Disclosure Regulations 2013.

88
Regulation 16(3), ibid.

89
Regulation 17, ibid.

90
Regulation 2, ibid.

91
'Scheme year' is defined in Regulation 2, ibid.

92
Regulation 17 and Schedule 6, ibid.

93
Paragraph 6 and Schedule 6, ibid. There are certain exceptions to the requirements to provide this information.

94
Regulation 4, ibid.

- information about funding principles, actuarial valuations and payment schedules (these requirements will generally not apply to unfunded DB public service pension schemes and DB schemes for local government workers[95])
- information about transfer credits
- information about lifestyling (this requirement will not apply in respect of DB benefits in public service pension schemes[96])
- information about accessing benefits, and
- information about benefits in payment.

197. The detail of the information that must be provided to scheme members and others and any exemptions are set out in the Disclosure Regulations 2013. Managers must provide the required information, along with confirmation that members may request further information and the postal and email addresses to which a person should send those requests and enquiries[97].

Who is entitled to information

198. Managers of a scheme must ensure that scheme members and others are given information in accordance with the Disclosure Regulations 2013, unless they are an 'excluded person' (as defined above).

199. The Disclosure Regulations 2013 make provision for scheme members and others to receive information that is relevant to their pension rights and entitlements under the scheme. The categories of people who are entitled to receive information vary according to the different types of information, and there are exemptions where information has already been provided in a specified period. The detail of who is entitled to any particular type of information is set out in the Disclosure Regulations 2013 but may include any of the following ('a relevant person'):

- active members
- deferred members
- pensioner members
- prospective members
- spouses or civil partners of members or prospective members
- other beneficiaries, and
- recognised trade unions.

95
Regulation 4 of the Disclosure Regulations 2013.

96
Regulation 18(1), ibid.

97
Regulation 4(7), ibid.

When basic scheme information must be provided

200. Managers must disclose certain basic information about the scheme and the benefits it provides to a prospective member (if practicable to do so) or a new member[98]. Where the manager has received jobholder information[99] for the member or prospective member they must provide the information within a month of the jobholder information being received[100]. Where they have not received jobholder information, they must provide the information within two months of the date the person became an active member of the scheme[101].

201. Managers must also provide the information on request to a relevant person within two months of the request being made, except where the same information was provided to the same person or trade union in the 12 months before the request[102].

What information must be disclosed on request

202. In addition to the basic scheme information, pension scheme members and other relevant persons are entitled to request certain scheme information or scheme documents including:

- information about the constitution of the pension scheme, and
- information about transfer credits[103].

How benefit statements and other information must be provided

203. Generally, schemes may choose how they provide information to scheme members, including by post, electronically (by email or by making it available on a website) or by any other means permitted by the law. For benefit statements issued under the 2013 Act, HM Treasury directions may specify how the information must be provided. Where schemes wish to provide information required under the Disclosure Regulations 2013 by electronic means there are important steps and safeguards that must first be met[104]. These include:

- scheme members and beneficiaries being provided with the option to opt out of receiving information electronically by giving written notice to the scheme
- managers being satisfied that the electronic communications have been designed:
  - so that the person will be able to access and either store or print the relevant information and
  - taking into account the requirements of disabled people

98 Regulation 6 of the Disclosure Regulations 2013.

99 Specified in regulation 3 of the Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010.

100 Regulation 6(5) of the Disclosure Regulations 2013.

101 Regulation 6(6), ibid.

102 Regulation 6(4) and (7), ibid.

103 Regulations 11, 14 and Parts 1 and 4 of Schedule 3, ibid.

104 Regulation 26, ibid.

- ensuring that members and beneficiaries who were members or beneficiaries of the public service pension scheme on 1 December 2010 (where the scheme had not provided information electronically prior to that date) has been sent a written notice (other than via email or website), informing them that:
  - it is proposed to provide information electronically in the future and
  - scheme members and beneficiaries may opt out of receiving information electronically by sending written notice.

204. Where schemes make information or a document available on a website for the first time, they must give notice (other than via a website) to the recipient[105]. They must ensure that the notice includes:

- a statement advising that the information is available on the website
- the website address
- details of where on the website the information or document can be read, and
- an explanation of how the information or document may be read on the website[106].

205. When any subsequent information is made available on a website, managers of a scheme must give a notice (other than via a website) to recipients informing them that the information is available on the website[107]. This notice will not be required where[108]:

- at least two documents have been given to the recipient by hand or sent to the recipient's last known postal address
- each of those letters asks the recipient to give their electronic (email) address to the scheme and informs the recipient of their right to request (in writing) that information or documents are not to be provided electronically
- a third letter has been given to the recipient by hand or sent to the recipient's last known postal address and includes a statement that further information will be available to read on the website and that no further notifications will be sent to the recipient and
- the managers of the scheme do not know the recipient's email address and have not received a written request that information or documents are not to be provided to the recipient electronically.

105
Regulation 27(1) and (5) of the Disclosure Regulations 2013.

106
Regulation 27(2), ibid.

107
Regulation 27(3) and (5), ibid.

108
Regulation 28, ibid.

206. In some cases, the Disclosure Regulations 2013 specify that information must be made available by one of the following methods[109]:

- available to view free of charge, at a place that is reasonable having regard to the request
- published on a website (in which case the procedure to be followed before making information available on a website does not apply, except that the person or trade union must be notified of certain details)
- given for a charge that does not exceed the expense incurred in preparing, posting and packing the information, or
- publicly available elsewhere.

Practical guidance

207. Schemes should design and deliver communications to scheme members in a way that ensures they are able to engage with their pension provision. Information should be clear and simple to understand as well as being accurate and easily accessible. It is important that members are able to understand their pension arrangements and make informed decisions where required.

208. Schemes should attempt to make contact with their scheme members and, where contact is not possible, schemes should carry out a tracing exercise to locate the member and ensure that their member data are up-to-date.

209. Where a person has made a request for information, schemes should acknowledge receipt if they are unable to provide the information at that stage. Schemes may encounter situations where the time period for providing information takes longer than expected. In these circumstances, schemes should notify the person and let them know when they are likely to receive the information. Scheme managers and managers (where different) must provide information in accordance with the time periods specified in the 2013 Act and Disclosure Regulations 2013.

210. To promote transparency, schemes should make information readily available at all times to ensure that prospective and existing members are able to access information when they require it.

Other legal requirements

211. Managers (or any other person specified in legislation) must comply with other legislation requiring information to be provided to members of public service pension schemes in certain circumstances. Not all requirements apply to all public service pension schemes and some may only arise in limited circumstances.

109
Regulation 29 of the Disclosure Regulations 2013.

Some of the requirements that schemes may need to be aware of are set out in or under the following legislation[110]:

- Occupational Pension Schemes (Contracting-out) Regulations 1996
- Occupational Pension Schemes (Transfer Values) Regulations 1996
- Occupational Pension Schemes (Winding up etc.) Regulations 2005
- Occupational Pension Schemes (Internal Dispute Resolution Procedures Consequential and Miscellaneous Amendments) Regulations 2008 (the requirements of these regulations are covered in the section of this code on 'Internal dispute resolution').

110
The legislation identified in this list is made under section 113 of the Pension Schemes Act 1993. There are other requirements that relate to providing information to members which arise under other legislation and which may be relevant to public service pension schemes (for example, under legislation relating to automatic enrolment and early leavers).

Resolving issues

212. This part covers:

- internal dispute resolution, and
- reporting breaches of the law.

Internal dispute resolution

Legal requirements

213. Scheme managers[111] must make and implement dispute resolution arrangements that comply with the requirements of the law and help resolve pensions disputes between the scheme manager and a person with an interest in the scheme. 'Pension disputes'[112] cover matters relating to the scheme between the managers and one or more people with an interest in the scheme. These exclude 'exempted disputes'.

214. There are certain 'exempted disputes' to which the internal dispute resolution procedure will not apply[113]. This includes disputes where proceedings have commenced in any court or tribunal, or where the Pensions Ombudsman has commenced an investigation into it. Certain other prescribed disputes, for instance medical-related disputes that may arise in relation to police and fire and rescue workers, are also 'exempted disputes'[114].

215. A person has an interest in the scheme if they:

- are a member or surviving non-dependant beneficiary of a deceased member of the scheme
- are a widow, widower, surviving civil partner or surviving dependant of a deceased member of the scheme
- are a prospective member of the scheme
- have ceased to be a member, beneficiary or prospective member or
- claim to be in one of the categories mentioned above and the dispute relates to whether they are such a person.

216. Dispute resolution arrangements may require people with an interest in the scheme to first refer matters in dispute to a 'specified person' in order for that person to consider and give their decision on those matters. The specified person's decision may then be confirmed or replaced by the decision taken by the scheme manager after reconsideration of the matters[115].

111
Legal requirements relating to the internal dispute resolution provisions are imposed on the 'managers' of a scheme, which the regulator generally takes to be the 'scheme manager' identified in scheme regulations in accordance with the 2013 Act.

112
Section 50(3) of the Pensions Act 1995.

113
Section 50(9), ibid.

114
Regulation 4 of the Occupational Pension Schemes (Internal Dispute Resolution Procedures Consequential and Miscellaneous Amendments) Regulations 2008.

115
Section 50(4A) of the Pensions Act 1995.

217. Scheme managers and specified persons (if used as part of a scheme's procedure) must take the decision required on the matters in dispute within a reasonable period of receiving the application. They must notify the applicant of the decision within a reasonable period of having taken it[116].

218. Internal dispute resolution procedures must state the manner in which an application for the resolution of a pension dispute is to be made, the particulars which must be included in such an application and the manner in which any decisions required in relation to such an application are to be reached and given[117]. The procedure must specify a reasonable period within which applications must be made by certain people[118].

219. Scheme managers must provide information about the scheme's dispute resolution procedure as well as information about The Pensions Advisory Service (TPAS) and the Pensions Ombudsman to certain people at certain stages[119].

Practical guidance

220. Scheme members expect their pension scheme to be managed effectively. Where a person with an interest in the scheme is not satisfied with any matter relating to the scheme (for example a decision which affects them), they have the right to ask for that matter to be reviewed.

221. Internal dispute resolution arrangements provide formal procedures and processes for pension scheme disputes to be investigated and decided upon quickly and effectively. They play a key role in the effective governance and administration of a scheme.

222. Schemes[120] can operate a two-stage procedure with a 'specified person' undertaking the first-stage decision. Alternatively, they may adopt a single-stage procedure if they consider that is more appropriate for their scheme.

223. With the exception of certain matters outlined below, the law does not prescribe the detail of the dispute resolution procedure. Schemes should decide on this and ensure it is fit for purpose.

116
Section 50(5) of the Pensions Act 1995.

117
Section 50B(4), ibid.

118
Section 50B(3)(a), ibid.

119
Regulation 6 of, and Part 1 of Schedule 2 to, the Disclosure Regulations 2013 and regulation 2 of the Occupational Pension Schemes (Internal Dispute Resolution Procedures) (Consequential and Miscellaneous Amendments) Regulations 2008.

120
See paragraph 25 for the definition of 'schemes'.

When applications should be submitted

224. Schemes may choose to specify time limits within which the following people must apply for a dispute to be resolved[121]:

- scheme members
- widows, widowers, surviving civil partners or surviving dependants of deceased scheme members
- surviving non-dependant beneficiaries of deceased scheme members, and
- prospective scheme members.

225. If schemes decide to specify time limits, they should publish and make those time limits readily available to ensure that those with an interest in the scheme are aware that they must submit an application within a prescribed time limit.

226. Scheme managers must ensure their scheme's procedure specifies a reasonable period within which applications by the following people must be made[122]:

- a person who has ceased to be within the categories in paragraph 224 above
- a person who claims that they were a person within the categories in paragraph 224 above and has ceased to be such a person, and the dispute relates to whether they are such a person.

227. A reasonable period would be six months beginning immediately after the date on which the person ceased to be, or claims they ceased to be, a person with an interest in the scheme. However, schemes have the flexibility to exercise their judgement and take an application outside a specified time period, if appropriate.

When decisions should be taken

228. Managers and specified persons (where applicable) must decide the matter in dispute within a reasonable period of receiving the application. A reasonable period is within four months of receiving the application. In the case of a two-stage dispute resolution procedure, the reasonable period applies to each stage separately. Where a dispute is referred to scheme managers for a second-stage decision, the reasonable period begins when the managers receive the referral. However, there may be cases where it will be possible to process an application sooner than the reasonable time given. Where this is the case, there should not be a delay in taking the decision.

121
Section 50B(3)(b) of the Pensions Act 1995.

122
Section 50B(3)(a) of the Pensions Act 1995.

229. There may be exceptional circumstances of a particular dispute which may prevent the process being completed within the reasonable time period stated above. For instance, where the dispute involves unusually complex and labour-intensive calculations or research, or delays occur that are outside the control of the scheme manager (or specified person), or because they need to obtain independent evidence.

230. The regulator recognises that the circumstances of each dispute are different and decision times may vary. Schemes should be satisfied that the time taken to reach a decision is appropriate to the situation and be able to demonstrate this, if necessary.

When applicants should be informed of a decision

231. Applicants must be notified of the decision made by a scheme manager and specified person (where applicable) within a reasonable time period after the decision has been made[123]. Schemes should usually notify applicants of the decision no later than 15 working days after the decision has been made. However, there may be cases where it is possible to notify an applicant sooner than the reasonable time given. Where this is the case, there should not be a delay in notifying them of the decision.

232. Schemes should provide the applicant with regular updates on the progress of their investigation. They should notify the applicant where the time period for a decision is expected to be shorter or longer than the reasonable time period and let them know when they are likely to receive an outcome.

Implementing the procedure and processes

233. Scheme regulations or other documents recording policy about the administration of the scheme should specify internal dispute resolution arrangements. Schemes should focus on educating and raising awareness of their internal dispute resolution arrangements and ensuring that they are implemented.

234. Schemes should ensure that the effectiveness of the arrangements is assessed regularly and be satisfied that those following the process are complying with the requirements set, which includes effective decision making. This is particularly important where the arrangements require employers participating in the pension scheme to carry out duties as part of the process, for example where schemes have implemented the two-stage procedure and employers are acting as the specified person for the first stage.

235. Schemes should confirm and communicate their arrangements to members, for example, in the joining booklet. Schemes should make their arrangements accessible to potential applicants, for example by publishing them on a scheme website.

123
Section 50(5) of the Pensions Act 1995.

236. Scheme managers must provide the following information about the procedure and processes the scheme has in place for the internal resolution of disputes to certain people in certain circumstances[124]:

- prospective members, if it is practicable to do so
- any scheme members who have not already been given the information
- certain relevant people who request the information and who have not been given that information in the previous 12 months, and
- members or prospective members when schemes receive jobholder information, or when a jobholder becomes an active member, in connection with automatic enrolment.

237. Scheme managers must also provide the postal or email address and job title of the person to contact in order to make use of the internal dispute arrangements.

238. In addition, scheme managers must provide information about TPAS and the Pensions Ombudsman at certain stages[125]. Upon receiving an application for the resolution of a pension dispute, scheme managers (or the specified person) must make the applicant aware as soon as reasonably practicable that TPAS is available to assist members and beneficiaries of the scheme and provide contact details for TPAS. When notifying the applicant of the decision, scheme managers must also inform the applicant that the Pensions Ombudsman is available to investigate and determine complaints or disputes of fact or law relating to a public service pension scheme and provide the Pension Ombudsman's contact details.

239. Schemes can decide what information they need from applicants to reach a decision on a disputed matter and how applications should be submitted. Schemes should ensure they make the following information available to applicants:

- the procedure and processes to apply for a dispute to be resolved
- the information that an applicant must include
- the process by which any decisions are reached, and
- an acknowledgement once an application has been received.

124
Regulation 6 of, and Part 1 of Schedule 2 to, the Disclosure Regulations 2013.

125
Regulation 2 of the Occupational Pension Schemes (Internal Dispute Resolution Procedures) (Consequential and Miscellaneous Amendments) Regulations 2008.

240. When reviewing an application, scheme managers and specified persons (where relevant) should ensure that they have all the appropriate information to make an informed decision. They should request further information if required. Scheme managers and specified persons should be satisfied that the times taken to reach a decision and notify the applicant are appropriate to the situation and that they have taken the necessary action to meet the reasonable time periods. Scheme managers should be able to demonstrate this to the regulator if required.

Reporting breaches of the law

Legal requirements

241. Certain people are required to report breaches of the law to the regulator where they have reasonable cause to believe that:

- a legal duty[126] which is relevant to the administration of the scheme has not been, or is not being, complied with
- the failure to comply is likely to be of material significance to the regulator in the exercise of any of its functions[127].

For further information about reporting late payments of employee or employer contributions, see the section of this code on 'Maintaining contributions'.

242. People who are subject to the reporting requirement ('reporters') for public service pension schemes are:

- scheme managers[128]
- members of pension boards
- any person who is otherwise involved in the administration of a public service pension scheme
- employers[129]: in the case of a multi-employer scheme, any participating employer who becomes aware of a breach should consider their statutory duty to report, regardless of whether the breach relates to, or affects, members who are its employees or those of other employers
- professional advisers[130] including auditors, actuaries, legal advisers and fund managers: not all public service pension schemes are subject to the same legal requirements to appoint professional advisers, but nonetheless the regulator expects that all schemes will have professional advisers, either resulting from other legal requirements or simply as a matter of practice
- any person who is otherwise involved in advising the managers of the scheme in relation to the scheme[131].

243. The report must be made in writing as soon as reasonably practicable[132]. See paragraph 263 for further information about how to report breaches.

126
The reference to a legal duty is to a duty imposed by, or by virtue of, an enactment or rule of law (s70(2)(a) of the Pensions Act 2004).

127
Section 70(2) of the Pensions Act 2004.

128
The legal requirement to report breaches of the law under section 70(1)(a) is imposed on the 'managers' of a scheme, which the regulator generally takes to be the 'scheme manager' identified in scheme regulations in accordance with the 2013 Act.

129
As defined in s318 of the Pensions Act 2004.

130
As defined in s47 of the Pensions Act 1995.

131
Section 70(1) of the Pensions Act 2004.

132
Section 70(2), ibid.

Practical guidance

244. Schemes[133] should be satisfied that those responsible for reporting breaches are made aware of the legal requirements and this guidance. Schemes should provide training for scheme managers and pension board members. All others under the statutory duty to report should ensure they have a sufficient level of knowledge and understanding to fulfil that duty. This means having sufficient familiarity with the legal requirements and procedures and processes for reporting.

Implementing adequate procedures

245. Identifying and assessing a breach of the law is important in reducing risk and providing an early warning of possible malpractice in public service pension schemes. Those people with a responsibility to report breaches, including scheme managers and pension board members, should establish and operate appropriate and effective procedures to ensure that they are able to meet their legal obligations. Procedures should enable people to raise concerns and facilitate the objective consideration of those matters. It is important that procedures allow reporters to decide within an appropriate timescale whether they must report a breach. Reporters should not rely on waiting for others to report.

246. Procedures should include the following features:

- a process for obtaining clarification of the law around the suspected breach where needed
- a process for clarifying the facts around the suspected breach where they are not known
- a process for consideration of the material significance of the breach by taking into account its cause, effect, the reaction to it, and its wider implications, including (where appropriate) dialogue with the scheme manager or pension board
- a clear process for referral to the appropriate level of seniority at which decisions can be made on whether to report to the regulator
- an established procedure for dealing with difficult cases
- a timeframe for the procedure to take place that is appropriate to the breach and allows the report to be made as soon as reasonably practicable
- a system to record breaches even if they are not reported to the regulator (the record of past breaches may be relevant in deciding whether to report future breaches, for example it may reveal a systemic issue), and
- a process for identifying promptly any breaches that are so serious they must always be reported.

133
See paragraph 25 for the definition of 'schemes'.

Judging whether a breach must be reported

247. Breaches can occur in relation to a wide variety of the tasks normally associated with the administrative function of a scheme such as keeping records, internal controls, calculating benefits and, for funded pension schemes, making investment or investment-related decisions.

Judging whether there is 'reasonable cause'

248. Having 'reasonable cause' to believe that a breach has occurred means more than merely having a suspicion that cannot be substantiated.

249. Reporters should ensure that where a breach is suspected, they carry out checks to establish whether or not a breach has in fact occurred. For example, a member of a funded pension scheme may allege that there has been a misappropriation of scheme assets where they have seen in the annual accounts that the scheme's assets have fallen. However, the real reason for the apparent loss in value of scheme assets may be due to the behaviour of the stock market over the period. This would mean that there is not reasonable cause to believe that a breach has occurred.

250. Where the reporter does not know the facts or events around the suspected breach, it will usually be appropriate to check with the pension board or scheme manager or with others who are in a position to confirm what has happened. It would not be appropriate to check in cases of theft, suspected fraud or other serious offences where discussions might alert those implicated or impede the actions of the police or a regulatory authority. Under these circumstances the reporter should alert the regulator without delay.

251. If the reporter is unclear about the relevant legal provision, they should clarify their understanding of the law to the extent necessary to form a view.

252. In establishing whether there is reasonable cause to believe that a breach has occurred, it is not necessary for a reporter to gather all the evidence which the regulator may require before taking legal action. A delay in reporting may exacerbate or increase the risk of the breach.

Judging what is of 'material significance' to the regulator

253. In deciding whether a breach is likely to be of 'material significance' to the regulator. It would be advisable for those with a statutory duty to report to consider the:

- cause of the breach
- effect of the breach
- reaction to the breach, and
- wider implications of the breach.

254. When deciding whether to report, those responsible should consider these points together. Reporters should take into account expert or professional advice, where appropriate, when deciding whether the breach is likely to be of material significance to the regulator.

Cause of the breach

255. The breach is likely to be of material significance to the regulator where it was caused by:

- dishonesty
- poor governance or administration
- slow or inappropriate decision making practices
- incomplete or inaccurate advice, or
- acting (or failing to act) in deliberate contravention of the law.

256. When deciding whether a breach is of material significance, those responsible should consider other reported and unreported breaches of which they are aware. However, historical information should be considered with care, particularly if changes have been made to address previously identified problems.

257. A breach will not normally be materially significant if it has arisen from an isolated incident, for example resulting from teething problems with a new system or procedure, or from an unusual or unpredictable combination of circumstances. But in such a situation, it is also important to consider other aspects of the breach such as the effect it has had and to be aware that persistent isolated breaches could be indicative of wider scheme issues.

Effect of the breach

258. Reporters need to consider the effects of any breach, but with the regulator's role in relation to public service pension schemes and its statutory objectives in mind, the following matters in particular should be considered likely to be of material significance to the regulator:

- pension board members not having the appropriate degree of knowledge and understanding, which may result in pension boards not fulfilling their roles, the scheme not being properly governed and administered and/or scheme managers breaching other legal requirements
- pension board members having a conflict of interest, which may result in them being prejudiced in the way that they carry out their role, ineffective governance and administration of the scheme and/or scheme managers breaching legal requirements
- adequate internal controls not being established and operated, which may lead to schemes not being run in accordance with their scheme regulations and other legal requirements, risks not being properly identified and managed and/or the right money not being paid to or by the scheme at the right time
- accurate information about benefits and scheme administration not being provided to scheme members and others, which may result in members not being able to effectively plan or make decisions about their retirement
- appropriate records not being maintained, which may result in member benefits being calculated incorrectly and/or not being paid to the right person at the right time
- pension board members misappropriating any assets of the scheme or being likely to do so, which may result in scheme assets not being safeguarded, and
- any other breach which may result in the scheme being poorly governed, managed or administered.

259. Reporters need to take care to consider the effects of the breach, including any other breaches occurring as a result of the initial breach and the effects of those resulting breaches.

Reaction to the breach

260. Where prompt and effective action is taken to investigate and correct the breach and its causes and, where appropriate, notify any affected members, the regulator will not normally consider this to be materially significant.

261. A breach is likely to be of concern and material significance to the regulator where a breach has been identified and those involved:

- do not take prompt and effective action to remedy the breach and identify and tackle its cause in order to minimise risk of recurrence
- are not pursuing corrective action to a proper conclusion, or
- fail to notify affected scheme members where it would have been appropriate to do so.

Wider implications of the breach

262. Reporters should consider the wider implications of a breach when they assess which breaches are likely to be materially significant to the regulator. For example, a breach is likely to be of material significance where the fact that the breach has occurred makes it appear more likely that other breaches will emerge in the future. This may be due to the scheme manager or pension board members having a lack of appropriate knowledge and understanding to fulfil their responsibilities or where other pension schemes may be affected. For instance, public service pension schemes administered by the same organisation may be detrimentally affected where a system failure has caused the breach to occur.

Submitting a report to the regulator

263. Reports must be submitted in writing and can be sent by post or electronically, including by email or by fax. Wherever possible reporters should use the standard format available via the Exchange online service on the regulator's website.

264. The report should be dated and include as a minimum:

- full name of the scheme
- description of the breach or breaches
- any relevant dates
- name of the employer or scheme manager (where known)
- name, position and contact details of the reporter, and
- role of the reporter in relation to the scheme.

265. Additional information that would help the regulator includes:

- the reason the breach is thought to be of material significance to the regulator
- the address of the scheme
- the contact details of the scheme manager (if different to the scheme address)
- the pension scheme's registry number (if available), and
- whether the concern has been reported before.

266. Reporters should mark urgent reports as such and draw attention to matters they consider particularly serious. They can precede a written report with a telephone call, if appropriate.

267. Reporters should ensure they receive an acknowledgement for any report they send to the regulator. Only when they receive an acknowledgement can the reporter be confident that the regulator has received their report.

268. The regulator will acknowledge all reports within five working days of receipt, however it will not generally keep a reporter informed of the steps taken in response to a report of a breach as there are restrictions on the information it can disclose.

269. The reporter should provide further information or reports of further breaches if this may help the regulator to exercise its functions. The regulator may make contact to request further information.

270. Breaches should be reported as soon as reasonably practicable, which will depend on the circumstances. In particular, the time taken should reflect the seriousness of the suspected breach.

271. In cases of immediate risk to the scheme, for instance, where there is any indication of dishonesty, the regulator does not expect reporters to seek an explanation or to assess the effectiveness of proposed remedies. They should only make such immediate checks as are necessary. The more serious the potential breach and its consequences, the more urgently reporters should make these necessary checks. In cases of potential dishonesty the reporter should avoid, where possible, checks which might alert those implicated. In serious cases, reporters should use the quickest means possible to alert the regulator to the breach.

Whistleblowing protection and confidentiality

272. The Pensions Act 2004 makes clear that the statutory duty to report overrides any other duties a reporter may have such as confidentiality and that any such duty is not breached by making a report. The regulator understands the potential impact of a report on relationships, for example, between an employee and their employer.

273. The statutory duty to report does not, however, override 'legal privilege'[134]. This means that oral and written communications between a professional legal adviser and their client, or a person representing that client, while obtaining legal advice, do not have to be disclosed. Where appropriate a legal adviser will be able to provide further information on this.

134
Section 311 of the Pensions Act 2004.

274. The regulator will do its best to protect a reporter's identity (if desired) and will not disclose the information except where lawfully required to do so. It will take all reasonable steps to maintain confidentiality, but it cannot give any categorical assurances as the circumstances may mean that disclosure of the reporter's identity becomes unavoidable in law. This includes circumstances where the regulator is ordered by a court to disclose it.

275. The Employment Rights Act 1996 (ERA) provides protection for employees making a whistleblowing disclosure to the regulator. Consequently, where individuals employed by firms or another organisation having a statutory duty to report disagree with a decision not to report to the regulator, they may have protection under the ERA if they make an individual report in good faith. The regulator expects such individual reports to be rare and confined to the most serious cases.

Appendix

Corresponding Northern Ireland legislation

GB legislation	NI legislation
Pension Schemes Act 1993 (c. 48) - Chapter 1 of Part 4 - section 113	Pension Schemes (Northern Ireland) Act 1993 (c. 49) - Chapter 1 of Part 4 - section 109
Pensions Act 1995 (c. 26) - section 47 - section 49 - section 50 - section 50B - section 87	Pensions (Northern Ireland) Order 1995 (SI 1995/3213 (NI 22)) - Article 47 - Article 49 - Article 50 - Article 50B - Article 85
Employment Rights Act 1996 (c. 18)	Employment Rights (Northern Ireland) Order 1996 (SI 1996/1919 (NI 16))
Data Protection Act 1998 (c. 29)	Data Protection Act 1998 (c. 29)
Freedom of Information Act 2000 (c.36)	Freedom of Information Act 2000 (c.36)
Pensions Act 2004 (c. 35) - section 5 - section 13 - section 70 - section 70A - section 90A - Part 3 - section 227 - section 248 - section 248A - section 249A - section 249B - section 311 - section 318	Pensions (Northern Ireland) Order 2005 (SI 2005/255 (NI 1)) - Article 4 - Article 9 - Article 65 - Article 65A - Article 85A - Part 4 - Article 206 - Article 225 - Article 225A - Article 226A - Article 226B - Article 283 - Article 2
Pensions Act 2008 (c. 30)	Pensions (No. 2) Act (Northern Ireland) 2008 (c. 13)

GB legislation	NI legislation
Public Service Pensions Act 2013 (c. 25) - section 1 - section 2 - section 3 - section 4 - section 5 - section 6 - section 7 - section 14 - section 15 - section 16 - section 28 - section 30 - Schedule 2 - Schedule 3	Public Service Pensions Act (Northern Ireland) 2014 (c. 2) - section 1 - section 2 - section 3 - section 4 - section 5 - section 6 - section 7 - section 14 - section 15 - section 16 - section 28 - section 31 - Schedule 2 - Schedule 3
Occupational Pension Schemes (Managers) Regulations 1986 (SI 1986/1718)	Occupational Pension Schemes (Managers) Regulations (Northern Ireland) 1986 (SR 1986 No. 320)
Occupational Pension Schemes (Contracting-out) Regulations 1996 (SI 1996/1172)	Occupational Pension Schemes (Contracting-out) Regulations (Northern Ireland) 1996 (SR 1996 No. 493)
Occupational Pension Schemes (Scheme Administration) Regulations 1996 (SI 1996/1715)	Occupational Pension Schemes (Scheme Administration) Regulations (Northern Ireland) 1997 (SR 1997 No. 94)
Occupational Pension Schemes (Transfer Values) Regulations 1996 (SI 1996/1847)	Occupational Pension Schemes (Transfer Values) Regulations (Northern Ireland) 1996 (SR 1996 No. 619)
Occupational Pension Schemes (Winding up etc.) Regulations 2005 (SI 2005/706)	Occupational Pension Schemes (Winding up, etc.) Regulations (Northern Ireland) 2005 (SR 2005 No. 171)
Occupational Pension Schemes (Scheme Funding) Regulations 2005 (SI 2005/3377)	Occupational Pension Schemes (Scheme Funding) Regulations (Northern Ireland) 2005 (SR 2005 No. 568)
Registered Pension Schemes (Provision of Information) Regulations 2006 (SI 2006/567)	Registered Pension Schemes (Provision of Information) Regulations 2006 (SI 2006/567)

GB legislation	NI legislation
Occupational Pension Schemes (Internal Dispute Resolution Procedures Consequential and Miscellaneous Amendments) Regulations 2008 (SI 2008/649)	Occupational Pension Schemes (Internal Dispute Resolution Procedures Consequential and Miscellaneous Amendments) Regulations (Northern Ireland) 2008 (SR 2008 No. 116)
Employers' Duties (Registration and Compliance) Regulations 2010 (SI 2010/5)	Employers' Duties (Registration and Compliance) Regulations (Northern Ireland) 2010 (SR 2010 No. 186)
Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010 (SI 2010/772)	Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations (Northern Ireland) 2010 (SR 2010 No. 122)
Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 (SI 2013/2734)	Occupational and Personal Pension Schemes (Disclosure of Information) Regulations (Northern Ireland) 2014 (SR 2014 No. 79)
Public Service Pensions (Record Keeping and Miscellaneous Amendments) Regulations 2014	Public Service Pensions (Record Keeping and Miscellaneous Amendments) Regulations (Northern Ireland) 2014

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Non-Executive Report of the: **Pensions Committee** 25 November 2015	TOWER HAMLETS
Report of: Zena Cooke - Corporate Director of Resources	**Classification:** Unrestricted
Quarterly Report - Key Pension Administration Performance Indicators: July 2015 to September 2015	

Originating Officer(s)	Anant Dodia – Pensions Manager
Wards affected	All wards

Summary
This report provides Members with the quarterly monitoring information on the performance of the Pensions Administration Service.

This report covers the period, July 2015 – September 2015, Quarter 2, 2015/16.

Members will continue to receive updates on Key Performance Indicators on quarterly basis.

Recommendations:

Members are recommended to note the contents of this report.

1. REASONS FOR THE DECISIONS

1.1 The report is provided for information.

2. ALTERNATIVE OPTIONS

2.1 There are no alternative options.

3. DETAILS OF REPORT

3.1 A number of key performance indicators (KPIs) are reported on quarterly basis to assess performance in key areas of work. The standards and data for Quarter 2, 2015/16 is detailed in the table below.

Key Performance Indicators from 1 July to 30 September 2015					
PROCESS	TARGET DAYS	TOTAL	WITHIN TARGET	%WITHIN TARGET	AVERAGE DAYS
Transfer in Quote	10	19	17	89.47%	6.11
Transfer in Actual	10	8	5	62.50%	7.38
Transfer out Quote	15	31	29	93.55%	4.26
Transfer out Actual	12	13	11	84.62%	8.23
Refund of Contributions	10	48	48	100.00%	1.02
Preserved Benefit	15	144	133	92.36%	4.53
Pension Estimate	10	27	25	92.59%	5.93
Retirement Options sent to member	10	87	83	95.40%	5.09
Retirement Grant paid to member	10	76	71	93.42%	7.58
Death benefits - Write to next of kin	5	18	17	94.44%	4.83

3.2 There has been a reduction in performance in certain areas over the past 3 months. This is due to the intensive manual input in relation to the production of this year's annual benefits statement. Weekly task lists are now produced and monitored to improve the efficiency of the service.

3.3 **Annual benefits Statements** - On 6 August 2015, an email was sent by the Local Government Association (LGA) to administering authorities in England and Wales, requesting information on the number of 2015 annual benefit statements they expected to issue prior to this year's deadline of 31st August 2015, and the issues that have made this years' deadline particularly challenging.

The main issues noted in the responses concerned late / incorrect data submitted by employers, pensions and payroll software issues and internal resourcing issues caused by a general increase in the workload of the pensions function.

The LGA shared these concerns with the Pensions Regulator (tPR), with funds self-certifying to tPR that they had failed to meet the 31 August 2015 statutory deadline. The Regulator responded on 9 October 2015, acknowledging the difficulties faced by funds in meeting the statutory deadline due to the introduction of a new benefit design, but with an expectation that all statements to be issued by at least 30 November 2015.

The Pension Service has now issued all annual benefit statements.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 The comments of the Corporate Director of Resources have been incorporated into the report.

5. LEGAL COMMENTS

5.1 There are no specific legal implications in this report.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 There are no specific comments arising from this report.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The monitoring arrangement for the Pension Fund and the work of officers, advisors and consultants should ensure the Fund optimises the use of its resources in achieving the best returns for member of the Fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 Accounts provide an effective mechanism to safeguard the Councils assets and assess the risks associated with its activities.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no any Crime and disorder Reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report
- None

Appendices
- None

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report
- None

Officer contact details for documents:
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Non-Executive Report of the: **PENSIONS COMMITTEE** **25 November 2015**	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
LGPS – Current Developments and Update (Pooling, MiFID II, Fossil Fuel and Scheme Advisory Board Work)	

Originating Officer(s)	Bola Tobun, Investment and Treasury Manager
Wards affected	All

Summary

This report covers a range of relevant pension's related issues for the Committee to be aware including changes to pensions saving and future consultation on pooling of investments in the LGPS.

The attached report covers:

1. Pooling of investments in the LGPS
2. MiFID II Impact on LGPS and Local Authorities
3. Fossil Fuel Divestment Campaign
4. Scheme Advisory Board work on separation of Pension Funds

Recommendations:

Members of the Pensions Committee are asked to:

- Note the contents of the report.

1. REASONS FOR THE DECISIONS

1.1 No decision required

2. ALTERNATIVE OPTIONS

2.1 No alternative as this is for information and update.

3. DETAILS OF REPORT

3.1 Pooling of investments in the LGPS

3.1.1 The Chancellor announced that a consultation on the pooling of investments for the LGPS would take place in his July budget update:
"*Local Government Pension Scheme pooled investments – The government will work with Local Government Pension Scheme administering authorities to ensure that they pool investments to significantly reduce costs, while maintaining overall investment performance. The government will invite local authorities to come forward with their own proposals to meet common criteria for delivering savings. A consultation to be published later this year will set out those detailed criteria as well as backstop legislation which will ensure that those administering authorities that do not come forward with sufficiently ambitious proposals are required to pool investments*."

3.1.2 The Chancellor followed this up with a speech at the Conservative Party Conference "We are going to find new ways to fund British infrastructure that drives our productivity…. At the moment we have 89 local government pension funds with 89 sets of fees and costs. It's expensive, and they invest little or nothing in our infrastructure. So I can tell you today we are going to work with councils to create half a dozen British wealth funds spread across the country."

- He said this plan would save "hundreds of millions in cost, and crucially they will invest billions in the infrastructure of their regions."
- Further information published on the U.K. government website said that small local pension funds "lack the expertise to invest in infrastructure." Of the £180 billion of assets in these plans, only 0.5% is invested in infrastructure projects. Countries with larger pooled public pension funds invest up to 8% in infrastructure, and 17% in housing and infrastructure, according to the website.

3.1.3 Whilst officials from DCLG have stressed that there is no specific cost saving target, the figure of £660m continues to be referenced by ministers. Also officials are keen to point out that government does understand the fiduciary responsibilities of the LGPS in ensuring that investments are made for the right investment return and risk reasons rather than just to fund UK infrastructure and that there is not expected to be any compulsory for the funds to invest in infrastructure.

3.1.4 The consultation on pooling is expected to be issued in November, but the government has made it clear that it is looking at the LGPS coming forward with proposals for pooling of investments with pool sizes of between £25-30bn and for 5-6 pools.

3.1.5 The consultation is expected to cover:

- Legislative changes circulated in draft to give the Secretary of State increased powers;
- Proposed changes in the investment regulations;
- Acceptable criteria for pooling;
- Back stop measures for recalcitrant schemes.

3.1.6 At the time of writing, nothing had been formally announced on timeframes, although the expected timeline is set out below:

Government to commission and receive independent advice	Oct 2015
Consultation (and the backstop enforcement regulation)	Early Nov 2015
Consultation response from all stakeholders (expectation is for 12-week response period)	Early Feb 2016
Draft Regulations	Published March 2016 Effective date April 2016
Creation of asset pools (phased in over three years)	April 2019
Transition of assets for those funds not meeting the requirements	Unknown

3.1.7 There are no plans to formally consult on the criteria for pooling, although the government has made it clear in discussions on the pooling objectives that the four key criteria are:

- Scale (£25-30bn pool target);
- Cost Savings;
- Governance;
- Infrastructure

3.1.8 Whilst the government has expressed a preference for regional pooling, it has emphasised that it is willing to consider alternative proposals. It has made it clear that it is looking for local government to come forward with suitable proposals for consideration. Government has publicly acknowledged the advance already made in this area made by some Funds, and indicated that it is its intention is to build on that progress. Following the budget statement, the Lancashire/LPFA, the London CIV and the LGPS National Frameworks have all stated that Government has individually reaffirmed to them that their initiatives are consistent with the objectives for fee savings through scale economies. Indeed the London CIV is referenced by government as a model for others to consider although it has indicated that it is perhaps concerned about the voluntary nature of the arrangements with London Funds retaining options around which assets to pool in the CIV. It is clear that the government sees that the Administering Authority should retain the asset allocation decision for the individual funds but that they expect the choice of investment managers to be made by the investment pool itself.

3.1.9 As might be expected, following the government announcement and follow up discussions with government departments, the majority of LGPS Funds are now considering options for pooling and collaboration with others. To a certain extent with the London CIV already in progress, most London funds have stood aside with discussions with funds outside of London, seeing the CIV as their pooled vehicle to take their funds forwards into pooling.

3.1.10 One major project being assisted by Hymans Robertson is Project 'POOL' a collaboration of metropolitan and county authorities which is looking at a range of options to come forward with proposals for government during the consultation period. This includes consideration of regional pools along with pools run along asset class lines and also an in-house investment option. Other projects include one for Wales which would amount to around £10bn of assets, but is expected to be acceptable despite its relatively small size. The South-West is also looking at options for a pool in the region along the lines of previous framework agreements.

3.1.11 Three pension funds have also reported to be in talks to launch an investment partnership comprising East Riding, Surrey and Cumbria. These are just an indication of some of the discussions underway between the 89 funds in England and Wales. Whilst it is not expected to be available for the Board meeting on the 20th November, should the consultation be issued by the time of the meeting a further update will be provided to the Board.

3.2 MiFID II Impact on LGPS and Local Authorities

3.2.1 The first Markets in Financial Instruments Directive was adopted in April 2004 and came into force in November 2007. Its aim was to improve the competitiveness of EU financial markets by creating a single market for investment services and activities, and ensuring a high degree of harmonised protection for investors in financial instruments, such as shares, bonds, derivatives and various structured products. Under the current regulations LGPS funds are classified as professional investors enabling them to undertake transactions in a wide range of investments including complex ones such as hedge funds, private equity and property.

3.2.2 MiFID II is a wide-ranging EU regulation designed to improve investor protection and make financial markets safer and more transparent. It replaces MiFID and comes into effect on 3 January 2017 for all investment firms. It imposes more stringent transaction reporting and fee and charges disclosure rules on investment managers, and enforces better product governance to ensure that products are only sold to suitable investors. Retail investors can buy investments traded on public markets. But restrictions apply to complex and sophisticated investments, including those covered under the Alternative Investment Fund Managers directive (AIFMD), which includes hedge funds, private equity, property, and commodities. Under MiFID II local authorities will be classified as retail investors and because of the relationship of the local authority as the Administering Authority of the Pension Fund, the follow through is that LGPS Funds will also be classified as retail investors. In the private sector, company pension funds are primarily separate legal entities with trustee status and will therefore be unaffected by these changes.

3.2.3 Under MiFID II, all financial services firms such as banks, brokers, advisers and fund managers will have to treat LGPS funds in the same way they do individuals and small businesses. That includes ensuring that investment products are suitable for the customer's needs, and that all the risks and features have been fully explained. Whilst recognising that this is appropriate for retail investors it also involves lots more documentation and administration for both the firm and the client, to prove to the regulator that all the steps have been taken, and as evidence in case of alleged mis-selling. Further under MiFID II, asset managers are not allowed to sell investments such as hedge funds, property and private equity to retail clients because of their complex nature.

3.2.4 LGPS Funds will be able to go through an election process to be upgraded to professional clients but it will take time and will be onerous as they will have to prove to each asset manager that they meet the strict qualitative and quantitative criteria. These include showing the requisite experience, expertise and knowledge so the funds are capable of making their own investment decisions. Although managers carry the regulatory risk, it is the funds that will have to collate the information to prove they are professional clients.

3.2.5 The qualitative criteria under MiFID II are that Funds will have to demonstrate an 'adequate assessment of the expertise, experience and knowledge of the client that gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the client is capable of making his own investment decisions and understanding the risks involved' This assessment 'should be performed in relation to the person authorised to carry out transactions on its behalf.'

3.2.6 The quantitative criteria - (2 of the following 3 must be satisfied):

- the client has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;
- the size of the client's financial instrument portfolio, defined as including cash deposits and financial instruments, exceeds EUR 500,000;
- the client works or has worked in the financial sector for at least one year in a professional position, which requires knowledge of the transactions or services envisaged.

3.2.7 The Local Government Association (LGA), DCLG, the Investment Association along with LGPS Funds are currently lobbying the Financial Conduct Authority to try to find ways of lessening the impact on local authorities and in particular LGPS Funds of the new European Directive. In addition it is hoped that transition arrangements can be put in place to ensure that Funds aren't forced into a fire-sale of current holdings once the directive comes into force in January 2017. A copy of the LGA paper issued to raise awareness of the issue to local authorities is attached as an appendix to this report for information. It is anticipated that the FCA will issue a consultation on the introduction of MiFID II and its impact on local authorities in early 2016. The FCA also presented to the London CIV Sectoral Joint Committee, which the

Vice Chair of Pensions Committee attends outlining the issues for the Committee. A copy of the presentation given to the CIV is attached for information and sets out clearly the timeline of the introduction of the Directive and the issues arising.

3.2.8 With the move to pooling of local authority investments, the introduction of MiFID II could impact on how some of these vehicles are set up and the status that they would attract. The London CIV which the London Borough of Tower Hamlets Pension Fund has supported will meet the criteria of a professional investor given its FCA status as an authorised contractual scheme. However, whilst the London CIV will be classified as a Professional Investor it is unclear at this stage whether the CIV will have to undertake the same level of due diligence with its LGPS clients as a fund manager would do. In addition it is unclear whether some of the structure which could be put forward under the pooling consultation by LGPS funds would fall into the classification of professional investors.

3.2.9 At this stage the contents of this report are for information only, but to make the Committee aware of the potential ramifications of the new EU directive and to note that the Fund may face additional scrutiny and resource requirements if it is to be able to meet the professional classification. It should also be noted that this could also impact on the Council's treasury function.

3.3 Fossil Fuel Divestment Campaign

3.3.1 Over the past six months the debate on responsible investment has been in large part due to the growing movement regarding climate change and the associated fossil fuel divestment campaign.

3.3.2 Responsible investment is about managing risks and identifying opportunities. This can be achieved via the following vehicles:

- Sustainable investment – This involves considering the financial impact of environmental, social and governance (ESG) factors on investments.
- Stewardship and governance – This concerns investors acting as responsible and active owners, through considered voting of shares, and engaging with company management when required.

3.3.3 Trustees have a fiduciary duty to act in the best interests of their members, as well as acting prudently, responsibly and honestly. Within the context of these duties, which include controlling risks, they must aim to achieve the best realistic return over the long term. And for London Borough of Tower Hamlets Pension Fund this means:

- to ensure the long-term solvency of the Fund
- to ensure that sufficient funds are available to meet all benefits as they fall due for payment
- not to restrain unnecessarily the investment strategy of the Fund so that the Council can seek to maximise investment returns (and hence minimise the cost of the benefits) for an appropriate level of risk.

3.3.4 The London Borough of Tower Hamlets Pension Fund (the Fund) is a member of the Local Authority Pension Fund Forum (LAPFF).

3.3.5 LAPFF does not support divestment from fossil fuel companies but considers active engagement with companies producing fossil fuels as a productive approach to effecting change. The approach of direct and collaborative engagement contrasts with blanket divestment. Once an asset owner divests, their ability to influence both the short and longterm direction of individual companies and the national and international energy sector is severely curtailed.

3.3.6 LAPFF's engagement strategy is to push for an orderly carbon transition by requiring companies to identify and tackle carbon risks in their business models. Therefore we can say the Fund was one of the prime movers/supporters of the strategic resilience shareholder resolutions put to BP and Shell's 2015 AGMs. These resolutions were unique in that they were supported by the boards and galvanised investor support and built on a history of previous engagement with resources companies on carbon asset risk. The Fund also votes on resolutions at global AGMs seeking transparency and disclosure of climate risks and setting emission reduction targets. In this manner our view is directly communicated to individual boards.

3.3.7 It should be noted that the Fund does have an increasing level of investment in renewable and low carbon energy production and will continue to make such investments where the risk/return profile fits the pension fund's investment strategy.

3.3.8 The LAPFF has long been concerned about climate and carbon-related risks to the underlying investment portfolios of member funds and has been engaging with companies and on public policy since 2002 to address the many risks related to climate change.

3.3.9 The LAPFF's engagement strategy is to ask companies to identify and tackle carbon risks in their business models. In doing so, the Forum supports an orderly transition requiring companies to identify and tackle carbon risks in their business models.

3.3.10 For coal, oil and gas companies, particular attention is given to carbon asset risk, by promoting a low carbon transition. For oil and gas companies, the focus should be on value at risk, particularly from high cost projects and support can be given to returning capital to investors where appropriate.

3.3.11 An example of engagement is the coordination undertaken with member funds to co-file and support shareholder resolutions to both the BP and Shell 2015 AGMs on strategic resilience for 2035 and beyond. The resolutions ask the companies to report on their operational emissions management; asset portfolio resilience to the International Energy Agency (IEA)'s scenarios; low-carbon energy research and development and investment strategies; relevant strategic key performance indicators and executive incentives; and public policy positions relating to climate change.

3.3.12 LAPFF also works in cooperation with other investors and organisations to maximise the voice of asset owners including through its membership of the

Aiming for An Investor Coalition, through collaborative engagement with the Investor Network on Climate Risk and as a signatory to the Principles for Responsible Investment.

3.3.13 The Principles for Responsible Investment were developed by an international group of institutional investors reflecting the increasing relevance of environmental, social and corporate governance issues to investment practices. The process was convened by the United Nations Secretary-General.

3.3.14 These principles are based on the belief that as institutional investors, they have a duty to act in the best long-term interests of their beneficiaries. In this fiduciary role, they believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). They also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with their fiduciary responsibilities, they commit to the following:

- Principle 1: To incorporate ESG issues into investment analysis and decision-making processes.
- Principle 2: To be active owners and incorporate ESG issues into our ownership policies and practices.
- Principle 3: To seek appropriate disclosure on ESG issues by the entities in which they invest.
- Principle 4: To promote acceptance and implementation of the Principles within the investment industry.
- Principle 5: We will work together to enhance our effectiveness in implementing the Principles
- Principle 6: To report on activities and progress towards implementing the Principles.

3.3.15 The Forum has also supported resolutions encouraging Chevron and Exxon to set carbon reduction targets and at Chevron to reduce capital expenditure on high cost, unconventional projects and increase the amount authorised for distribution to shareholders in the form of dividends as a climate risk hedging mechanism.

3.3.16 Encouraging appropriate regulatory frameworks is also crucial. A recent example is the LAPFF's participation in correspondence from global asset owners and managers to the G7 leaders urging stronger action by major industrial nations on emissions, and climate action. As set out in the Forum's Statement on Climate Change, LAPFF members are interested in investment opportunities afforded by a low-carbon future which increase asset diversification and provide long-term returns. LAPFF will continue to engage with companies on aligning their business models with a 2°C scenario, to push for an orderly carbon transition and to file and support relevant shareholder resolutions to companies.

3.4 Scheme Advisory Board – Separation of Pension Funds

3.4.1 The National LGPS Scheme Advisory Board was formally set up on 1st April 2015 having operated in shadow form for over a year. The purpose of the Board is to encourage best practice, increase transparency and coordinate technical and standards issues. It will consider items passed to it from the Department of Communities and Local Government ("DCLG"), the Board's sub-committees and other stakeholders as well as items formulated within the Board. Recommendations may be passed to the DCLG or other bodies. It is also likely that it will have a liaison role with the Pensions Regulator. Guidance and standards may be formulated for local scheme managers and pension boards.

3.4.2 In June this year, the Board sought bids from advisors to look at options for separation of host authority and pension fund with a report to be delivered to the Board September 2015 setting out positives and negatives and cost implications from a range of options. A link to the notice for the invitation to bid can be found here:

http://www.lgpsboard.org/images/PDF/BoardJune2015/OfS_Instructions_for_bids.pdf

3.4.3 The options for reform that the Board were asking to be considered were:

1. **Option 1 -** Stronger role for Section 151 Officer within a distinct entity of the host authority
    - Separation of financial statements and audit arrangements
    - Pension fund-specific annual governance statement
    - Specific delegations or require a senior officer to lead the function
    - Group the responsibility for all LGPS related activities within one function.
2. **Option 2** – Joint Committee of two or more administering authorities
    - Delegation of full scheme manager function and all decision making to a section 102(5) joint committee
    - Employment of staff and contractual issues dealt with through lead authority or wholly owned company
    - Ownership of assets unchanged
    - Consideration be given to enshrining the structure in legislation in the form of a combined authority
3. **Option 3 -** LGPS complete separation of the pension fund from the authority
    - DCLG or Treasury to create single purpose Pensions Bodies
    - Remove decision making from elected members

3.4.4 KPMG was appointed to undertake the work looking into the options for separation and due to report back to the Board September 2015. At this stage there is no indication of how they might approach this work or the likely outcome or recommendations to the Board, but clearly if any of these recommendations are put forward to DCLG and then consulted upon, they could again have far reaching implications for the LGPS and administering authorities.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 The comments of the Corporate Director of Resources are incorporated in the report.

5. LEGAL COMMENTS

There are no immediate legal implications arising from this report. However due consideration will need to be given to the issues that will arise from:

the proposed pooling of pension fund investments once the consultation is underway;

the introduction of the 2nd Markets in Financial Instruments Directive which comes into effect on the 3rd January 2017;

the report being prepared by KPMG into the options for separation of host authority and pension fund which the Pensions Scheme Advisory Board has called for.

When deciding whether or not to proceed with a project, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty).

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.

6.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

7. BEST VALUE (BV) IMPLICATIONS

7.1 To have an efficient, cost reduction platform for investment management of the Fund by pooling and collaborating is considered to be a good decision which can result in greater cost savings to the fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 The rigorous robust management of LBTH Pension Fund results in better quicker and more effective decision making which can lead to better Fund performance and reduction in the contribution required from the Council towards the Fund. The monitoring arrangement for the Pension Fund and the work of the Pensions Committee should ensure that the Fund optimises the use of its resources in achieving the best returns for the Council and members of the Fund.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- NONE

Appendices

- LGA MiFIDIIPaperOct2015
- Presentation on Local Authorities LGPS under MiFIDII-LGA

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report

- NONE

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The Markets in Financial Instruments Directive (MiFID II) and its impact on LGPS investments

Why be concerned?

1. It is our understanding that under MiFID II local authorities will be defaulted to retail client status - currently they are professional clients. There will be the opportunity to elect for professional client status.

What does that mean for me as an LGPS administering authority?

2. As a retail client your authority could be faced with a much reduced pool of asset managers and consultants willing to provide services, many may not deal with retail clients at all.

3. Those managers who are willing to deal with you will offer a restricted range of products and due to the extra compliance checks and reporting required for retail clients those products could cost more. First estimates are that up to 50% of LGPS assets may be affected.

4. If when the directive comes into force (January 2017) you hold assets in products outside of the scope of those available to retail clients you may find that the manager will eject you from that product resulting in a 'fire sale' of assets. This could be mitigated if FCA were to provide some form of transition period or 'grandparenting' - allowing you to retain products purchased as a professional investor for a period of time.

How can I elect for professional status?

5. The process will be similar to that in MiFID I (see ANNEX 1) although there may be some changes to the criteria. Effectively you will have to demonstrate to <u>each</u> manager you use that you meet the qualitative and quantitative criteria as set out below

6. The qualitative criteria - an 'adequate assessment of the expertise, experience and knowledge of the client that gives reasonable assurance, in light of the nature of the

transactions or services envisaged, that the client is capable of making his own investment decisions and understanding the risks involved'

This assessment 'should be performed in relation to the person <u>authorised to carry out transactions on its behalf</u>.'

7. The quantitative criteria - (2 of the following 3 must be satisfied)

- the client has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;
- the size of the client's financial instrument portfolio, defined as including cash deposits and financial instruments, exceeds EUR 500,000;
- the client works or has worked in the financial sector for at least one year in a professional position, which requires knowledge of the transactions or services envisaged

How long will it take for an election to be completed?

8. Depending on how the actual criteria look when published in 2016 it could be a matter of weeks. However as each manager will have to assess each of its LGPS clients this cannot be able to be done all at once. Therefore it may be that some form of managed election process across the whole of the LGPS will be needed. For example if a significant number of authorities wait until very late 2016 to elect then don’t be surprised if the process is not completed by the January 2017 implementation date.

9. There is a duty on elected professional clients to keep firms informed about any change that could affect that status. Such changes could result in the process having be repeated and depending on the nature of the change the danger that the authority could be reverted back to retail client status.

What's the timeline?

February 2015: Feedback Statement on dealing commission regime and potential changes under MiFID II

March 2015: FCA Discussion Paper and ongoing dialogue in areas where we have policy choices to make
Summer 2015: EU legislation on MiFID II implementing measures is adopted and formal approval process begins
December 2015: Consultation on implementing MiFID II requirements
Early 2016: EU legislation on MiFID II implementing measures is finalised and published
June 2016: FCA Policy Statement (rules) on implementation of MiFID II
3 January 2017: MiFID II rules come into effect for all investment firms

What should I do?

10. Make your committee aware of the issue as soon as possible.

11. Discuss the implications with your asset managers, find out if they will they still deal with you as a retail client and what assets will be affected.

12. Prepare for an assessment against the qualitative and quantitative criteria - what evidence would you put forward to back up your election for professional status? In particular assess who will be judged against the qualitative criteria and if necessary be prepared to amend your delegations appropriately.

What are LGA doing?

13. We are in discussions with the FCA, DCLG and the Investment Association (IA) to find ways to lessen the impact on LGPS authorities, in particular we are:

- Investigating with DCLG and HMT the potential impact on pooling arrangements and in particular any impact on the potential for infrastructure investment via pools
- Discussing the election process under MiFID II with FCA to see if there are changes that could make the process smoother for local authorities in relation to their pensions functions
- Attempting to achieve a period of transition to avoid a forced sale of assets for those authorities who have not completed the election to professional status by January 2017

- Discussing with IA the possibility of standard documentation and process for election to professional status

LGA Pensions Team

16th October 2015

ANNEX 1

Extract from FCA New Conduct of Business Sourcebook Chapter 3 Client categorisation

ELECTIVE PROFESSIONAL CLIENTS

3.5.3

A firm may treat a client as an elective professional client if it complies with (1) and (3) and, where applicable, (2):

(1) the firm undertakes an adequate assessment of the expertise, experience and knowledge of the client that gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the client is capable of making his own investment decisions and understanding the risks involved (the "qualitative test");

(2) in relation to MiFID or equivalent third country business in the course of that assessment, at least two of the following criteria are satisfied:

(a) the client has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;

(b) the size of the client's financial instrument portfolio, defined as including cash deposits and financial instruments, exceeds EUR 500,000;

(c) the client works or has worked in the financial sector for at least one year in a professional position, which requires knowledge of the transactions or services envisaged;

(the "quantitative test"); and

(3) the following procedure is followed:

(a) the client must state in writing to the firm that it wishes to be treated as a professional client either generally or in respect of a particular service or transaction or type of transaction or product;

(b) the firm must give the client a clear written warning of the protections and investor compensation rights the client may lose;

and

(c) the client must state in writing, in a separate document from the contract, that it is aware of the consequences of losing such protections.

[Note: first, second, third and fifth paragraphs of section II.1 and first paragraph of section II.2 of annex II to MiFID]

3.5.4

If the client is an entity, the qualitative test should be performed in relation to the person authorised to carry out transactions on its behalf.

[Note: fourth paragraph of section II.1 of annex II to MiFID]

3.5.5

The fitness test applied to managers and directors of entities licensed under directives in the financial field is an example of the assessment of expertise and knowledge involved in the qualitative test.

[Note: fourth paragraph of section II.1 of annex II to MiFID]

3.5.6

Before deciding to accept a request for re-categorisation as an elective professional client a firm must take all reasonable steps to ensure that the client requesting to be treated as an elective professional client satisfies the qualitative test and, where applicable, the quantitative test.

[Note: second paragraph of section II.2 of annex II to MiFID]

3.5.7

An elective professional client should not be presumed to possess market knowledge and experience comparable to a per se professional client

[Note: second paragraph of section II.1 of annex II to MiFID]

3.5.8

Professional client are responsible for keeping the firm informed about any change that could affect their current categorisation.

[Note: fourth paragraph of section II.2 of annex II to MiFID]

3.5.9

(1) If a firm becomes aware that a client no longer fulfils the initial conditions that made it eligible for categorisation as an elective professional client , the firm must take the appropriate action.

(2) Where the appropriate action involves re-categorising that client as a retail client, the firm must notify that client of its new categorisation.

[Note: fourth paragraph of section II.2 of annex II to MiFID and article 28(1)
of the MiFID implementing Directive]

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Financial Conduct Authority

MiFID II Client Categorisation Regime

Local authorities & the Local Government Pension Scheme ("LGPS")

Agenda

- Timeline
- MiFID II & the Client categorisation regime
- Why retail and what is the practical impact?
- FCA's Role
- Opting-up regime – current criteria
- Desired outcomes (1) – Local authorities
- Desired outcomes (2) - what about the LGPS?
- Benefits of retail client status

Timeline

- ***June 2014***: MiFID II published in Official Journal
- ***2015 – 2016***: FCA stakeholder engagement
  March 2015: FCA Discussion Paper Published (*including treatment of Local authorities*)
- ***Early 2016***: FCA Consultation Paper on Conduct Matters
- ***Q2 2016***: FCA Policy Statement
- ***July 2016***: Transposition deadline
- ***3 January 2017***: MiFID II applies

MiFID II & Client Categorisation Regime

- Improving investor protection
- Retained key principles of regime
- Local authorities re-categorised as retail – BUT can "opt-up" to professional status
- Decision taken during L1 process

Why retail and what practical impact?

- Why? To increase protection for all clients, especially Local authorities
- Retail clients vs. professional clients
- Firms will need retail permissions
- Marketing restrictions for alternative investment funds (professional-only)

FCA's Role

- FCA has **no discretion** to change default retail categorisation
- But we can…
- Design alternative/additional criteria to current quantitative criteria for opting-up

Opting-up Regime - Current Criteria

- Retail clients can opt-up if they meet specific criteria – COBS 3.5.3R

- This consists of:

(i) **a qualitative test**
(ii) **a quantitative test;** and the
(iii) **requirement** to follow a **specific procedure**

Desired Outcome (1) – Local authorities

- FCA intends to exercise discretion
- Why? To protect smaller, less sophisticated Local authorities
- Proportionate thresholds– flexible approach to opting-up

Desired Outcome (2): What about LGPS?

- LGPS Administering authorities not legally separate from Local authorities **So**…
- FCA required to apply retail categorisation
- Flexible opt-up conditions

Benefits of Retail Client Status

- Local authorities will benefit from full suite of MiFID's regulatory protections
- Additional disclosures/information (e.g. costs & charges)
- Suitability & appropriateness assessments – wider scope in MiFID II

Questions or Comments?

- All welcome.

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Non-Executive Report of the: **PENSIONS COMMITTEE** **25 November 2015**	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
Collaboration Work Update – (London CIV and National LGPS Framework)	

Originating Officer(s)	Bola Tobun, Investment and Treasury Manager
Wards affected	All

Summary

This report provides the Committee with an update on the progress of the Collective Investment Vehicle (CIV) being set up by local government funds in London in collaboration with London Councils. It also provides an update on the progress of the National LGPS Frameworks, in which the Fund is involved.

Recommendations:

Members of the Pensions Committee are asked to:

- Note the contents of the report.

1. REASONS FOR THE DECISIONS

1.1 No decision required

2. ALTERNATIVE OPTIONS

2.1 No alternative as this is for information and update.

3. DETAILS OF REPORT

London CIV

3.1 Committee members have received a number of reports and presentations which have covered both the calls for structural reform emanating from CLG and the work that has been going on in London to consider ways of working more collaboratively with other funds and more specifically to consider options for the establishment of a collective investment vehicle in London.

3.2 Following a Board meeting of the London CIV on 8th September, the interim Board has now been replaced by a permanent Board. The Chair of the Board is Lord Kerslake with non-executive director appointments of Chris Bilsland and Lisa Arnold with a further non-executive director expected to be appointed during the next few months. The new Investment Advisory Committee has been established which replaces the Technical Sub-Group which had helped in the establishment of the CIV. An officer from the Council, the Investment & Treasury Manager has been appointed to the new Investment Advisory Committee.

3.4 Negotiations and contractual arrangements have been ongoing with fund managers to ensure that the initial range of managers to be transitioned across to the London CIV is ready once approval has been given by the FCA.

3.5 The London CIV continues to make progress and the Financial Conduct Authority (FCA) authorised the company as an Alternative Investment Fund Manager on 15 October 2015. The Company's entry in the FCA register can be found here:

https://register.fca.org.uk/ShPo_FirmDetailsPage?id=001b000000sD6OtAAK

3.6 The application for Fund authorisation was submitted to the FCA on 15 October and authorisation was granted 13 November 2015 as the FCA treated the application as a priority. As the FCA authorised the Fund in line with the London CIV timetable, it is now possible to launch the CIV's first sub-fund before the end of the year. On the assumption that the first fund will be launched as planned the aim is to open the remaining eight sub-funds in the first quarter of 2016. Detailed fund information has been sent to all the boroughs that are invested in the same or similar mandates with the relevant Fund Managers and each borough has been asked to give feedback about their intention to transition to the CIV or not. If all boroughs do transition the CIV will have in excess of £6bn under management by the end of this financial year.

3.7 Regulatory Capital: with the adoption of the revised Articles and the signing of the Shareholders Agreement it has been possible to issue share subscription letters to each borough for the B shares that will generate the required regulatory capital. The London Borough of Tower Hamlets Pension Fund in accordance with the Committee's decision (23 July 2015) will pay the regulatory capital to the London CIV by 30 November 2015.

3.8 The Investment Advisory Committee (IAC) has now been established and is working on a range of options for consideration by the Sectoral Joint Committee with papers at the recent meeting on Infrastructure.

3.9 Working groups have been established to come forward with proposals on ethical tracker funds, options for fixed interest, further work on infrastructure, private rented sector and social housing. The initial managers have been selected, these are not publicly available at this stage. In addition, further work is being undertaken over the coming months by the investment committee and the CIV to identify new areas for the CIV to consider in particular in the alternative investment field and fixed income.

3.10 As the London Collective Investment Vehicle (CIV) enters its final implementation phase, the Fund has been asked to make the final investment decision to invest in sub-funds proposed for the CIV launch in November 2015.

3.11 Four managers have now been identified as offering potential opportunities for the launch of the CIV. These managers will provide the CIV with 9 sub-funds, covering just over £6bn of Borough assets and providing early opportunity to 20 boroughs. The sub-funds will consist of 6 'passive' equity sub-funds covering £4.2bn of assets, 2 Active Global Equity mandates covering £1.6bn and 1 Diversified Growth (or multi-asset) Fund covering just over £300m.

3.12 20 boroughs are currently invested in one or more of these mandates and LBTH is one of them. Those boroughs that do not have an exact match across for launch are able to invest in these sub-funds from the outset at the reduced Asset Management Company (AMC) rate that the CIV has negotiated with managers.

3.13 There are a number of other managers with whom discussions are still ongoing, but these are currently being viewed as 'post-launch' (phase 2, spring 2016) opportunities.

3.14 LBTH Pension Fund is one of the London LGPS Funds with direct links to the launch sub-funds. An indication was given to London CIV by the s151 officer having consulted with the Chair and Vice Chair of the Pensions Committee, that the Fund would transfer the current holdings with one of the two global equity managers to the CIV and to hold on transferring the UK Equity mandate to the CIV pending more desirable negotiation entry terms for this mandate.

National LGPS Frameworks

3.15 The Fund Officer is now working closely with a number of other authorities to develop national procurement frameworks, with the work of the group being recognised at the recent LGC Investment Awards.

3.16 Current frameworks under development include the re-letting of the actuarial and investment consultancy frameworks as they are nearing the end of the 4 year framework lifespan for the original frameworks. In addition the

Environmental, Social and Governance (ESG) Framework is currently being developed and it is anticipated that this framework will be available for call off by early summer 2016. This is likely to offer a number of lots, which funds will be able to call off including voting services, governance overlay and research work.

3.17 It is anticipated that work will also commence shortly on the formation of a framework for third party administration services. Consideration is also being given by the National Frameworks for the establishment of a passive fund manager framework and a transition manager framework.

3.18 The Fund has been a keen proponent of collaborative working believing that this will deliver benefits to the Fund not just in terms of financial savings but also delivering wider governance benefits.

3.19 it is important to recognise that the work that the Fund and others, particularly in London have been doing to work collaboratively means that the Fund is in a reasonable position to respond to any consultation on pooling of investments with the establishment of the London CIV appearing to be recognised as an important part of those pooling arrangements which have already commenced. The indications from government are that we could expect to see a consultation which seeks to deliver between 5-6 LGPS investment pools across England and Wales of around £30bn each to deliver efficiency savings across the LGPS. Full participation by London Boroughs in the London CIV would deliver a pool of investments close to this magnitude.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 The comments of the Corporate Director of Resources are incorporated in the report.

5. LEGAL COMMENTS

There are no immediate legal implications arising from this report. However due consideration will need to be given to the issues that will arise from:

the proposed pooling of pension fund investments once the consultation is underway;

When deciding whether or not to proceed with a project, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty).

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.

6.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

7. BEST VALUE (BV) IMPLICATIONS

7.1 To have an efficient, cost reduction platform for investment management of the fund by pooling and collaborating is considered to be a good decision which can result in greater cost savings to the fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 The rigorous robust management of LBTH Pension Fund results in better quicker and more effective decision making which can lead to better Fund performance and reduction in the contribution required from the Council towards the Fund. The monitoring arrangement for the Pension Fund and the work of the Pensions Committee should ensure that the Fund optimises the use of its resources in achieving the best returns for the Council and members of the Fund.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report
- NONE

Appendices
- NONE

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report
- NONE

Officer contact details for documents:
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Non-Executive Report of the: **Pensions Committee** 25 November 2015	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
2014/15 Pension Fund Annual Report and Audit Report (ISA 260 Report)	

Originating Officer(s)	Bola Tobun, Investment and Treasury Manager
Wards affected	All wards

Summary

This report presents the Pension Fund Annual Report and Statement of Accounts for 2014/15 and 2014/15 Pension Fund Audit Report (ISA 260 Report) following the audit by KPMG.

The Statement of Accounts has been prepared under International Financial Reporting Standards (IFRS) rules and is now presented for consideration by the Pensions Committee.
This report introduces
.

Recommendations:

The Pensions Committee is recommended to:

- Approve the Pension Fund Statement of Accounts;
- Approve the Pension Fund Annual Report (Appendix B):
- Note the draft ISA 260 (Appendix A).

1. REASONS FOR THE DECISIONS

1.1 The Local Government Pension Scheme Regulations 2013, Regulation 53(2) state that ‘An administering authority is responsible for managing and administering the Scheme in relation to any person for which it is the appropriate administering authority under these Regulations’ and the internal audit report covered the area of how the Fund was being administered.

1.2 The Committee acts as quasi-trustee to the Pension Fund and as such acts in the capacity of the Administering Authority of the Pension Fund. The Committee’s terms of reference require it to receive and approve an Annual Report and Accounts on the activities of the Fund prior to publication. The Local Government Pension Scheme Regulations 2013, Regulation 57 require the Pension Fund to publish this by 1 December following the financial year end and for the Report to contain a number of standard items.

1.3 The publication of the Pension Fund Annual Report and Statement of Accounts helps to keep Fund members informed, shows good governance and also helps to demonstrate effective management of Fund assets

2. ALTERNATIVE OPTIONS

2.1 There are no alternative options in so far as the publication of the Statement of Accounts and Annual Reports is a legislative requirement.

3. DETAILS OF REPORT

3.1 The Council as an administering authority under the Local Government Pension Scheme Regulations is required to produce a separate set of accounts for the scheme’s financial activities and assets and liabilities.

3.2 The contents and format of the accounts are determined by statutory requirements and mandatory professional standards as established by the Chartered Institute of Public Finance (CIPFA) in their Service Code of Recommended Practice (SERCOP).

3.3 The London Borough of Tower Hamlets is the Administering Authority for the London Borough of Tower Hamlets’ Pension Fund and the Pensions Committee act as trustees of the Pension Fund which includes overseeing the accounting and financial management of the Pension Fund.

3.4 The Pensions Committee reviewed the Pension Fund Annual Report and Accounts at its meeting on 23rd July 2015. KPMG started the audit of the account October 2015.

3.5 KPMG is required to issue an ISA 260 report and opinion on the council’s accounts and this includes an opinion on the Pension Fund. This report sets out their opinions and any issues which they believe the Committee should be aware of.

3.6 At the time of writing this report, work on the audit of the Pension Fund accounts is substantially complete, subject to the completion of the auditor’s final review and completion procedures. The auditor expects to issue an unqualified audit opinion on the Pension Fund and their comments are included within the attached draft ISA 260. Comments on their findings are included under Section 3.

3.7 Since the Annual Report and Accounts were initially presented to the Pensions Committee in July, there have been a small number of amendments which have been included within the updated version. At the time of writing this report, these are mainly presentational. KPMG has not identified any significant issues to bring to the attention of the Pensions Committee.

3.8 THE ANNUAL REPORT AND STATEMENT OF ACCOUNTS

3.8.1 The Accounts comprise two main statements with supporting notes. The main statements are:

- Dealings with Members Employers and Others which is essentially the funds revenue account
- The Net Assets Statement which can be considered as the funds balance sheet.

3.8.2 The return on investment section of the accounts sets out the movement in the net worth of the fund in the year by analysing the relevant financial transactions and movements in the market value of the investment portfolio. The statement has two main sections:

- The financial transactions relating to the administration of the fund.
- The transactions relating to its role as an investor.

3.8.3 The fund income section of the report principally relates to the receipt of contributions from employers and active members and the payment of pensions benefits. The section indicates that the Fund is cash positive in that the receipt of contributions exceeds the pension payments £5.2m in 2014/15 compared to £8.2m in 2013/14 and £3.2m in 2012/13.

3.8.4 The Fund net cash flow position in 2014/15 is 36% less than the previous year. Investment income increased over the year by £5.2m (46.8%) mainly due to an increase in dividend income. Transfer Values received (amounts paid over when a fund member transfers their benefits from one fund to another) decreased by £1.8m (51.4%). It is not possible to predict the value of transfer value payments as they are dependent on an individual’s length of service and salary and as such may vary significantly. Employee contributions rose by £1.0m (10.0%), the increase being attributable to the new CARE scheme which sees contributions deducted from all additional pay and also to the increase in the banding rate which sees higher rates of pay subject to a contribution rate of up to 12.5%. Employer contributions went up by £3.7m (8.7%) due to an increase in the employer’s deficit funding payment of £2m.

3.8.5 In 2014/15 the overall Fund expenditure increased by £5.7m (11.4%). The major contributor to the increase was the rise in transfers out of £4.5m (160.7%). There was a modest increase in investment management costs of £0.1m (4.2%) while administration costs fell by £0.3m (27.3%). Benefits payable rose by £1.4m (3.2%).

3.8.6 Overall, fund membership has increased. The active members increased marginally by 68 (1%) and deferred and retired membership numbers by 122 (1.8%) and 106 (2.5%) respectively.

3.8.7 The investment performance section of the report details returns on the investment portfolio and the impact of managers' activities and investment markets on the value of investments. The Fund achieved a return on its investment portfolio of 11.8% in 2014/15 outperforming the benchmark return of 11.4% by 0.4%. The Fund posted a 3 year return of 10.7% which is marginally better than the benchmark return of 10.0% but delivered a 10 year return of 7.1% underperforming a benchmark return of 7.4% by 0.3%.

3.8.8 Overall, fund assets increased by £125m. The increase was mostly due to gains made from performance of financial markets in which the Fund held its investments and a net gain between fund income and expenditure.

3.8.9 The net asset statement represents the net worth (£1,138m) of the Fund as at the 31st March 2015. The statement reflects how the transactions outlined in the other statement have impacted on the value of the Fund's assets.

3.5.10 The annual report also includes three key statements (Funding Strategy Statement, Statement of Investment Principles and Governance Compliance Statement) relating to the management and governance of the scheme and each statement serves a different purpose.

3.8.11 The Funding Strategy Statement undergoes a detailed review and was updated after the triennial valuation. The 2013 triennial valuation outcome was reported, discussed and approved at the Pensions Committee meeting of 27th February 2014.

3.8.12 The purpose of the Funding Strategy statement is threefold:

- 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 contributions rates as possible; and
- To take a prudent longer-term view of funding those liabilities.

3.8.13 The Statement of Investment Principles facilitates adherence to best practice in the management of pension schemes as set out by the revised Myners Principles and the fund is required to state the extent to which it has complied with these principles.

3.8.14 The Governance Compliance Statement sets out the council's policy as the administering authority in relation to its governance responsibilities for the Fund.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 The comments of the Corporate Director of Resources have been incorporated into the report.

5. LEGAL COMMENTS

5.1 Regulation 34 of the Local Government Pension Scheme (Administration) Regulations 2008 imposes a duty on the Council as an administering authority to prepare a pension fund annual report.

5.2 The report should deal with the following matters:

(a) management and financial performance during the year of the pension;
(b) an explanation of the investment policy for the fund and a review of performance;
(c) a report on arrangements made during the year for administration of the fund;
(d) a statement by an actuary who carried out the most recent valuation of the fund and the level of funding disclosed by that valuation;
(e) a Governance Compliance Statement;
(f) a Fund Account and Net Asset Statement;
(g) an Annual Report dealing with levels of performance and any other appropriate matters;
(h) the Funding Strategy Statement;
(i) the Statement of Investment Principles;
(j) statements of policy concerning communications with members and employing authorities; and
(k) any other material which the authority considers appropriate.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The Pension Fund Accounts demonstrate financial stewardship of the fund's assets. A financially viable and stable pension fund is a valuable recruitment and retention incentive for the Council.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The monitoring arrangement for the Pension Fund and the work of the officers, advisers and consultants should ensure that the Fund optimises the use of its resources in achieving the best returns for members of the Fund.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 Accounts provide an effective mechanism to safeguard the Council's assets and assess the risks associated with its activities.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no any Crime and Disorder Reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- NONE

Appendices

- NONE

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report

- NONE

Officer contact details for documents:
Bola Tobun(Investment & Treasury Manager) x4733

cutting through complexity

Report to those charged with governance (ISA 260) 2014/15

London Borough of Tower Hamlets Pension Fund

November 2015

Contents

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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Andrew Sayers, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Trevor Rees (on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk). After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

Introduction

This document summarises:

- **the key issues identified during our audit of the financial statements for the year ended 31 March 2015 for the Pension Fund.**

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Scope of this report

This report summarises the key findings arising from:

- our audit work at the London Borough of Tower Hamlets Pension Fund (‘the Pension Fund’) in relation to the Pension Fund’s 2014/15 financial statements and Annual Report.

Financial statements

Our *External Audit Plan 2014/15*, presented to you in June 2015, set out the four stages of our financial statements audit process.

This report focuses on the third stage of the process: substantive procedures. Our on site work for this took place during October 2015.

We are now in the final phase of the audit, the completion stage. Some aspects of this stage are also discharged through this report.

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages.
- Section 3 sets out our key findings from our audit work in relation to the 2014/15 financial statements of the Pension Fund.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

Headlines

This table summarises the headline messages for the Pension Fund. Section three of this report provides further details on each area.

Proposed audit opinion	We anticipate issuing an unqualified audit opinion on the Pension Fund's financial statements as contained in the Pension Fund Annual Report by 30 November 2015.
Audit adjustments	Our audit has not identified any significant audit adjustments. A number of minor amendments focused on presentational improvements have been made to the draft financial statements. We have not raised any recommendations as a result of our audit of the Pension Fund in 2014/15.
Key financial statements audit risks	We review risks to the financial statements on an ongoing basis. We identified one significant risk specific to the Pension Fund during 2014/15 with respect to the financial statements. This risk related to the LGPS reforms which commenced on 1 April 2014. We have worked with officers throughout the year to discuss this key risk and our detailed findings are reported in section 3 of this report. There are no matters to report to you as a result of our audit work on this significant risk.
Accounts production and audit process	We have noted that the quality of the accounts and the supporting working papers has been maintained. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales. The Authority has good processes in place for the production of the accounts and good quality supporting working papers. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.
Completion	At the date of this report our audit of the financial statements is complete subject to completing our final review and completion procedures. Before we can issue our opinion we require a signed management representation letter. We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.

Proposed opinion and audit differences

We have not identified any issues in the course of the audit of the Fund that are considered to be material.

We anticipate issuing an unqualified audit opinion in relation to the Fund's financial statements, as contained in the Pension Fund Annual Report by 30 November 2015.

Proposed audit opinion

Subject to all review and completion procedures being resolved satisfactorily, we anticipate issuing an unqualified audit opinion on the Pension Fund's financial statements included in the Pension Fund Annual Report following approval by the Pensions Committee on 25 November 2015.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The final materiality level (see Appendix 3 for more information on materiality) for this year's audit was set at £20 million. Audit differences below £1 million are not considered significant.

We did not identify any significant misstatements.

We identified a small number of presentational adjustments required to ensure that the accounts are compliant with the *Code of Practice on Local Authority Accounting in the United Kingdom 2014/15 ('the Code')*. We understand that the Pension Fund will be addressing these where significant.

Pension Fund Annual Report

We have reviewed the Pension Fund Annual Report and confirmed that it complies with the requirements of the Local Government Pension Scheme (Administration) Regulations 2008.

The statutory deadline for publishing the document is 1 December 2015.

Financial Statements (continued)
Significant risks and key areas of audit focus

We have worked with the Authority throughout the year to discuss significant risks and key areas of audit focus.

This section sets out our detailed findings on those risks.

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In our External Audit Plan 2014/15, presented to you in June 2015, we identified the significant risks affecting the Authority and the Fund's 2014/15 financial statements. We have now completed our testing of these areas and set out our evaluation following our substantive work.

The table below sets out our detailed findings for each of the risks that are specific to the Authority.

Significant audit risk	Issue	Findings
LGPS Reforms	From 1 April 2014, all members of the LGPS have automatically joined the new career average defined benefit scheme. The new scheme provides more flexibility on when members can take their pension and also how much they pay in. There is a risk that pension administration systems have not been set up to correctly reflect the changes resulting from LGPS 2014 and will therefore not accurately calculate the pension benefits due to members. While any errors in the system are unlikely to result in material misstatements in 14/15, the possible cumulative effect in future years means that specific audit work is needed on ensuring that the changes required to the system have been accurately reflected.	We have reviewed the controls and processes that the Pension Fund has put in place to accurately capture the data required by LGPS 2014. Our work focused on testing that the system has been set up to accurately calculate future benefit entitlement by testing a sample of calculations for members of the Pension Fund who retired in 2014/15. We have no matters to report in respect of the testing performed.

Financial Statements (continued)
Significant risks and key areas of audit focus (continued)

In our *External Audit Plan 2014/15* we reported that we would consider two risk areas that are specifically required by professional standards and report our findings to you. These risk areas were Management override of controls and the Fraud risk of revenue recognition.

The table below sets out the outcome of our audit procedures and assessment on these risk areas.

Areas of significant risk	Summary of findings
Management override of controls Audit areas affected ■ All areas	Our audit methodology incorporates the risk of management override as a default significant risk. Management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We have not identified any specific additional risks of management override relating to this audit. In line with our methodology, we carried out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual. There are no matters arising from this work that we need to bring to your attention.
Fraud risk of revenue recognition Audit areas affected ■ None	Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. In our External Audit Plan 2014/15 we reported that we do not consider this to be a significant risk for Local Authorities and Pension Funds as there is unlikely to be an incentive to fraudulently recognise revenue. This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.

Financial Statements (continued)
Accounts production and audit process

The Authority has a well established and sound accounts production process. This operated well in 2014/15, and the standard of accounts and supporting working papers was good.

Officers dealt promptly and efficiently with audit queries and the audit process was completed within the planned timescales.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.

Before we can issue our opinion we require a signed management representation letter.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the significant qualitative aspects of the Authority's accounting practices and financial reporting. We also assessed the Authority's process for preparing the accounts and its support for an efficient audit.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	The Pension Fund continues to maintain a good financial reporting process and produce statements of accounts to a good standard. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 30 June 2015. The Pension Fund has made a small number of presentational changes to the accounts presented for audit however there have been no changes which we consider to be fundamental.
Quality of supporting working papers	We issued our *Accounts Audit Protocol* including our required working papers for the audit in July 2015. The quality of working papers provided was good and met the standards specified in our *Accounts Audit Protocol*.
Response to audit queries	Officers resolved all audit queries in a timely manner.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of the London Borough of Tower Hamlets Pension Fund for the year ending 31 March 2015, we confirm that there were no relationships between KPMG LLP and the London Borough of Tower Hamlets Pension Fund, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 2 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the Corporate Director of Resources for presentation to the Pensions Committee. We require a signed copy of your management representations before we issue our audit opinion.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- significant difficulties encountered during the audit;
- significant matters arising from the audit that were discussed, or subject to correspondence with management;
- other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and
- matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions/objections, opening balances etc).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report.

Appendix 1: Audit differences

Our audit has not identified any significant audit adjustments. A number of minor amendments focused on presentational improvements have been made to the draft financial statements.

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We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

Audit differences

Our audit has not identified any significant audit adjustments.

A number of minor amendments focused on presentational improvements have been made to the draft financial statements. The Finance Department are committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Appendix 2: Declaration of independence and objectivity

The *Code of Audit Practice* requires us to exercise our professional judgement and act independently of both Public Sector Audit Appointments Ltd and the Authority.

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Requirements

Auditors appointed by Public Sector Audit Appointments Ltd must comply with the *Code of Audit Practice* (the 'Code') which states that:

"Auditors and their staff should exercise their professional judgement and act independently of both the Commission and the audited body. Auditors, or any firm with which an auditor is associated, should not carry out work for an audited body that does not relate directly to the discharge of auditors' functions, if it would impair the auditors' independence or might give rise to a reasonable perception that their independence could be impaired."

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code, the detailed provisions of the Statement of Independence included within the Public Sector Audit Appointments Ltd *Terms of Appointment* ('Public Sector Audit Appointments Ltd Guidance') and the requirements of APB Ethical Standard 1 *Integrity, Objectivity and Independence* ('Ethical Standards').

The Code states that, in carrying out their audit of the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time. Public Sector Audit Appointments Ltd guidance requires appointed auditors to follow the provisions of ISA (UK &I) 260 Communication of *Audit Matters with Those Charged with Governance*' that are applicable to the audit of listed companies. This means that the appointed auditor must disclose in writing:

- Details of all relationships between the auditor and the client, its directors and senior management and its affiliates, including all services provided by the audit firm and its network to the client, its directors and senior management and its affiliates, that the auditor considers may reasonably be thought to bear on the auditor's objectivity and independence.
- The related safeguards that are in place.
- The total amount of fees that the auditor and the auditor's network firms have charged to the client and its affiliates for the provision of services during the reporting period, analysed into appropriate categories, for example, statutory audit services, further audit services, tax advisory services and other non-audit services. For each category, the amounts of any future services which have been contracted or where a written proposal has been submitted are separately disclosed. We do this in our *Annual Audit Letter*.

Appointed auditors are also required to confirm in writing that they have complied with Ethical Standards and that, in the auditor's professional judgement, the auditor is independent and the auditor's objectivity is not compromised, or otherwise declare that the auditor has concerns that the auditor's objectivity and independence may be compromised and explaining the actions which necessarily follow from his. These matters should be discussed with the Audit Committee and Pensions Committee.

Ethical Standards require us to communicate to those charged with governance in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on our independence and the objectivity of the Engagement Lead and the audit team.

General procedures to safeguard independence and objectivity

KPMG's reputation is built, in great part, upon the conduct of our professionals and their ability to deliver objective and independent advice and opinions. That integrity and objectivity underpins the work that KPMG performs and is important to the regulatory environments in which we operate. All partners and staff have an obligation to maintain the relevant level of required independence and to identify and evaluate circumstances and relationships that may impair that independence.

Appendix 2: Declaration of independence and objectivity (continued)

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.

Acting as an auditor places specific obligations on the firm, partners and staff in order to demonstrate the firm's required independence. KPMG's policies and procedures regarding independence matters are detailed in the *Ethics and Independence Manual* ('the Manual'). The Manual sets out the overriding principles and summarises the policies and regulations which all partners and staff must adhere to in the area of professional conduct and in dealings with clients and others.

KPMG is committed to ensuring that all partners and staff are aware of these principles. To facilitate this, a hard copy of the Manual is provided to everyone annually. The Manual is divided into two parts. Part 1 sets out KPMG's ethics and independence policies which partners and staff must observe both in relation to their personal dealings and in relation to the professional services they provide. Part 2 of the Manual summarises the key risk management policies which partners and staff are required to follow when providing such services.

All partners and staff must understand the personal responsibilities they have towards complying with the policies outlined in the Manual and follow them at all times. To acknowledge understanding of and adherence to the policies set out in the Manual, all partners and staff are required to submit an annual ethics and independence confirmation. Failure to follow these policies can result in disciplinary action.

Auditor declaration

In relation to the audit of the financial statements of the London Borough of Tower Hamlets Pension Fund for the financial year ending 31 March 2015, we confirm that there were no relationships between KPMG LLP and the London Borough of Tower Hamlets Pension Fund, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

Appendix 3: Materiality and reporting of audit differences

For 2014/15 our materiality for the Pension Fund is £20 million.

We have not identified any significant audit differences that need to be reported to the Pensions Committee.

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Materiality

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects: materiality by value, nature and context.

- Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.
- Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.
- Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2014/15, presented to you in June 2015

Materiality for the Pension Fund was set at £20 million which equates to around 1.8 percent of gross assets. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Pensions Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Pensions Committee any misstatements of lesser amounts to the extent that these are identified by our audit work.

Under ISA 260, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of the Pension Fund, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £1 million.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Pensions Committee to assist it in fulfilling its governance responsibilities.

Appendix 4: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

KPMG's Audit Quality Framework consists of seven key drivers combined with the commitment of each individual in KPMG.

The diagram summarises our approach and each level is expanded upon.

At KPMG we consider audit quality is not just about reaching the right opinion, but how we reach that opinion. KPMG views the outcome of a quality audit as the delivery of an appropriate and independent opinion in compliance with the auditing standards. It is about the processes, thought and integrity behind the audit report. This means, above all, being independent, compliant with our legal and professional requirements, and offering insight and impartial advice to you, our client.

KPMG's Audit Quality Framework consists of seven key drivers combined with the commitment of each individual in KPMG. We use our seven drivers of audit quality to articulate what audit quality means to KPMG.

We believe it is important to be transparent about the processes that sit behind a KPMG audit report, so you can have absolute confidence in us and in the quality of our audit.

Tone at the top: We make it clear that audit quality is part of our culture and values and therefore non-negotiable. Tone at the top is the umbrella that covers all the drives of quality through a focused and consistent voice. Andrew Sayers as the Engagement Lead sets the tone on the audit and leads by example with a clearly articulated audit strategy and commits a significant proportion of his time throughout the audit directing and supporting the team.

Association with right clients: We undertake rigorous client and engagement acceptance and continuance procedures which are vital to the ability of KPMG to provide high-quality professional services to our clients.

Clear standards and robust audit tools: We expect our audit professionals to adhere to the clear standards we set and we provide a range of tools to support them in meeting these expectations. The global rollout of KPMG's eAudIT application has significantly enhanced existing audit functionality. eAudIT enables KPMG to deliver a highly technically enabled audit. All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.

Recruitment, development and assignment of appropriately qualified personnel: One of the key drivers of audit quality is assigning professionals appropriate to the Authority's risks. We take great care to assign the right people to the right clients based on a number of factors including their skill set, capacity and relevant experience.

We have a well developed technical infrastructure across the firm that puts us in a strong position to deal with any emerging issues. This includes:

- A national public sector technical director who has responsibility for co-ordinating our response to emerging accounting issues, influencing accounting bodies (such as CIPFA) as well as acting as a sounding board for our auditors.

- A national technical network of public sector audit professionals is established that meets on a monthly basis and is chaired by our national technical director.

- All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.

- A dedicated Department of Professional Practice comprised of over 100 staff that provide support to our audit teams and deliver our web-based quarterly technical training.

Appendix 4: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

Quality must build on the foundations of well trained staff and a robust methodology.

Commitment to technical excellence and quality service delivery: Our professionals bring you up- the-minute and accurate technical solutions and together with our specialists are capable of solving complex audit issues and delivering valued insights.

Our audit team draws upon specialist resources including Forensic, Corporate Finance, Transaction Services, Advisory, Taxation, Actuarial and IT. We promote technical excellence and quality service delivery through training and accreditation, developing business understanding and sector knowledge, investment in technical support, development of specialist networks and effective consultation processes.

Performance of effective and efficient audits: We understand that how an audit is conducted is as important as the final result. Our drivers of audit quality maximise the performance of the engagement team during the conduct of every audit. We expect our people to demonstrate certain key behaviors in the performance of effective and efficient audits. The key behaviors that our auditors apply throughout the audit process to deliver effective and efficient audits are outlined below:

- timely Engagement Lead and manager involvement;
- critical assessment of audit evidence;
- exercise of professional judgment and professional scepticism;
- ongoing mentoring and on the job coaching, supervision and review;
- appropriately supported and documented conclusions;
- if relevant, appropriate involvement of the Engagement Quality Control reviewer (EQC review);
- clear reporting of significant findings;
- insightful, open and honest two-way communication with those charged with governance; and
- client confidentiality, information security and data privacy.

Commitment to continuous improvement: We employ a broad range of mechanisms to monitor our performance, respond to feedback and understand our opportunities for improvement.

Our quality review results

Public Sector Audit Appointments Ltd publishes information on the quality of work provided by us (and all other firms) for audits undertaken on behalf of them (http://www.psaa.co.uk/audit-quality/principal-audits/kpmg-audit-quality/).

The latest Annual Regulatory Compliance and Quality Report issued June 2015 showed that we are meeting the overall audit quality and regulatory compliance requirements.

cutting through complexity™

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TOWER HAMLETS

The London Borough of Tower Hamlets Pension Fund
Annual Report 2014/15

WWW.TOWERHAMLETS.GOV.UK

Contents

Foreword by Chris Holme: Acting Corporate Director, Resources

This is to introduce the London Borough of Tower Hamlets (LBTH) Pension Fund Annual Report and Accounts for 2014/15. The Pensions Committee has the responsibility for the management of all aspects of the Pension Fund including the performance of the professional fund managers appointed to administer its investment portfolio.

The new Local Government Pension Scheme (LGPS) started on 01 April 2014 and it has been a remarkable period for officers communicating the change to scheme members and considerable amount of work has been invested in ensuring that the administration systems would be able to deliver the regulatory changes.

On 1 May 2014, the Government launched a second consultation on further proposed changes to the LGPS entitled: Opportunities for Collaboration, Cost Savings and Efficiencies. The responses received were evaluated. The consultation paper proposed a solution, based on cutting fees, moving all actively managed assets to passive funds, and the establishment of collective investment vehicles (CIVs).

A joint London Borough Pension Working Group led by London Councils launched a Collective investment vehicle to enable London Boroughs to participate in a scheme of joint pension fund investing. It will be an Authorised Contractual Scheme (ACS). This scheme will require FCA (Financial Conduct Authority) approval – this approval is being sought.

LBTH agreed to participate in the CIV at Full Council in 2014 following recommendation by Pensions Committee and Cabinet.

All asset classes delivered a positive performance over the year resulting in an overall increase in the assets under management, notwithstanding there was volatility during the year, particularly with geopolitical concerns in the Ukraine and in the Middle East. The sharp falls in the oil price over the year, helped to boost markets and lower inflation, with even Europe starting to show some tentative signs of recovery by the year end. However, there remain concerns over the timing of any interest rate rises and the effect that this will have on bond markets and any wider implications for equity markets. For some time now, commentators have suggested that government bond markets look overstretched with bond yields remaining at low levels.

A funding update report was prepared and provided by the Fund Actuary to illustrate the estimated development of the funding position from 31 March 2013 to 31 March 2015, for the Fund. It is addressed to London Borough of Tower Hamlets in its capacity as the Administering Authority of the London Borough of Tower Hamlets Pension Fund.

This report illustrate as at 31 March 2015 the funding level has increased to 73.8% with corresponding deficit of £396m, from the funding level at the latest formal valuation of 71.8% with corresponding estimated deficit £365m. This was largely as a result of asset performance being better than expected. This has been offset by a decrease in the discount rate as the liability of the Fund grew from £1,293m as at 31 March 2013 triennial valuation to £1,514m as at 31 March 2015. Although equities have rebounded; bond yields are at record lows potentially raising the valuation of the Fund's liabilities. However, it is worth noting that the Council is a long term investor and has a relatively secure long term income stream. Therefore, the Fund should be able to alter strategy that enables it to ride out periods of market underperformance and should not have to crystallise losses during market downturns.

The Fund has seen continued growth in assets over the year benefiting from continued buoyant and booming of the financial markets, especially equities. The overall value of the portfolio of assets grew by 11.8% in 2014/15 outperforming benchmark by 0.4%. This performance is reflective of average return on pension fund assets nationally and also average gains in financial markets. Markets continue to be volatile therefore the short to medium term outlook for the performance of the Fund remains uncertain.

The Investment Strategy allocates assets across a range of asset classes and further attempts to minimise exposure to significant movements within each asset class by appointing fund managers that pursue contrasting but complementary investment strategies. This approach ensures a diversified and balanced portfolio that targets steady and sustainable growth. However, asset allocation can drift away from target over time due to market or manager performance. To ensure that strategic asset allocation is in line with target and Fund Strategy objectives, the Fund's swing manager, L&G Investment Management is tasked with rebalancing the portfolio between equities and bonds when allocation significantly varies from target.

The Fund net cash flow position remains positive with contributions and transfers in outstripping benefits paid and transfers out by £5.2m plus a further net inflow from investment income of £16.6m. The Pensions Committee monitor this aspect of the Fund closely as they recognised the need for the Fund to be able to pay its liabilities as they fall due and the ongoing austerity programme affecting public services.

In accordance with the new regulatory requirement to have additional governance arrangement in place by creating a Pension Board to assist the Administering Authority, the London Borough of Tower Hamlets, in ensuring compliance with regulations. This board has been established and appointments are currently underway with its first meeting due to take place towards the end of July 2015.

Chris Holme

Governance of the Pension Scheme

The London Borough of Tower Hamlets Pension Fund is part of the Local Government Pension Scheme (LGPS) and is governed by Statute.

The London Borough of Tower Hamlets is the Administering Authority for the London Borough of Tower Hamlets Pension Fund. The Pensions Committee has delegated responsibility for the management of the Fund and oversees the general framework within which the Fund is managed and sets investment policy on behalf of the Council and other employers in the Fund. Therefore, the Pensions Committee considers all investment aspects of the Pension Fund. The Corporate director of Resources has delegated authority for the day to day running of the Fund.

MANAGEMENT AND ADVISERS TO THE PENSION FUND as at 31st March 2015

The pensions Committee during 2014/15 was made up of eight Councillor Members, an Employer Representative and a Scheme Member representative.

Pensions Committee:

Councillors:	Councillor Rajib Ahmed (Chair) Councillor Abdul Asad Councillor Andrew Cregan Councillor Shafiqul Haque Councillor Claire Harrisson Councillor Ayas Miah Councillor Harun Miah Councillor Mohammed Mufti Miah
Trade Union Representative (non-voting):	Frank West (GMB)
Admitted Bodies Representative (non-voting):	John Gray (Circle Anglia Ltd)

Contact details for the Pensions Committee:-

Pensions Committee
London Borough of Tower Hamlets
Town Hall, Mulberry Place
5 Clove Crescent
London, E14 2BG

Staff, Advisers & Investment Managers

The management and administration of the pension Fund is delegated to the Corporate Director of Resources, having responsibility for the day to day management of the Fund.

London Borough of Tower Hamlets Responsible Officers:

Chris Holme – Acting Corporate Director of Resources

Bola Tobun – Investment & Treasury Manager

Kevin Miles – Chief Accountant

Anant Dodia – Pensions Manager

Advisers:

Consulting Actuary - Hymans Robertson LLP
Barry McKay - Actuarial Consultant/Adviser

Investment Consultant - Hymans Robertson LLP
Matt Woodman – Senior Investment Consultant

Independent Investment Adviser
Raymond Haines

Custodial Services - State Street Bank

Performance Measurement Services - WM Company

Legal Advisers - Legal Services
London Borough of Tower Hamlets, Town hall, Mulberry Place, 5 Clove Crescent, London, E14 2BG

Auditor - KPMG LLP (UK)

Investment Managers:

Baillie Gifford & Co
Calton Square, 1 Greenside Row, Edinburgh EH1 3AN

GMO UK Limited
1 London Bridge, London, SE1 9BG

Investec Asset Management
25 Basinghall Street, London, EC2V 5HA

Legal & General Investment Management Limited
One Coleman Street, London, EC2R 5AA

Ruffer LLP
80 Victoria Street, London SW1E 5JL

Schroder Investment Management Limited
31 Gresham Street, London EC2V 7QA.

Governance and Oversight Review

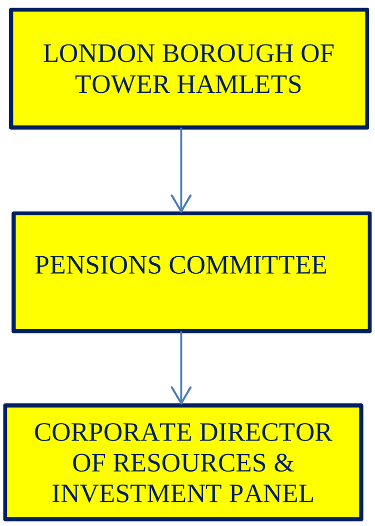
The Pension Fund Regulations require a new additional governance arrangement (Pensions Board) to be in place from 1 April 2015.

Although London Borough of Tower Hamlets is the Administering Authority of the pension Fund, but the delegated responsibility for the management of the pension fund is with the Pensions Committee and the new regulatory requirement is for a Pensions Board to assist the Authority in monitoring compliance with regulations by overseeing the Pensions Committee work in how the Fund is administered.

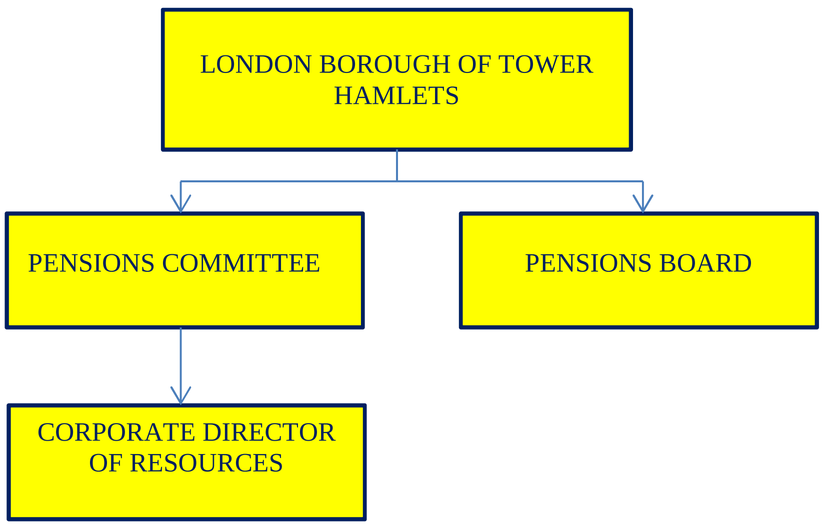
Full Council approved the establishment of the Pensions Board at its meeting in September 2015 with delegation authority for the composition of it and terms of reference to the Pensions Committee. Pensions Committee agreed the composition of the board comprising three Employer Representatives, three Employee Representatives and an Independent Chairman. The first meeting of the Pensions Board will take place in July 2015.

Please see below chart illustrating the old governance arrangement for the reporting year and new governance arrangement for 2015/15.

For Financial Year 2014/15



From Financial Year 2015/16



At the onset of Committee meetings, Committee members are required to make declarations of interest both in relation to membership of the Local Government Pension Scheme and relationship to any employer bodies within the Pension Fund. Further declarations are required as and when agenda items arise where a member may have a conflict of interest. The Governance Officer maintains a record of the Conflicts of Interest which covers Pensions Committee and Pensions Board Members as well as officers closely connected with the Fund.

A legal officer is present at the Committee meetings to provide guidance on legal matters and is also required to comment on other items where there could be conflicts of interest.

Pensions Committee Attendance 2014/15

Attendee	Voting Rights	13-Jul	17-Sep	19-Nov	24-Feb
Member					
Cllr Rajib Ahmed	√		Present	Present	Present
Cllr Abdul Asad	√				Present
Cllr Andrew Cregan	√	Present	Present	Present	
Cllr Shafiqul Haque	√				
Cllr Ayas Miah	√	Present	Present	Present	Present
Cllr Clare Harrisson	√	Present	Present	Present	Present
Cllr Harun Miah	√		Present		
Cllr John Pierce	√	Present			
Cllr Mohammed Mufti Miah	√			Present	Present
John Gray (Non-voting)	x	Present	Present	Present	Present
Frank West (Non-voting)	x	Present	Present	Present	
Officers					
Bola Tobun	x	Present	Present	Present	Present
Kevin Miles	x	Present	Present	Present	Present
Anant Dodia	x	Present	Present	Present	Present
Chris Holme	x	Present	Present	Present	Present
Graham White	x	Present	Present		
Ngozi Adedeji	x		Present	Present	Present
Nishaat Ismail	x	Present	Present	Present	Present
Antonella Burgio	x	Present	Present	Present	
David Knight	x				Present
Public					
Raymond Haines	x		Present		
Matt Woodman (Hymans)	x	Present			

Training was provided to the Committee with a time slot at the Committee meetings. The topics covered in the training programme for the Committee in 2014/15 were provided in line with the Knowledge and Skills Framework to help ensure that the Committee are able to achieve high levels of the specialist knowledge required of them. The attendance at the training session is the same as set out in the table above for Pensions Committee attendance

Topics covered during the financial year were:

- General pensions framework
- Scheme-specific legislation for LGPS
- Constitutional framework for pension fund committees within administering authorities Pension scheme governance
- Valuations, funding strategy and inter-valuation monitoring
- Investment strategy – Asset Allocation, Fixed income
- Monitoring of investment performance

Knowledge and Skills Policy Statement

CIPFA Code of Practice on Public Sector Pensions – Finance Knowledge and Skills

The adoption of the CIPFA "Pensions Finance, knowledge and skills framework, Technical Guidance for Elected Representatives and Non-executives in the Public Sector" (2010) provides the basis for a training and development programme for the Pensions Committee based on the latest national guidance.
London Borough of Tower Hamlets Pension Fund adopts the key recommendations of the Code of Practice on Public Sector Pensions Finance Knowledge and Skills.

London Borough of Tower Hamlets recognises that effective financial administration, scheme governance and decision-making can only be achieved where those involved have the requisite knowledge and skills.

London Borough of Tower Hamlets will ensure that it has formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective acquisition and retention of the relevant public sector pension scheme finance knowledge and skills for those in the organisation responsible for financial administration, scheme governance and decision-making.

These policies and practices will be guided by reference to a comprehensive framework of knowledge and skills requirements such as that set down in the CIPFA Pensions Finance Knowledge and Skills Frameworks.

London Borough of Tower Hamlets will report on an annual basis how these policies have been put into practice throughout the financial year.

London Borough of Tower Hamlets has delegated responsibility for the implementation of the requirements of the CIPFA Code of Practice to the Corporate Director of Resources, who will act in accordance with the organisation's policy statement, and where they are a CIPFA member with CIPFA Standards of Professional Practice.

London Borough of Tower Hamlets recognises the importance of ensuring that it has the necessary resources to discharge its pension administration responsibilities and that all staff and members charged with the financial administration, governance and decision-making with regard to the pension scheme are fully equipped with the knowledge and skills to discharge the duties and responsibilities allocated to them.

London Borough of Tower Hamlets therefore seeks to utilise individuals who are both capable and experienced and it will provide and/or arrange training for staff and members of the pensions decision making and governance bodies, to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills.

PENSIONS KNOWLEDGE AND SKILLS FRAMEWORK FOR PENSIONS COMMITTEE MEMBERS

Core technical areas and areas of knowledge

Legislative and governance framework
- General pensions framework
- Scheme-specific legislation for LGPS
- Pensions regulators and advisors
- Constitutional framework for pension fund committees within administering authorities
- Pension scheme governance

Accounting and auditing standards
- Accounts and Audit regulations
- Role of internal and external audit

Procurement of financial services and relationship management
- Procurement requirements of UK and EU legislation
- Supplier risk management

Investment performance and risk management
- Monitoring of investment performance
- Performance of advisors
- Performance of the Pensions Committee
- Performance of support services

Financial markets and investment products
- Investment strategy
- Financial markets
- Regulatory requirements regarding investment products

Actuarial methods, standards and practices
- Valuations, funding strategy and inter-valuation monitoring
- Ill-health and early retirement
- Admitted bodies
- Outsourcing and bulk transfers

Risk Management

Risk management forms a key part of Pension Fund Governance and is part of the ongoing decision making process for the Committee. The benefits of successful risk management are clear for the Fund; improved financial performance, better delivery of services, and improved Fund governance and compliance.

There are four general approaches to treating risk: avoid, reduce, transfer or accept.

- Avoidance of risk – not undertaking the activity that is likely to trigger the risk
- Reducing the risk – controlling the likelihood of the risk occurring, or controlling the impact of the consequences if the risk does occur.
- Transferring the risk – handing the risk on elsewhere, either totally or in part – e.g. through insurance.
- Accepting the risk – acknowledging that the ability to take effective action against some risks may be limited or that the cost of taking action may be disproportionate to the potential benefits gained.

The types of risk that the Fund is exposed to fall into the following broad categories:

- Financial – These relate to investment related risks including market, currency, credit and interest rate risks – these are outlined in detail in the Statement of Accounts.
- Strategic – Failure to meet strategic objectives such as performance targets, Funding Strategy Statement objectives, etc.
- Regulatory – Regulatory changes impacting on the Fund, or failure to comply with legislation or meet statutory deadlines.
- Reputational – Poor service damaging the reputation of the Fund.
- Operational – Data maintenance, service delivery targets.
- Contractual – 3rd party providers, failure to deliver, effective management of contracts.
- Communication – Failure to keep all stakeholders notified of things that affect them, be they employers, scheme members or contractors.

The Funding Strategy Statement (appendix 3) explains the fund's key risks and how they are identified, mitigated, managed and reviewed.

The Fund's investment managers and custodian are audited separately and at different times. The Council receives audited assurance reports AAF01/06, SSAE16 and ISAE3402 from their independent auditors. Any exceptions highlighted by their auditors are evaluated by officers.

The council is the primary employer in the Fund and the risks of late payment of contributions are with admitted and scheduled bodies who are treated by the Pension Regulations as part of the Council for pension purposes. All contributions received from external payroll providers are reconciled monthly.

Investment and Performance Review

Major investment markets delivered positive returns over the period as a whole. This outcome could be attributed to several factors including increased investor confidence, the improved economic backdrop, and the continuation of loose monetary policy in many developed countries.

Although there were several geopolitical flashpoints around the world, notably in the Middle East and Ukraine, and these situations created uncertainty in terms of global security, they had a limited impact on investment markets. However, the sharp fall in the oil price in the second half of 2014 and extreme weakness in the Russian currency during December 2014 were of greater concern to investors and caused a rise in volatility in financial markets. However, the falling oil price was beneficial for some countries, businesses such as airlines and cruise companies, and consumers more generally.

The main contributors to the positive performance of **Baillie Gifford Diversified Growth Fund** included economic risk assets such as listed equities, emerging market bonds and property. Allocations to asset classes such as absolute return, structured finance and infrastructure were also helpful. No single asset class detracted from returns over the 12-month period under review. The Fund maintained a broadly diversified portfolio with a substantial allocation to more defensive assets such as investment grade bonds, structured finance and cash.

Looking back at the last twelve months for **Ruffer portfolio**, not only have their equities made useful gains, increasingly led by Japan. The main contributors to the performance in the year were their long-dated inflation-linked bonds. With little inflation expectation built into them, they benefitted from the continued fall in global bonds yields, both real and nominal. Continued low inflation readings, collapsing commodity prices, further Japanese QE and hopes of full-blown Eurozone QE all drove global yields lower, thus raising bond prices. The quest for duration drove the 2068 UK index-linked bond up over 50% during the twelve month period.

The benchmark return for the 12 month period to 31 March 2015 was 15.0% and the assets invested with **GMO** lagged this with a return of 13.6% (net of fees).

These strong absolute equity returns mask a significant amount of volatility during the period. Market sentiment was confused by the positives of continuing low interest rates and quantitative easing offsetting concerns over plunging oil prices, anaemic global growth and significant geo-political tensions (including ISIS in the Middle East and the Russia/Ukraine conflict). From a regional perspective, there was a very large dispersion of returns. Japan led the way with an impressive 27.1% return bolstered by the continuation of 'Abenomics' - Prime Minister Abe's policy based upon fiscal stimulus, monetary easing and much needed structural reforms. The other strong performer was North America, with a 25.1% return, though much of this can be attributed to the strong US dollar, which appreciated by more than 10% against the pound over the period.

Schroder (Property) – The portfolio returned 16.0% over the year; lagged the benchmark of 16.6% resulting in underperformance of the benchmark by 0.6%. The UK investments assets (97% of the portfolio's value) outperformed by +1.4% over the past twelve months, over the three years and 0.5% over the five years. The Continental European Fund (3% of the portfolio) produced a negative return this year (-8.1%), and still remains a drag to total returns in aggregate over the past five years in particular.

The twelve months to March 2015 was a good year for UK commercial real estate, with the market delivering unleveraged total returns of 18.3% (source: IPD monthly digest). Most of this performance has been driven by a favourable fall in property yields, as investors seek income. Looking ahead to the second half of 2015, we expect that total returns will remain in double figures, but that rental growth will make a larger contribution to performance. The recovery in the economy, combined with low levels of development, means that the balance between demand and supply is now swinging in favour of landlords and we anticipate that rental growth will accelerate as a result.

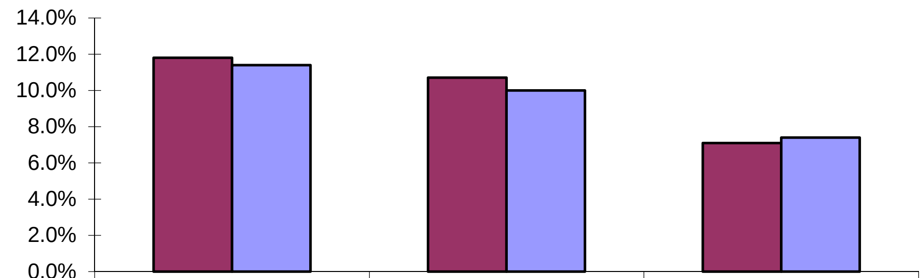
The **Investec** Bond portfolio underperformed the target set over the 12 months period returning 1.9% versus the 2% plus Overnight GBP LIBOR Rate of 2.6%. The investments in currencies made the largest contribution to the returns over the period. These gains were largely down to the manager longer-term positions, which are designed to benefit from macroeconomic trends, such as the position in the US dollar. With the exception of early 2015, the US economy has been growing robustly – and this has translated into dollar strength. Elsewhere, the portfolio's holdings in emerging market bonds made a small positive contribution to returns over the period. These 12 months were a challenging time for emerging market economies, and their bond markets in particular – returns were patchy and prices had a tendency to fluctuate quite wildly. But falling inflation in the second half of 2014 – which boosted bonds – allowed for short periods of positive performance. More negatively, the portfolio's credit positioning detracted from relative returns given the manager's defensive positioning at a time when credit markets ended the period higher.

Investment Performance of the Fund

The Council's Statement of Investment Principles sets the Fund's investment objective as "to follow an investment strategy which will achieve an appropriate balance between maximising the long-term return on investments and minimising short-term volatility and risk".

In 2014/15 the fund had a good performance achieving a return on its investment portfolio of 11.8%, outperforming the benchmark of 11.4%. The three year return also outperformed the benchmark with the fund returning 10.7% against a benchmark of 10.0%. The return for 10 year continued to lag the benchmark by 0.3%.

Fund Performance (One, Three and 10 Years)



	One Year	3 Years	10 Years
Fund	11.8%	10.7%	7.1%
Benchmark	11.4%	10.0%	7.4%
Rank	73	59	84

Fund Management Activity

The continued recovery in the equity markets and strong returns from the fund's global equity managers and absolute return funds was a major contributor to the outperformance.

During the year the decision was taken to rebalance the fund to ensure the strategic allocation was in line with target and to reduce the overweight position in equities. This resulted in 2% of the fund's assets from GMO being divested and the proceeds held as cash and being managed internally.

The fund continues to participate in the Collective Investment Vehicle (CIV) and during the year made a further contribution of £50k to the set up and initial running costs of the scheme.

The fund received a positive cash flow from dealings with members of £5.2m and the 2015/16 cash flow forecast predicts that it will continue to be positive.

Asset Allocation

The asset allocation within the portfolio is in line with or within the agreed tolerance of the benchmark asset allocation as at 31 March 2015 as set out below. The Committee has agreed to take corrective action and rebalance asset allocation where bond to equity allocation moves by +/-5%.

Analysis of Asset Allocation

Asset Class	Benchmark	Fund Position	Variance
UK Equities	24.0%	23.5%	-0.5%
Global Equities	37.0%	39.1%	2.1%
UK Index Linked	3.0%	5.2%	2.2%
Pooled Bonds	14.0%	8.7%	-5.3%
Property	12.0%	10.5%	-1.5%
Alternatives	10.0%	8.9%	-1.1%
Cash	0.0%	4.2%	4.2%

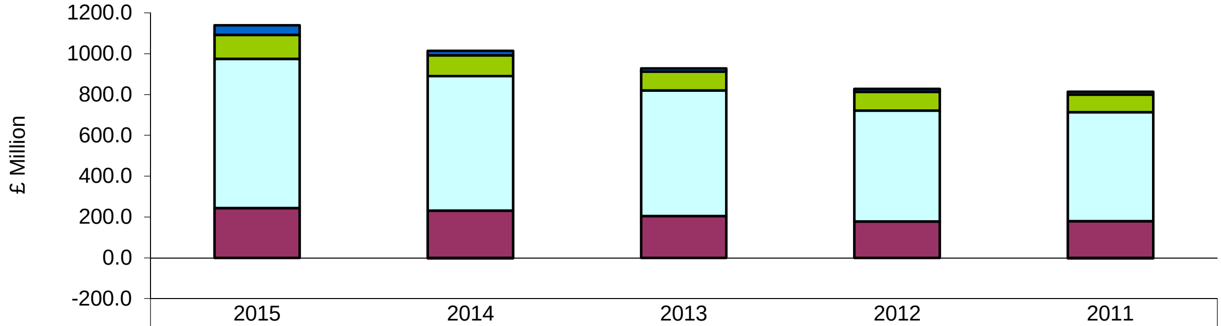
The fund remains close to its strategic allocation although the bond mandate is slightly underweight it is offset to an extent by the overweight position of index-linked gilts.

All investment activity is regulated by the Fund's Statement of Investment Principles which together with the Myners Compliance Statement are set out in Appendix 2.

Financial Accounts

During the financial year 2014/15 the value of the Fund rose by £125.3m to £1,138.2m, an increase of 12.4%. This is principally attributable to the performance of the financial markets in which the Fund held its investments.

ANALYSIS OF ASSET CLASS

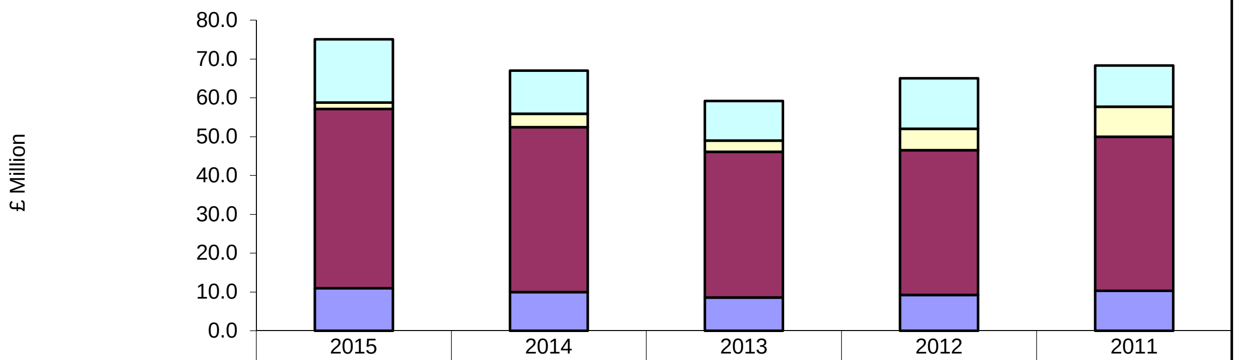


	2015	2014	2013	2012	2011
Cash	47.2	21.6	15.1	14.2	13.5
Derivatives	0	-0.4	0.5	0.2	-0.4
Property Units	116.9	102.1	92.1	92	86.2
Unit Trusts	730	658.7	615.2	542.9	532.8
Equities	244.3	231.0	203.9	177.9	180.1

Fund Income

There was a significant increase in the amount of income received by the Fund in 2014/15 compared to 2013/14.

Fund Income Analysis



	2015	2014	2013	2012	2011
Investment Income	16.3	11.1	10.2	13	10.6
Transfer Values	1.7	3.5	2.9	5.5	7.7
Council Related Contributions	46.1	42.4	37.5	37.3	39.7
Employees Contributions	11.0	10.0	8.6	9.2	10.3

Investment income increased over the year by £5.2m (46.8%) mainly due to an increase in dividend income. Transfer Values received (amounts paid over when a fund member transfers their benefits from one fund to another) decreased by £1.8m (51.4%). It is not possible to predict the value of transfer value payments as they are dependent on an individual's length of service and salary and as such may vary significantly. Employee contributions rose by £1.0m (10.0%), the increase being attributable to the new CARE scheme which sees contributions deducted from all additional pay and also to the increase in the banding rate which sees higher rates of pay subject to a contribution rate of up to 12.5%.

Employer contributions went up by £3.7m (8.7%) due to an increase in the employer's deficit funding payment of £2m.

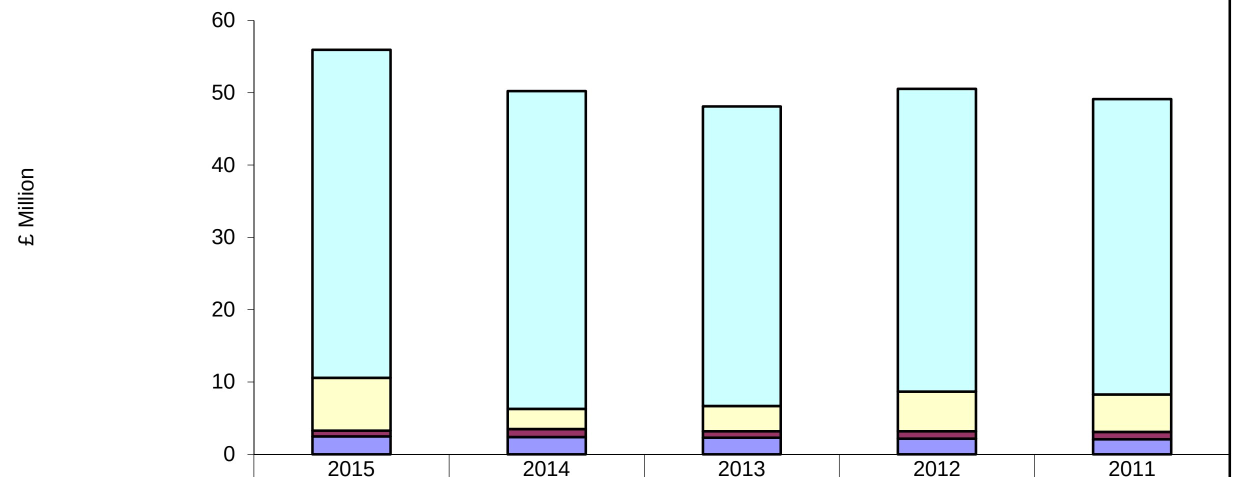
Fund Income Variance Analysis

Type of Income	2015 £m	2014 £m	Variance %
Employees Contributions	11	10	10.0%
Council Related Contributions	46.1	42.4	8.7%
Transfer Values	1.7	3.5	-51.4%
Investment Income	16.3	11.1	46.8%
Total Fund Income	**75.1**	**67**	**12.1%**

Fund Expenditure

In 2014/15 the overall Fund expenditure increased by £5.7m (11.4%). The major contributor to the increase was the rise in transfers out of £4.5m (160.7%). There was a modest increase in investment management costs of £0.1m (4.2%) while administration costs fell by £0.3m (27.3%). Benefits payable rose by £1.4m (3.2%).

Fund Expenditure Analysis



	2015	2014	2013	2012	2011
Benefits Payable	45.3	43.9	41.4	41.8	40.8
Transfer Values	7.3	2.8	3.5	5.5	5.2
Administration	0.8	1.1	0.9	1.0	1.0
Investment Management	2.5	2.4	2.3	2.2	2.1

The increase in transfers out is principally due to the higher value of transfer payments being made, although the number of staff leaving had increased but not significantly. The substantial reduction in administration costs of £300k (27.3%) shows a return to normal following the additional costs charged in the previous year to accommodate the purchase of the new Altair pension administration system and also the charge for triennial valuation fees. The investment management fees which are performance based have risen in line with the increase in the market value of the funds held.

Fund Expenditure Variance Analysis

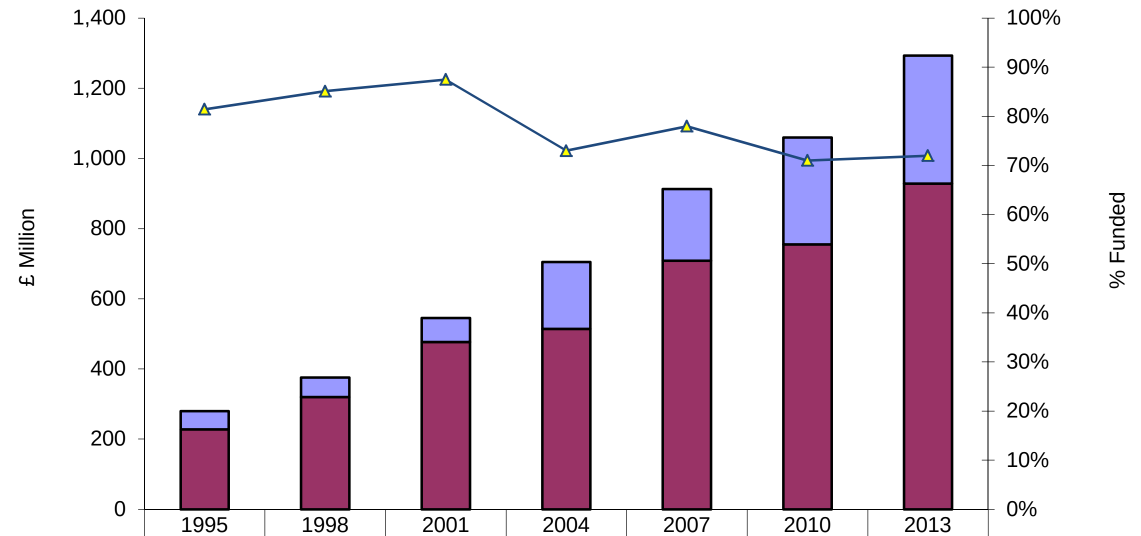
Type of Expenditure	2015 £m	2014 £m	Variance £m	Variance %
Investment Management	2.5	2.4	0.1	4.2%
Administration	0.8	1.1	-0.3	-27.3%
Transfer Values	7.3	2.8	4.5	160.7%
Benefits Payable	45.3	43.9	1.4	3.2%
Total Fund Expenditure	55.9	50.2	5.7	11.4%

Funding Level

The Council is required to value the Pension Fund every three years.

The fund was valued by the consultant actuary Hymans Robertson LLP as at the 31st March 2013. The Actuary calculated that the Pension Fund is 71.8% funded and has a deficit of £365m.

Movement in Funding Level



	1995	1998	2001	2004	2007	2010	2013
Deficit	52.0	56.0	68.1	191.0	204.8	305.0	365.0
Assets	228.0	320.0	477.2	514.0	708.4	755.0	928.0
Funding	81%	85%	88%	73%	78%	71%	72%

The funding position increased by 0.8% between the previous revaluation in 2010 and the 2013 valuation. This is principally attributable to an increase in the market value of assets with a reduction in ill-health retirements and slower rate of increase in salaries having a positive effect too. The deficit increase of £60m was brought about by an increase in the value of the Fund's liabilities owing to the decrease in the real gilt yield.

On the recommendation of the Actuary, the Council adopted a strategy to recover the deficit over a 20-year period. This will involve the Council paying a lump sum of £18.5m in 2014/15 rising to £20.5m and £22m in 2015/16 and 2016/17 respectively, into the pension fund specifically to recover the deficit.

Although the increase in deficit has necessitated an increase in the overall monetary amounts payable by the Council, the contribution rate element of this has been held at 15.8% of employee pay.

It should be emphasised that the deficit does not affect employees' pension entitlement. The Council is under a statutory obligation to provide sufficient funds to pay pensions and has adopted a strategy recommended by the Actuary to achieve full funding in twenty years. Councils can take a long-term perspective because of their financial stability and statutory backing. It should be recognised that the position is not unique to the Tower Hamlets Fund. All Pension Funds in both the public and private sectors have been subject to declining investment returns and increasing life expectancy, which has resulted in rising deficits in many cases. The 2013 valuation exercise has shown the fund to be gradually maturing as the proportion of employee members has fallen whilst the deferred and pensioner numbers have risen.

The Scheme Details

The London Borough of Tower Hamlets Pension Fund is part of the Local Government Pension Scheme (LGPS) and is governed by Statute. The main regulations governing the operation of the scheme during the year were the Superannuation Act 1972 and the Local Government Pension Scheme Regulations 2013. The Local Government Pension Scheme Regulations 2013 introduced the new 2014 LGPS which amongst other things changed the benefits structure from a final salary to career average revalued earning (CARE) scheme. In addition the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 covers the investment aspects of the funds.

The London Borough of Tower Hamlets is the Administering Authority for the Pension Fund and pensions and entitlement to benefits are fully protected in law. Membership of the Scheme is open to all employees of the Council including school employees with the exception of teachers (who have their own pension scheme). Other employers are admitted to the Pension Fund and depending on their status; their employees may also be able to participate in the LGPS. Employee contributions are determined by central government and are between 5.5% and 12.5% of pensionable pay. Employer rates are set by the Fund actuary every 3 years following a valuation of the assets and liabilities of the Fund, with the next valuation due to take place as at 31 March 2016.

The conditions of the Local Government Pension Scheme (LGPS) Regulations made it clear that the benefits that are payable to Scheme members and as such the benefits are guaranteed for those members and therefore members are not reliant on investment performance for their pension benefits. The contributions payable by Scheme members are also defined in the Regulations. Employing Authorities are required to pay contributions into the Scheme in order to meet the cost of funding employee benefits and as such, are required to meet any shortfall in funding the pension liabilities of Scheme members.

The Pension Scheme as applying during the financial year 2014/15 was a defined benefit career average revalued earnings scheme which aligns LGPS retirement age with an individual's state pension age. The key benefits of the scheme are outlined below:

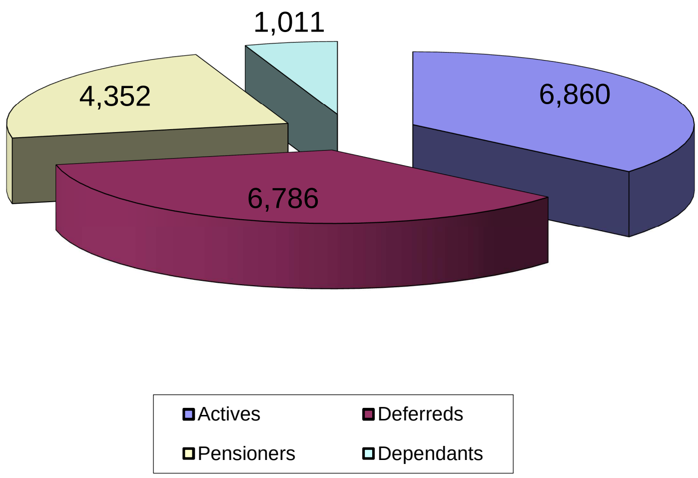
- Pension benefits based on a 1/49th accrual basis for each year of pensionable service with benefits calculated on the career average pay revalued annually in line with inflation.
- Pre-2014 benefits guaranteed with a final salary link for any benefits earned prior to 1 April 2014.
- Option to pay 50% of the contribution rate to accrue 50% of the benefits.
- Option to convert some pension to lump sum on retirement on a 1:12 ratio.
- Life assurance cover 3x member final pay applicable from the day of joining scheme.
- Pensions for dependents: - spouses, civil partners and eligible co-habiting partners and eligible children.
- An entitlement to have pension paid early on medical grounds.
- Pensions increase annually in line with the cost of living.

It should be noted that the foregoing is not an exhaustive list and that certain conditions have to be met for an individual to be entitled to the benefits outlined.

The foregoing benefit structure came into effect on 1 April 2014 and saw the start of significant changes to the public sector pension schemes, with most other schemes introducing their changes a year later on 1 April 2015. The previous LGPS introduced in 2008 was a defined benefit final salary scheme and was in operation until 31 March 2014, although it should be recognised that a large number of scheme members will have benefits accrued under both schemes and indeed some under the pre-2008 scheme. The key benefits under the 2008 scheme are outlined below:

- A guaranteed pension based on final pay and length of time in the scheme and an accrual rate of 1/60th per annum.
- Tax free lump sum on benefit accumulated prior to 1 April 2008 and option to convert some of the pension into tax free lump sum on post 1 April 2008 service.
- Life assurance cover 3x member final pay applicable from the day of joining scheme.
- Pensions for spouses/civil and co-habiting partners and children.
- An entitlement to have pension paid early on medical grounds.
- Pensions increase annually in line with the CPI.

Scheme Membership
The Fund currently has a membership of 19,009 comprising the following categories as set out in the below chart. Membership to the scheme is automatic for full and part-time employee unless they opt out.



The total pension fund membership has increased by 1.8% between 2013/14 and 2014/15. The number of actives members (those currently contributing to the fund) has increased by 68 (1.0%). The deferred membership category (members who have contributed in the past but who have not yet become entitled to their benefits) has increased by 122 (1.8%) and pensioner members by 106 (2.5%). The dependants' category saw an increase of 36 (3.5%).

The table below sets out the movement in membership number between the different categories in 2013/14 and 2014/15.

Movement in Fund Membership

Membership Type	31-Mar-15	31-Mar-14	Variance No.	Variance
Actives	6,860	6,792	68	1.0%
Deferreds	6,786	6,664	122	1.8%
Pensioners	4,352	4,246	106	2.5%
Dependants	1011	975	36	3.7%
Total	19,009	18,677	332	1.8%

The membership of the fund over the last five years is as set out below.

Membership Type	31-Mar-15	31-Mar-14	30-Mar-13	30-Mar-12	31-Mar-11
Actives	6,860	6,792	5,298	5,252	5,686
Deferreds	6,786	6,664	6,292	6,060	5,601
Pensioners	4,352	4,246	4,148	4,064	3,914
Dependants	1011	975	979	940	931
Total	19,009	18,677	16,717	16,316	16,132

Fund Employers

London Borough of Tower Hamlets is the administering authority for the fund. The scheme is open to all council employees and scheduled bodies. Admitted bodies require the agreement of the administering authority to participate in the fund. The scheduled and admitted bodies participating in the fund are set out below.

Scheduled Bodies

- Bethnal Green Academy
- Canary Wharf College
- Culloden Primary School
- London Enterprise Academy
- Old Ford Primary School
- Sir William Burrough School
- Solebay Academy
- St Pauls Way Communuity School
- Tower Hamlets Homes Ltd

Admitted Bodies

- Agilisys
- Capita
- Circle Anglia Ltd
- East End Homes
- Ecovert FM Ltd
- Gateway Housing Association
- Greenwich Leisure Ltd
- Look Ahead Housing and Care*
- One Housing Group
- Redbridge Community Housing Ltd

- Swan Housing Association
- Tower Hamlets Community Housing

*Look Ahead Housing and Care ceased to be an admitted body of the fund in September 2014

Contributions to the Fund
Employees pay contributions based on the level of pay they receive with rates being set between 5.5% to 12.5% of pensionable pay. The employers contribution rate used during the financial year ranged from 15.9% to 41.4% of pensionable pay.

The following table shows the contributing employers and the contributions received from each during the year.

Contributing Employers	Active Members	Contributions from Members £	Contributions from Employers £
London Borough of Tower Hamlets	6,155	9,730,977	22,356,297
Agilisys	41	111,437	265,384
Bethnal Green Academy	20	45,343	132,334
Canary Wharf College	6	7,599	19,823
Capita	7	9,418	28,056
Circle Anglia Ltd	3	4,600	83,794
Culloden Academy	18	17,765	92,728
East End Homes	35	106,536	445,698
Ecovert FM Ltd	13	3,690	14,053
Gateway Housing Association	1	1,769	32,967
Greenwich Leisure Limited	7	18,496	46,629
London Enterprise Academy	1	2,110	4,924
Old Ford Academy	34	20,109	111,626
One Housing Group	9	14,832	93,802
Redbridge Community Housing Ltd	2	3,718	10,125
Sir William Burrough School	5	12,291	44,908
Solebay Academy	1	861	4,797
St.Pauls Way Community School	17	61,490	156,584
Swan Housing Association	1	1,922	17,749
Tower Hamlets Community Housing	16	56,207	241,218
Tower Hamlets Homes Limited	342	799,836	2,651,086
Total	6,734	11,031,007	26,854,581

* The Council contributed an additional £18.5m in respect of deficit funding

The full accounts are as set out in Appendix 1.

The Council is required to publish a number of statements relating to the operation of the fund. The statements and the associated reports are as set out in the following appendices.

Appendix 2 Statement of Investment Principles
Appendix 3 Funding Strategy Statement
Appendix 4 Communications Strategy Statement
Appendix 5 Governance Compliance Statement
For further information on the Local Government Pension Scheme and your entitlement, please contact Anant Dodia at anant.dodia@towerhamlets.gov.uk or by telephoning 020 7364 4248.

Statement from the Actuary

An actuarial valuation of the London Borough of Tower Hamlets Pension Fund was carried out by Hymans Robertson LLP as at 31 March 2013 to determine the contribution rates that should be paid into the Fund by the employing authorities as from 1 April 2014 to 31 March 2017 in order to maintain the solvency of the Fund.

On the basis of the assumptions adopted, the valuation revealed that the value of the Fund's assets represented 71.8% of the Funding Target and the estimated deficit on the Fund at the valuation date was £365m. The Actuary has determined that the deficit can be recovered over a period of 20 years and the agreed monetary contribution to recover the deficit for the term of the revaluation is £18.5m (2014/15) rising to £20.5m (2015/16) and £22m (2016/17).

The Common Rate of Contribution payable by each employing authority under Regulation 77 for the period 1 April 2014 to 31 March 2017 is 35.5% of pensionable pay.

Individual Adjustments are required under Regulation 77 for the period 1 April 2014 to 31 March 2017 resulting in a Minimum Total Contribution Rates expressed as a percentage of pensionable pay are as set out below:

		Minimum Contribution for the year ending				
Employer Name as per 31 March 2013	Year ending 31 March 2015	Additional Monetary Deficit Payment £	Year ending 31 March 2016	Additional Monetary Deficit Payment £	Year ending 31 March 2017	Additional Monetary Deficit Payment £
London Borough of Tower Hamlets	15.8%	18.5m	15.8%	20.5m	15.8%	22m
Tower Hamlets Community Housing Limited	34.7%		36.1%		37.6%	
Redbridge Community Housing Limited	17.7%		17.7%		17.7%	
East End Homes Limited	31.1%		32.3%		33.6%	
Greenwich Leisure Limited	17.7%		17.7%		17.7%	
Swan Housing Association Limited	26.2%	10k	26.2%	10k	26.2%	11k
Gateway Housing Association (Bethnal Green & Victoria Park)	25.6%	26k	25.6%	27k	25.6%	28k
One Housing Group (Toynbee Island Homes)	41.4%		41.4%		41.4%	
Circle Anglia Limited	27.7%		27.7%		27.7%	
Tower Hamlets Homes	23.1%		23.1%		23.1%	
Look Ahead Housing & Care Limited	19.9%		19.9%		19.9%	
Ecovert FM Limited	22.5%		22.5%		22.5%	
Bethnal Green Academy	20.6%	141k	20.6%	146k	20.6%	152k
Sir William Burrough School	25.3%		23.6%		21.8%	
St Pauls Way Community School	16.7%		17.8%		18.9%	
Capita	19.6%		19.6%		19.6%	
Canary Wharf College	15.9%		15.9%		15.9%	
Agilisys	16.8%		16.8%		16.8%	

In addition to the certified contribution rates, payments to cover the additional liabilites arising from early retirements (other than ill-health) will be made to the Fund by the employers.

The results of the triennial valuation depend on the actuarial assumptions made about the future of the Fund. The effect on the valuation of the Fund of changes to the main assumptions are set out in the table below.

Sensitivity of valuation results to changes in asumptions

		Impact	
Assumption	Change	Deficit (£m)	Future service rate (% of pay)
Discount rate	Increases by 0.5%	Falls by £112m	Falls by 3%
Salary increases	Increases by 0.5%	Rises by £31m	Rises by 2%
Price inflation/pension increases	Increases by 0.5%	Rises by £92m	Rises by 2%
Life expectancy	Increases by 1 year	Rises by £39m	Rises by 1%

This is not an exhaustive list of assumptions but those that are likely to have the biggest impact. The effect of changes are shown in isolation and it is possible that the Fund could experience changes to more than one assumption simultaneously.

The next triennial valuation of the Fund is due as at 31 March 2016. The contribution rates payable by the individual employers will be revised with effect from 1 April 2017.

Statement of Responsibilities

The London Borough of Tower Hamlets as Administering Authority of the London Borough of Tower Hamlets Pension Fund is required to:

- Make arrangements for the proper administration of its financial affairs and to secure that one of its Officers has the responsibility for the administration of those affairs. In this council, that officer is the Acting Corporate Director of Resources;
- Manage its affairs to secure economic, efficient and effective use of resources and safeguard its assets;
- Approve the Statement of Accounts

Responsibilities of the Acting Corporate Director of Resources

The Acting Corporate Director of Resources is responsible for the preparation of the Pension Fund Statement of Accounts in accordance with proper practices as set out in CIPFA's Code of Practice on Local Authority Accounting in the United Kingdom ("the Code of Practice").

In preparing this Statement of Accounts, the Acting Corporate Director of Resources has:

- Selected suitable accounting policies and then applied them consistently
- Made judgements and estimates that were reasonable and prudent; and
- Complied with the Code of Practice, except where otherwise stated.

The Acting Corporate Director of Resources has;

- Kept proper accounting records which were up to date; and
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

Responsible Financial Officer's Certificate:

I certify that the Accounts set out on pages 19 to 33 have been prepared in accordance with proper practices and that they give a true and fair view of the financial transactions of the Pension Fund during the year ended 31st March 2015 and the amount and disposition of the Fund's assets and liabilities as at 31 March 2015.

Chris Holme
Acting Corporate Director of Resources

Independent auditor's report to the members of the London Borough of Tower Hamlets on the pension fund financial statements published with the Pension Fund Annual Report

for and on behalf of KPMG LLP, Appointed Auditor

Chartered Accountants

15 Canada Square, London, E14 5GL

28 November 2014

TOWER HAMLETS

The London Borough of Tower Hamlets Pension Fund

Appendix 1

Statement of Accounts 2014/15

PENSION FUND ACCOUNTS

PENSION FUND ACCOUNT	Note	2013/14 £'000	2014/15 £'000
DEALINGS WITH MEMBERS, EMPLOYERS AND OTHERS DIRECTLY INVOLVED IN THE SCHEME			
Contributions			
From employers	3	42,401	46,135
From members	3	9,982	11,031
Transfers in			
Transfers in from other pension funds	4	3,527	1,719
Benefits			
Pensions	4	(35,681)	(37,265)
Lump sum benefits	4	(8,178)	(8,055)
Payments to and on account of leavers			
Refunds of contributions		(3)	(125)
State scheme premiums		(3)	(132)
Transfers out to other pension funds		(2,778)	(7,263)
Administrative expenses	13	(1,087)	(803)
NET ADDITIONS FROM DEALINGS WITH MEMBERS		**8,180**	**5,242**

RETURN ON INVESTMENTS		2013/14 £'000	2014/15 £'000
Investment income	11	11,540	16,581
Taxes on Income		(410)	(329)
Change in market value of investments			
Realised		22,195	23,292
Unrealised	10	46,918	82,933
Investment management expenses	13	(2,364)	(2,450)
NET RETURN ON INVESTMENTS		**77,879**	**120,027**
Net increase in the Fund during the year		86,059	125,269
Add: Opening net assets of the scheme		926,871	1,012,930
CLOSING NET ASSETS OF THE SCHEME		**1,012,930**	**1,138,199**

NET ASSETS STATEMENT AS AT 31ST MARCH		2014 £'000	2015 £'000
Investments Assets			
Equities		230,998	244,335
Pooled Investment Vehicles			
Unit Trusts		566,768	628,744
Property		102,073	116,945
Other		91,918	101,303
Derivative Contracts			
Forward Foreign Exchange Contracts		238	0
		991,995	1,091,327
Cash deposits	6	5,292	5,414
Other investment balances	5	817	978
Investments Liabilities			
Forward Foreign Exchange Contracts	10	(647)	0
Other investment balances	5	0	(223)
Current Assets	5	16,954	42,154
Current Liabilities	5	(1,481)	(1,451)
TOTAL NET ASSETS		**1,012,930**	**1,138,199**

NOTES TO THE PENSION FUND ACCOUNTS

1. INTRODUCTION

The Council is the administering authority for the Pension Fund and has executive responsibility for it. The Council delegates its responsibility for administering the Fund to the Pensions Committee which is responsible for considering all pension matters and discharging the obligations and duties of the Council under the Superannuation Act 1972 and other statutes relating to investment issues. The Committee meets quarterly to determine investment policy objectives, appoint investment managers, monitor investment performance and make representations to the Government on any proposed changes to the Local Government Pension Scheme. The Committee is required to obtain proper advice on the investment strategy of the Fund for which it has established an Investment Panel which includes professional investment advisors. The Panel meets quarterly to determine the general investment strategy, monitor the performance of the Fund and individual managers and consider technical reports on investment issues. The Fund employs eight specialist investment managers with mandates corresponding to the principal asset classes.

The day to day administration of the Fund and the operation of the management arrangements and administration of the investment portfolio is delegated to the Corporate Director of Resources.

The Fund is operated as a funded, defined benefits scheme which provides for the payment of benefits to former employees of the London Borough of Tower Hamlets and those of bodies admitted to the Fund. These individuals are referred to as "members". The benefits include not only retirement pensions, but also widows' pensions, death grants and lump sum payments in certain circumstances. The Fund is financed by contributions from members, employers and from interest and dividend receipts and gains on the Fund's investments.

The objective of the Pension Fund's financial statements is to provide information about the financial position, performance and financial adaptability of the Fund. They show the results of the stewardship of management - that is the accountability of management for the resources entrusted to it - and the disposition of its assets at the period end.

2. ACCOUNTING POLICIES

(a) **Accounts**

The accounts summarise the transactions and net assets of the Pension Fund and comply in all material respects with Chapter 2 ("Recommended Accounting Practice") of the Statement of Recommended Practice (Financial Reports of Pensions Schemes) 2007 and the Code of Practice on Local Authority Accounting issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

The Fund is administered in accordance with the Local Governement Pension Scheme Regulations 2013 (as amended) and the Local Governemnt Pension Scheme (Management and Investment of Funds) Regulations 2009.

(b) **Basis of preparation**

Except where otherwise stated, the accounts have been prepared on an accruals basis, that is income and expenditure are recognised as earned or incurred, not as received or paid.

(c) The financial statements of the Fund do not take account of liabilities to pay pensions and other benefits after 31st March 2015. The actuarial present value of promised retirement benefits, valued on an IAS19 basis is disclosed in note 12 of the Accounts as permitted under IAS26.

Fund Account - Revenue Recognition

Contribution Income

Normal contributions, both from the members and from the employer, are accounted for on an accruals basis at the percentage rate recommended by the actuary in the payroll period to which it relates. Any amount due in the year but unpaid will be classified as a current asset.

Employer deficit contributions are accounted for in accordance with the agreement under which they are paid.

(d) **Investments**

Investments are shown in the Net Assets Statement at market value on the following bases.

(i) Listed securities are shown by reference to bid price at the close of business on 31st March 2015.

(ii) Pooled investment vehicles are valued at bid price, middle market price or single price at close of trading on 31st March 2015.

(iii) Property unit trusts are shown by reference to bid price at close of business on 31st March 2015.

(iv) The Fund does not hold any direct property holdings and therefore does not employ a separate property valuer.

(v) Investments designated in foreign currencies are valued in sterling at the exchange rates ruling on 31st March 2015. Where the Council has entered into a transaction denominated in a foreign currency, the transaction is converted into sterling at the exchange rate applicable on the date the transaction was effective.

(vi) Foreign exchange contracts are recognised in the net asset statement at their fair value. The amounts included in the accounts represent unrealised gains or losses on forward contracts.

(vii) Cash is represented by deposits held with financial institutions repayable on demand without penalty.

(e) **Investment Income**

(i) Interest income is recognised in the Fund account as it accrues.

(ii) Dividend income is recognised in the Fund account on an accruals basis. Any amount not received by the end of the reporting period is disclosed in the net asset statement as a current financial asset.

(iii) Distributions from pooled funds are re-invested and as such are recognised in the change in market value.

(iv) Changes in the net market value of investments held at any time during the year are recognised as income and comprise all realised and unrealised gains/losses.

NOTES TO THE PENSION FUND ACCOUNTS

2 ACCOUNTING POLICIES Cont...

Fund account - expense items

(f) **Management Expenses**

The Code of Practice does not require any breakdown of pension fund administrative expenses. However in the interests of greater transparency, the Council discloses its pension fund management expenses in accordance with the CIPFA guidance on accounting for LGPS management costs.

<u>Administrative Expenses</u>

Staff costs of the pensions of the pensions administration team are charged direct to the fund. Associated management, accommodation and other overheads are apportioned to this activity and charged as expenses to the fund.

<u>Oversight & Governance Costs</u>

Staff costs relating to oversight and governance are charged direct to the fund. Associated management, accommodation and other overheads are apportioned to this activity and charged as expenses to the fund.

<u>Investment Management Expenses</u>

Fund managers' fees are paid in accordance with the terms of each individual management agreement. The fees are based mainly on a percentage of the value of funds under their management and increase or reduce as the value of the investments change.

(g) **Benefits Payable**

Pensions and lump sums payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the net assets statement as current liabilities.

Net assets statement

Financial Assets

(h) Financial assets are included in the net assets statement on a fair value basis as at the reporting date. A financial asset is recognised in the net assets statement on the date the fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of the assets are recognised by the fund.

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

(i) Market-quoted investments

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

(ii) Fixed interest securities

Fixed Interest Securities – are recorded at net market value based on their bid price.

(iii) Unquoted investments

The Forward Foreign Exchange Contracts are stated at fair value which is determined by the gain or loss that would arise at the settlement date from entering into an equal and opposite contract at the reporting date.

2.a CRITICAL JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

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

There is just one item in the authority's net asset statement as at 31st March 2015 for which there which there is a significant risk of material adjustment in the forthcoming financial year.

Pensions Liability - Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund investments. A firm of consulting actuaries is engaged to provide the Council with expert advice about the assumptions to be applied.

The assumptions interact in complex ways. During 2014/15, the Council's actuaries advised that the net pensions liability had increased by £139.9 million to £628.5 million as a result of falling real bond yields.

3. CONTRIBUTIONS

Contributions represent the total amounts receivable from the employing authority in respect of its own contributions and those of its pensionable employees. Employees pay contributions based on the level of pay they receive, with contribution rates set between 5.5% and 12.5% dependent on pensionable pay. The employer's contributions are made at a rate determined by the Fund's actuary necessary to maintain the Fund in a state of solvency, having regard to existing and future liabilities. The Primary Contribution Rates used during the financial year ending the 31 March 2015 range from 15.9% to 41.4% of pensionable pay. The Council paid an agreed additional monetary contribution of £18.5m to recover the deficit. Contributions shown in the revenue statement may be categorised as follows:-

	2013/14 £'000	2014/15 £'000
Members normal contributions		
Council	8,849	9,731
Admitted bodies	222	221
Scheduled body	911	1,079
Total members	**9,982**	**11,031**
Employers		
Normal contributions		
Council	21,210	22,356
Admitted bodies	1,064	1,015
Scheduled bodies	2,505	3,484
Deficit funding contributions		
Council	16,500	18,500
Other contributions		
Council	1,122	780
Total employers	**42,401**	**46,135**
Total contributions	**52,383**	**57,166**

Employer deficit funding contributions are accounted for on the due dates on which they are payable under the schedule of contributions set by the scheme actuary or on receipt if earlier than the due date.

Note: The Council is required to operate an Additional Voluntary Contribution (AVC) scheme for employees. In 2014/15 employees made contributions of £60,530.28 (£26,465.94 in 2013/14) into the AVC Scheme operated by Aviva (Norwich Union) and £9,455.96 to Equitable Life (£6,444.33 in 2013/14). The contributions are not included in the Pension Fund Accounts in accordance with regulation 4(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 but are deducted from salaries and remitted directly to the provider.

4. BENEFITS, REFUNDS OF CONTRIBUTIONS AND TRANSFER VALUES

Benefits payable and refunds of contributions have been brought into the accounts on the basis of all valid claims approved during the year. Benefits are index linked to keep pace with inflation. In April 2011, the method of indexation changed from the retail prices index to the consumer prices index.

Transfers out/in are those sums paid to, or received from, other pension schemes and relate to the period of previous pensionable employment. Transfer values are brought into the accounts on a cash basis. Benefits payable are analysed below.

	2013/14				2014/15			
	Council £'000	Admitted Bodies £'000	Scheduled Bodies £'000	Total £'000	Council £'000	Admitted Bodies £'000	Scheduled Bodies £'000	Total £'000
Pensions	(33,852)	(968)	(861)	(35,681)	(35,259)	(1,126)	(880)	(37,265)
Lump sum retirement benefits	(6,817)	(31)	(288)	(7,136)	(6,027)	(307)	(379)	(6,713)
Lump sum death benefits	(990)	0	(52)	(1,042)	(1,232)	(42)	(68)	(1,342)
Total Pensions and Benefits	**(41,659)**	**(999)**	**(1,201)**	**(43,859)**	**(42,518)**	**(1,475)**	**(1,327)**	**(45,320)**
Transfer Values Received	3,527	0	0	3,527	1,719	0	0	1,719
Transfer Values Paid	(2,778)	0	0	(2,778)	(7,263)	0	0	(7,263)
Total	**(40,910)**	**(999)**	**(1,201)**	**(43,110)**	**(48,062)**	**(1,475)**	**(1,327)**	**(50,864)**

5. DEBTORS AND CREDITORS

Unless otherwise stated, all transactions are accounted for on an accruals basis. The following amounts were debtors or creditors of the Pension Fund as at 31st March.

	2013/14 £'000	2014/15 £'000
Debtors		
Other Investment Balances		
Investment sales	27	8
Dividends receivable	514	583
Tax recoverable	276	387
	817	978
Current Assets		
Contributions due from admitted bodies	86	101
London Borough of Tower Hamlets Pension Fund	62	230
	148	331
Total Debtors	**965**	**1,309**
Creditors		
Other Investment Balances		
Investment purchases	0	223
Current Liabilities		
Unpaid benefits	1,171	1,138
Administrative expenses	263	313
London Borough of Tower Hamlets Pension Fund	47	0
	1,481	1,451
Total Creditors	1,481	1,674
Net Debtors	**(516)**	**(365)**

6. CASH

The deposits held by fund managers can be further analysed as follows:

	2013/14 £'000	2014/15 £'000
Aberdeen: Private Equity Portfolio	10	10
GMO	3,803	2,930
Schroders: Multi Asset Portfolio	14	15
Schroders: Property Portfolio	1,465	2,458
London Borough of Tower Hamlets Pension Fund	16,806	41,823
TOTAL CASH	**22,098**	**47,236**

7. TAXATION

UK Income Tax
Investment income is subject to UK tax which the Fund cannot recover under current tax legislation, except for tax deducted at source from Property unit trusts.

Value Added Tax
As Tower Hamlets Council is the Administering Authority for the Fund, VAT input tax is recoverable on all Fund activities.

Overseas Tax
Taxation agreements exist between the UK and certain other European countries whereby a proportion of the tax deducted locally from investment earnings may be reclaimed. The proportion reclaimable and the timescale involved varies from country to country.

8. STATEMENT OF INVESTMENT PRINCIPLES

The Council, as the Administering Authority of the Pension Fund, is required to prepare, maintain and publish a Statement of Investment Principles (SIP) in accordance with the Local Authority Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 1999. The SIP which is published as part of the Local Government Pensions Scheme Annual Report was approved by the Council's Pensions Committee on 14th November 2014.

9. MEMBERSHIP OF THE FUND

The following table sets out the membership of the Fund at 31st March 2015

	2014	2015
London Borough of Tower Hamlets		
Active Members	6,158	6,249
Pensioners	4,043	4,131
Deferred Pensioners	6,332	6,434
Dependants	959	993
	17,492	**17,807**
Admitted & Scheduled Bodies		
Active Members	634	611
Pensioners	203	221
Deferred Pensioners	332	352
Dependants	16	18
	1,185	**1,202**

The following bodies have been admitted into the Fund:

Admitted Bodies

Agilysis
Capita
Circle Anglia Ltd.
East End Homes
Ecovert FM Ltd.
Gateway Housing Association (formerly Bethnal Green and Victoria Park Housing Association)
Greenwich Leisure Limited
Look Ahead Housing and Care
One Housing Group (formerly Island Homes)
Redbridge Community Housing Ltd.
Swan Housing Association
Tower Hamlets Community Housing

Scheduled Bodies

Bethnal Green Academy
Canary Wharf College
Culloden Primary School
London Enterprise Academy
Old Ford Primary School
Sir William Burrough School
Solebay Academy
St. Pauls Way Community School
Tower Hamlets Homes Limited

10. INVESTMENTS

The Fund employs eight specialist investment managers with mandates corresponding to the principal asset classes.

Manager	**Mandate**
Baillee Gifford Life Ltd.	Global Equity, Diversified Growth
GMO UK Ltd.	Global Equity
Investec Asset Management	Absolute Return Bonds
Legal & General Investment Management	UK Equity, Index Linked Gilts
Ruffer LLP	Diversified Growth
Schroders Asset Management Property Fund	Property

The value of the Fund, by manager, as at 31st March was as follows:

	2014		2015	
	£ million	%	£ million	%
Baillee Gifford Life Ltd - Diversified Growth	46.9	4.7	50.7	4.6
Baillee Gifford Life Ltd - Equities	183.1	18.4	217.7	19.8
GMO UK Ltd.	261.3	26.2	274.3	25.0
Investec Asset Management	97.5	9.8	99.6	9.1
Legal & General Investment Management - Equities	211.6	21.2	225.7	20.1
Legal & General Investment Management	49.0	4.9	59.4	5.9
Ruffer LLP	45.0	4.5	50.6	4.6
Schroders Asset Management Property Fund	103.1	10.3	119.5	10.9

10. INVESTMENTS (continued)

The movement in the opening and closing value of investments during the year, together with related direct transaction costs, were as follows:

	Market Value as at 1 Apr 2014 £'000	Purchases £'000	Sales £'000	Change in Market Value £'000	Market Value as at 31 Mar 2015 £'000
Baillee Gifford Life Ltd - Diversified Growth	46,889	72	0	3,724	50,685
Baillee Gifford Life Ltd - Equities	183,066	2,004	0	32,600	217,670
GMO UK Ltd.	256,678	196,511	(184,536)	1,984	270,637
Investec Asset Management	97,502	0	0	2,129	99,631
Legal & General Investment Management	260,556	0	0	24,585	285,141
Ruffer LLP	45,030	0	0	5,588	50,618
Schroders Asset Management Property	101,628	12,757	(9,762)	12,322	116,945
	991,349	211,344	(194,298)	82,932	1,091,327

A further analysis of investments assets is as follows.

	Market Value as at 1 Apr 2014 £'000	Purchases £'000	Sales £'000	Change in Market Value £'000	Market Value as at 31 Mar 2015 £'000
UK Investment Assets					
Quoted	734,671	14,833	(9,762)	80,948	820,690
Overseas Investment Assets					
Quoted	257,087	196,511	(184,536)	1,575	270,637
Unquoted	(409)	0	0	409	0
	991,349	211,344	(194,298)	82,932	1,091,327

11. INVESTMENT INCOME

Investment income is broken down as follows.

	2013/14 £'000	2014/15 £'000
Dividends from overseas equities	7,886	10,617
Net rents from properties	3,427	5,234
Interest on cash deposits	58	170
Foreign tax	169	231
TOTAL	**11,540**	**16,252**

12 ACTUARIAL POSITION

The Local Government Pension Scheme Regulations require a triennial revaluation of the Fund to assess the adequacy of the Fund's investments and contributions in relation to its overall and future obligations. The contribution rate required for benefits accruing in the future is assessed by considering the benefits that accrue over the course of the three years to the next valuation. The employer's contribution rate is determined by the Actuary as part of the revaluation exercise.

The 2013 statutory triennial revaluation of the Pension Fund completed by the Actuary (Hymans Robertson) in the year estimated the deficit on the Fund to be £365 million and the funding level to be 72%. This compares to a deficit at the previous revaluation in 2010 of £305 million and a corresponding funding level of 71%.

The Actuary has determined that the deficit can be recovered over a period of 20 years and the agreed contributions to recover the deficit for the term of the revaluation is as set out below :-

	£m
2014/15	18.50
2015/16	20.50
2016/17	22.00

The FSS requires that the Fund operates the same target funding level of all on-going employers of 100% of its accrued liabilities valued on the on-going basis, to be achieved over a 20 year period (a period equivalent to the expected future working lifetime of the remaining scheme members). The valuation of the Fund as at 31st March 2013 determined that this would require a contribution (additional to the future contribution rate) of 15.2% of members' pensionable pay equivalent to £18.5 million per annum.

The Council, as Administering Authority, prepares a Funding Strategy Statement (FSS) in respect of the Fund in collaboration with the Fund's Actuary and after consultation with the employers and investment advisors. The Actuary is required to have regard to this statement when carrying out the valuation. The FSS includes the Fund's funding policy, the objectives of which are:

- to ensure the long-term solvency of the Fund
- to ensure that sufficient funds are available to meet all benefits as they fall due for payment
- not to restrain unnecessarily the investment strategy of the Fund so that the Council can seek to maximise investment returns (and hence minimise the cost of the benefits) for an appropriate level of risk.

The basis of valuing the Fund's assets (see note 2) is compatible with the basis of placing a value on members' benefits as both are related to market conditions at the valuation date.

12. ACTUARIAL POSITION (continued)

In accordance with the funding policy, the Actuary determines the employer contribution requirement for future service for the Fund as a whole, and for employers who continue to admit new members. The cost of future service benefits is assessed, taking into account expected future salary increases. In order to place a current value on future benefit cashflows the Actuary "discounts" the future cashflows to the valuation date at a suitable rate. The Actuary adopts a "gilt-based" valuation which uses the yield on suitably dated Government bonds as the discount rate. This is then uplifted to the "funding basis discount rate" taking into account the Fund's current and expected future investment strategy to reflect the percentage by which the Fund is anticipated to "outperform" the yield on Government bonds. The contribution rate required to meet the expected cost of future service benefits is derived as this value less expected member contributions expressed as a percentage of the value of members' pensionable pay. This is known as the "Projected Unit method". The future contribution rate for 2013/14 was 15.8%.

In addition, the Actuary compares the value of the Fund's assets with the estimated cost of members' past service. The ratio of the asset value to the estimated cost of members' past service benefits is known as the "funding level". If the funding level is more than 100% there is a "surplus"; if it less than 100% there is a "shortfall". The next valuation will be as at 31st March 2016 and the recommendations implemented from 1st April 2017.

Although the funding shortfall is significant, it should be noted that current legislation provides that the level of members' basic pension entitlement and contributions are not affected by the financial position of the Fund. It is the Council's responsibility to ensure that pension entitlements are fully funded and that the impact on Council Tax is minimised. It should also be recognised that the Council is a long-term investor both because a high proportion of pension benefits do not become payable until far in the future and the Council has a relatively secure long-term income stream.

The latest full triennial actuarial valuation of the Fund's liabilities in accordance with IAS26 took place at 31st March 2013. The main actuarial assumptions used in revaluation and applied during the intervaluation period were as follows:

Financial Assumptions	Nominal	Real	
Price inflation (CPI)	2.5%		
Pay increases	3.8%	1.3%	Real rates are nominal rates
Funding basis discount rate	4.6%	2.1%	adjusted for inflation

Longevity (in years)	Male	Female
Average future life expectancy for a pensioner aged 65 at the valuation date	22.2	24.2
Average future life expectancy at age 65 for a non-pensioner aged 45 at the valuation date	24.3	26.4

Actuarial Value of Promised Retirement Benefits

IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed and for this purpose the actuarial assumptions and methodology should be based on IAS19.

The actuarial present value of promised retirement benefits calculated in line with IAS19 assumptions is estimated to be £1.783 million (£1,503 million in 2013/14).

13. MANAGEMENT EXPENSES

	2013/14 £'000	2014/15 £'000
Administration costs	906	714
Investment management expenses	2,364	2,450
Oversight & governance	181	90
	3,451	3,254

14. INVESTMENT EXPENSES

	2013/14 £'000	2014/15 £'000
Management fees	2,278	2,357
Custody fees	86	93
	2,364	2,450

15. RISK MANAGEMENT

Nature and extent of risks arising from financial instruments

Risk and Risk Management

The fund's primary long-term risk is that the fund's assets will fall short of its liabilities. The aim of investment risk management is to minimise the risk of a reduction in the value of the fund and to maximise the opportunity for gains across the whole portfolio. The fund achieves this through asset diversification to reduce exposure to market risk and credit risk to an acceptable level.

Credit risk

Credit risk is the risk that a counter party to a financial instrument may fail to pay amounts due to the Pension fund. The market value of investments generally reflect an assessment of credit in their pricing and consequently the risk of loss is implicitly provided for in the carrying value of the fund's financial assets and liabilities. The fund carries out a review of its investment managers annual internal control reports to ensure that managers are diligent in their selection and use of counterparties and brokers. Deposits are made with banks and financial institutions that are rated independently and meet the Council's credit criteria.

The Council only invests money with institutions with a minimum Fitch credit rating of A+ or higher.

Liquidity risk

This is the risk that the Fund might not have the cash flow required in order to meet its financial obligations when they become due. Over the years contributions have tended to be greater than benefits and this has ensured that sufficient cash has been available to meet payments.

The Fund currently operates two bank accounts. One is held by the Fund's custodian (State Street Bank) and holds cash relating to the investment activities and the other is the LBTH Pension Fund bank account and this is used to hold cash relating to member activities.

Should the Fund have insufficient money available to meet its commitments it may, under Regulation 5.2 borrow cash for up to 90 days. If there was a longer term shortfall then the Fund's assets could be sold to provide additional cash. A significant proportion of the Fund is made up of readily realisable assets.

Market risk

This is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises; interest rate risk, currency risk and other price risk. The Fund mitigates these risks as follows:

<u>Interest rate risk</u>

Cash deposits held in the Pension Fund bank account are invested in accordance with the Council's approved Treasury Management Strategy.

The Fund holds a percentage of its portfolio in fixed interest securities to mitigate this risk should interest rates fall.

The Fund's direct exposure to interest rate movements as at 31st March 2014 and 31st March 2015 is set out below.

Interest Rate Risk	As At 31st March 2014	As At 31st March 2015
Asset Type	£'000	£'000
Cash and cash equivalents	5,292	5,414
Cash balances	16,954	42,154
Fixed interest securities	146,517	159,079
Total	**168,763**	**206,647**

Interest Rate Risk - Sensitivity Analysis	Carrying Amount As At 31st March 2015	Change in year in net assets available to pay benefits	
		+100 BPS	-100 BPS
Asset Type		£'000	£'000
Cash and cash equivalents	5,414	54	(54)
Cash balances	42,154	422	(422)
Fixed interest securities	159,079	(1,591)	1,591
Total change in net assets available	**206,647**	**(1,115)**	**1,115**

Interest rate risk - sensitivity analysis

Interest rates can vary and can affect both income to the fund and the value of net assets available to pay benefits. A 100 basis point (BPS) movement in interest rates is consistent with the level of sensitivity applied as part of the fund's risk management strategy. The table below shows the effect of a +/- 100 BPS change in interest rates.

Interest Rate Risk - Sensitivity Analysis	Carrying Amount As At 31st March 2014	Change in year in net assets available to pay benefits	
		+100 BPS	-100 BPS
Asset Type		£'000	£'000
Cash and cash equivalents	5,292	53	(53)
Cash balances	16,954	170	(170)
Fixed interest securities	146,517	(1,465)	1,465
Total change in net assets available	**168,763**	**(1,242)**	**1,242**

15. RISK MANAGEMENT (continued)

Currency risk

The Fund invests in financial instruments denominated in currencies other than Sterling and as a result is exposed to exchange rate risk. This is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. To alleviate this risk the Fund allows investment managers to use derivative contracts, in accordance with the contract conditions:

Following analysis of historical data in consultation with the fund's investment advisors, the Council considers the likely volatility associated with foreign exchange rate movements to be 6.3%. This analysis assumes all other variables, in particular interest rates, remain constant.

The following table summarises the Fund's currency exposure as at 31 March 2015 and as at the previous year end.

Currency Exposure - Asset Type	As At 31st March 2014	As At 31st March 2015
Asset Type	£'000	£'000
Overseas quoted securities	238,710	245,548
Overseas unit trusts	5,949	3,808
Cash	13	14
Total overseas assets	**244,672**	**249,370**

Currency Exposure - Sensitivity Analysis	Carrying Amount As At 31st March 2015	Change in year in net assets available to pay benefits	
		+6.3%	-6.3%
Asset Type	£'000	£'000	£'000
Overseas quoted securities	245,548	261,018	230,078
Overseas unit trusts	3,808	4,048	3,568
Cash	14	15	13
Total change in net assets available	**249,370**	**265,081**	**233,659**

Currency Exposure - Sensitivity Analysis	Carrying Amount As At 31st March 2014	Change in year in net assets available to pay benefits	
		+5.8%	-5.8%
Asset Type		£'000	£'000
Overseas quoted securities	238,710	252,555	224,865
Overseas unit trusts	5,949	6,294	5,604
Cash	13	14	12
Total change in net assets available	**244,672**	**258,863**	**230,481**

The percentage change in the year of 6.3% represents the average change in currency exposure, derived by multiplying the weight of each currency by the change in its exchange rate relative to GBP.

Other Price risk

To mitigate the risk of a loss owing to a fall in market prices the Fund maintains a diverse portfolio of investments. Diversification ensures that the Fund has a balance of investments that offer different levels of risk and return.

The Fund employs a number of investment managers, with differing but complementary styles, to mitigate the risk of underperformance of any single manager and to ensure that any fall in market prices should not affect the Fund as a whole.

Manager performance and asset allocation policy is regularly reviewed by the Pensions Investment Panel. The Fund also uses certain derivative instruments as part of efficient portfolio management.

Other price risk - sensitivity analysis

Potential price changes are determined based on the observed historical volatility of asset class returns. 'Riskier' assets such as equities will display greater potential volatility than bonds. The potential volatilities are consistent with a one standard deviation movement in the change in value of the assets over the latest three years.

Following analysis of historical data and expected investment return movement during the financial year, in consultation with the Fund's investment advisors, the Council has determined that the following movements in market price risk are reasonably possible for the 2014/15 reporting period. This analysis assumes that all other variables, in particular foreign currency exchange rates and interest rates remain the same.

Price Risk - sensitivity analysis	Potential Market Movements (+/-)
Asset Type	
UK equities	10.1%
Global equity	10.0%
Total fixed interest	3.4%
Alternatives	4.1%
Cash	0.0%
Pooled Property Investments	2.4%

15. RISK MANAGEMENT (continued)

Had the market price of the Fund's investments increased/decreased in line with the above, the change in net assets available to pay benefits in the market price would have been as follows:

Asset Type	Value as at 31 March 2015 £'000	Percentage change %	Value on increase £'000	Value on decrease £'000
Cash and cash equivalents	47,236	0.0%	47,236	47,236
Investment portfolio assets				
UK equities	225,693	10.1%	248,488	202,898
Global equity	488,307	10.0%	537,138	439,476
Total fixed interest	159,079	3.4%	164,488	153,670
Alternatives	101,303	4.1%	105,456	97,150
Pooled Property Investments	116,945	2.4%	119,752	114,138
Net derivative assets	0	0.0%	0	0
Investment income due	978	0.0%	978	978
Amounts receivable for sales	0		0	0
Amounts payable for purchases	(223)	0.0%	(223)	(223)
Total assets available to pay benefits	**1,139,318**		**1,223,313**	**1,055,323**

Had the market price of the Fund's investments increased/decreased in line with the above, the change in net assets available to pay benefits in the market price would have been as follows:

Asset Type	Value as at 31 March 2014 £'000	Percentage change %	Value on increase £'000	Value on decrease £'000
Cash and cash equivalents	22,098	0.0%	22,098	22,098
Investment portfolio assets				
UK equities	211,541	12.1%	237,074	186,008
Global equity	440,153	11.9%	492,311	387,995
Total fixed interest	146,517	2.8%	150,678	142,356
Alternatives	91,919	4.4%	95,963	87,875
Pooled Property Investments	101,628	1.9%	103,518	99,738
Net derivative assets	(409)	0.0%	(409)	(409)
Investment income due	817	0.0%	817	817
Amounts receivable for sales	0		0	0
Amounts payable for purchases	0	0.0%	0	0
Total assets available to pay benefits	**1,014,264**		**1,102,050**	**926,478**

Refinancing risk

The Council does not have any financial instruments that have a refinancing risk as part of its treasury management and investment strategies.

16. FINANCIAL INSTRUMENTS DISCLOSURES

The net assets of the Fund are made up of the following categories of financial instruments:

	Long-term 2013/14 £'000	Long-term 2014/15 £'000	Current 2013/14 £'000	Current 2014/15 £'000
Financial Assets				
Loans and receivables	0	0	17,709	42,902
Financial assets at fair value through profit or loss	991,757	1,091,327	5,592	5,593
Total Financial Assets	**991,757**	**1,091,327**	**23,301**	**48,495**
Financial Liabilities				
Payables	0	0	(1,481)	(1,674)
Financial liabilities at fair value through profit or loss	0	0	(647)	0
Total Financial Liabilities	**0**	**0**	**(2,128)**	**(1,674)**

As all investments are disclosed at fair value, carrying value and fair value are therefore the same.

Fair Value Hierarchy

IFRS7 requires the Fund to classify fair value instruments using a three-level hierarchy.
The three levels are summarised as follows:

Level 1 - inputs that reflect quoted prices for identical assets or liabilities in active markets. Products classified as level 1 comprise quoted equities, quoted fixed securities, quoted index-linked securities and unit trusts

Level 2 - inputs other than quoted prices for identical assets or liabilities in active markets

Level 3 - inputs that are not based on observable data. Such instruments would include unquoted equity investments and hedge fund of funds.

The following sets out the Fund's assets and liabilities according to the fair value hierarchy as at 31st March 2015.

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Equities	244,335	0	0	244,335
Pooled Funds				
Unit Trusts	628,744	0	0	628,744
Property Unit Trust	116,945	0	0	116,945
Other	101,303	0	0	101,303
Derivative Contracts				
Forward Foreign Exchange Contracts	0	0	0	0
Cash and bank Deposits	47,467	0	0	47,467
Current Assets	1,079	0	0	1,079
Current Liabilities	(1,674)	0	0	(1,674)
	1,138,199	**0**	**0**	**1,138,199**

During the year ended 31st March 2015 there were no transfers between the levels of the fair value hierarchy.

The equivalents at 31st March 2014 were as follows:

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Equities	230,998	0	0	230,998
Pooled Funds				
Unit Trusts	566,768	0	0	566,768
Property Unit Trust	102,073	0	0	102,073
Other	91,918	0	0	91,918
Derivative Contracts				
Forward Foreign Exchange Contracts	0	(409)	0	(409)
Cash and bank Deposits	22,160	0	0	22,160
Current Assets	903	0	0	903
Current Liabilities	(1,481)	0	0	(1,481)
	1,013,339	**(409)**	**0**	**1,012,930**

16. FINANCIAL INSTRUMENTS DISCLOSURES

Net gains and losses on financial istruments

	Long-term	
	2013/14 £'000	2014/15 £'000
Financial Assets		
Loans and receivables		180
Financial assets at fair value through profit or loss	69,645	106,225
Total Financial Assets	**69,645**	**106,405**
Financial Liabilities		
Payables		
Financial liabilities at fair value through profit or loss	(532)	409
Total Financial Liabilities	**(532)**	**409**

17. RELATED PARTY TRANSACTIONS

The London Borough of Tower Hamlets Pension Fund is administered by The London Borough of Tower Hamlets.

In accordance with IAS24 'Related Party Disclosure', material transactions with related parties not disclosed elsewhere in the financial statements are detailed below.

The Council incurred costs of £669k (£680k 2013/14) relating to administration of the Fund and has been reimbursed by the Fund for these expenses. The Council contributed £18.5m (£16.5m 2013/14) to the Fund in respect of back funding. All monies owing to and from the Fund were paid in the year.

During the year no Committee Members or Council Chief Officers with direct responsibility for pension fund issues, have undertaken any declarable transactions with the Pension Fund, other than administrative services undertaken by the Council on behalf of the Pension Fund.

The pension fund cash held by London Borough of Tower Hamlets is invested on the money markets by the treasury management operations of the Council. During the year to 31st March 2015, the Fund held an average investment of £24.8m (£6.0m 31st March 2014), earning interest of £180k (£62k in 2013/14).

The Council has a subsidiary company, Tower Hamlets Homes, who are within the Fund. During the year the Fund received contribution payments totalling £3.5m (£2.3m 2013/14) from this company.

Fund administration expenses payable to the administrating authority are as set out in the table below.

Fund Administration Expenses	2013/14 £'000	2014/15 £'000
Payroll / HR Support	374	370
Corporate Finance	306	299
	680	669

Key Management Personnel

Employees holding key positions in the financial management of the fund as at 31st March 2015 include:
Chief Accountant

The financial value of their relationship with the fund is as set out below

	2013/14 £'000	2014/15 £'000
Short term benefits	18	20
Long term/post retirement benefits	4	4

Governance

Each member of the pension fund committee is required to declare their interests at each meeting of the Committee. These are recorded as part of the public record of each meeting. For 2014/15 there were no Members of the Pension Fund Committee who had involvement with other organisations.

Compensation of key management - It was not practical to include costs relating to key management personnel within the Pension Fund Accounts, principally as they are charged to the Council's Accounts and have not been charged to the Pension Fund. All costs are disclosed within note 33 of the Council's main accounts.

18. CONTINGENT LIABILITIES

The Council has also provided an assurance that it will meet the pension liabilities of Tower Hamlets Homes in the event the ALMO is unable to fund the liabilities arising from its pension obligations. The liability as at 31st March 2015 was £9.654m (£1.752m 2013/14).

19. CONTINGENT ASSETS

Admitted body employers in the Fund hold insurance bonds to guard against the possibility of not being able to meet their pension obligations. These bonds are drawn in favour of the pension fund and payment will only be triggered in event of employer default.

20. IMPAIRMENT LOSSES

During 2014/15 impairment losses were nil (impairment losses in 2013/14 were also nil).

TOWER HAMLETS

The London Borough of Tower Hamlets Pension Fund

Appendix 2

Statement of Investment Principle

Introduction

The Myners Code of Investment Principles

The Government commissioned a report in 2000 entitled “Review of Institutional Investment in the UK”. The Review, which was undertaken by Paul Myners was published in March 2001 and is referred to as The Myners Review. The Pensions Committee of the London Borough of Tower Hamlets believes the Myners Report constitutes an important guide to best practice in the management of pension schemes. Following a review in October 2008 the Treasury published a revised set of six principles. Local authorities are required to state the extent to which the administering authority Compliant with the six principles set out in a document published by the Chartered Institute of Public Finance and Accountancy entitled “CIPFA Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme Investment in the United Kingdom”.

COMPLIANCE

In accordance with regulation 12(3) of the LGPS (Management and Investment of Funds) Regulations 2009, the Council acting in its capacity as Administering Authority is required to state the extent to which it complies with guidance given by the Secretary of State and where it does not comply the reasons for non-compliance.

The set of six Myners Principles as they apply to Local Authority Pension Funds are:

• Effective Decision Making

• Clear Objectives

• Risk and Liabilities

• Performance Assessment

• Responsible Ownership

• Transparency and Reporting

The Pensions Committee has produced, and maintains, a record of compliance (Myners Code Adherence Document) with these principles.

The extent to which the Scheme complies with these principles is outlined in the table at the end of this document.

BACKGROUND TO THE FUND

The Legal Requirements

The Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2009 require pension fund administering authorities to prepare, maintain and publish a statement of the principles governing their decisions on the investment of the pension fund.

The Statement must cover the policy on:

(a) the types of investment to be held;

(b) the balance between different types of investments;

(c) risk, including the ways in which risks are to be measured and managed;

(d) the expected return on investments;

(e) the realisation of investments;

(f) the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments;

(g) the exercise of the rights (including voting rights) attaching to investments, if the authority has any such policy; and

(h) stock lending.

THE PENSIONS COMMITTEE

The London Borough of Tower Hamlets is the Administering Authority for the London Borough of Tower Hamlets Pension Fund. The Pensions Committee is the body with delegated powers to administer the Fund. The Committee comprised of elected representatives of Tower Hamlets Council and a non-voting employer and scheme member representatives recognise that they have fiduciary duties and responsibilities towards beneficiaries, employers and local taxpayers.

RESPONSIBILITIES

The Pensions Committee terms of reference as at the date of the publication of this Statement are as follows:

TERMS OF REFERENCE

The Pensions Committee will be responsible for the functions set out below.

1) To act as Trustees of the Council's Pension Fund within the terms of the Superannuation Act 1972, the Local Government Pension Scheme Regulations 1997 (as amended) and the Local Government Pension Scheme Management and Investment of Funds) Regulations 1998 (as amended).
2) To make arrangements for the appointment of and to appoint suitably qualified pension fund administrators, advisers, investment managers and custodian's and periodically to review those arrangements.
3) To formulate and publish a Statement of Investment Principles.
4) To set the overall strategic objectives for the Pension Fund, having taken appropriate expert advice, and develop a medium term plan to deliver the objectives.
5) To determine the strategic asset allocation policy, the mandates to be given to the investment managers and the performance measures to be set for them.
6) To monitor the performance and effectiveness of the investment managers and their compliance with the Statement of Investment Principles.
7) To set an annual budget for the operation of the Pension Fund and to monitor income and expenditure against budget.
8) To receive and approve an Annual Report on the activities of the Fund prior to publication.

9) To make arrangements to keep members of the Pension Fund informed of performance and developments relating to the Pension Fund on an annual basis.
10) To keep the terms of reference under review.
11) To determine all matters relating to admission body issues.
12) To focus on strategic and investment related matters at two Pensions Committee meetings.
13) To review the Pension Fund's policy and strategy documents on a regular cycle and review performance against the Fund's objectives within the business plan
14) To maintain an overview of pensions training for Members.
15) The Pension Committee will also co-opt a non-voting employer representative and a non-voting scheme representative.

The Committee is also responsible for reviewing performance of the investment managers (including the AVC manager), the expertise and sustainability of the investment process, procedures, risk management, internal controls, transaction costs and key personnel. It is also responsible for reviewing social, environmental and ethical matters and the exercise of rights including voting rights.

Members of the Committee receive training in their responsibilities as quasi trustees to the Pension Fund and in the operation of the pension scheme, with training primarily provided as part of the formal Committee meeting process to ensure that as many Members as possible are in attendance.
The Fund's investment advisor, officers of the Council and other external providers will provide the training itself with the Committee reviewing the programme of training to be administered to ensure that it is appropriate to the Committee's needs. The Pensions Committee has embraced the CIPFA Knowledge and Skills Framework and has undertaken a training programme to ensure that Committee Members have the requisite knowledge and skills to be able to fulfil their responsibilities as 'trustees' of the Pension Fund.

The Council's Corporate Director of Resources is responsible for ensuring the following are provided to the Committee for decision making, where appropriate including: -
(a) Budget setting and monitoring
(b) Annual Report and Accounts
(c) Preparation of Statement of Investment Principles
(d) Obtaining the Actuarial Report
(e) Developing and maintaining the Funding Strategy Statement
(f) Scheme Communications

The responsibilities of the following are set out below:

(a) **Investment Manager** – Day-to-day decisions on investment of the Fund's assets within the mandates approved by Committee and set out by the Investment Management Agreement. Exercise of corporate actions within the policy set by this Statement of Investment Principles. Reporting to the Executive Officers and Pensions Committee on performance against established benchmarks.

(b) **Custodian** – Providing safe keeping for the share certificates and other documents of title to Fund investments. Receiving and accounting for dividends and corporate actions.

(c) **Actuary** – Carrying out the actuarial valuation of the Fund's assets and liabilities every three years in accordance with the regulations. The valuation report specifies the level of funding to cover accrued liabilities and the consequent changes (if any) to the employer's contribution rates. The actuary is also responsible for negotiating bulk transfer arrangements and determining contribution rates for new employers where these are established between triennial valuations.

(d) **Investment Consultant** – The investment consultant is there to provide the Pension Committee and officers of the Council with investment related advice pertinent to the management of the Pension Fund to ensure that its investments are appropriate and prudent.

(e) **Administrators** – The Council is the Fund administrator that undertake the day-to-day administration of the Pension Fund, including the payment of pension benefits and maintenance of pension benefit records.

Advice

The Committee takes expert professional financial advice to assist it with managing the Fund Regulation 12(3) also requires Administering Authorities to have regard to guidance given by the Secretary of State on investment decision making and to state in their Statement how far they comply with that guidance.
Advice to the Members of the Pension Committee is given by the executive officers of the Council (including, but not limited to, the Corporate Director of Resources and the Director Law Probity and Governance & Monitoring Officer).
The Pension Fund has access to the use of external providers for actuarial and investment services for advice. The Pension Fund employs the services of an actuary to provide ongoing actuarial advice and to carry out a valuation of the Fund every three years (the triennial valuation) in accordance with the Local Government Pension Scheme Regulations 2013. In addition the Fund also uses an appointed investment advisor to provide professional advice to the Committee on investment related issues.
The Pensions Committee monitors the level of fees that are paid to the advisers in order to ensure that the advice is charged at an appropriate level, and represents value for money. The Committee will carry out procurement exercises at appropriate intervals to ensure that this continues to be the case.

Fund Objective

The primary objective of the Scheme is to provide pension and lump sum benefits for members on their retirement and/or benefits on death, before or after retirement, for their dependents, on a defined benefits basis.

The Council aims to fund the Scheme in such a manner that, in normal market conditions, all accrued benefits are fully covered by the value of the Scheme's assets and that an appropriate level of contributions is agreed by the employer to meet the cost of future benefits accruing. For employee members, benefits will be based on service completed but will take account of future salary increases.

This funding position will be reviewed at each triennial actuarial valuation, or more frequently as required.

Therefore the primary investment objective of the Fund is to ensure that due regard is paid to the best financial interests of all its stakeholders. Against this background, the Fund's approach to investing is to:

- Optimise the return on investment consistent with a prudent level of risk;
- Ensure that there are sufficient assets to meet the liabilities; and
- Ensure the suitability of assets in relation to the needs of the Fund.

INVESTMENT STRATEGY

The Pensions Committee has translated these objectives into a suitable strategic asset allocation benchmark for the Scheme. All day to day investment decisions have been delegated to the Scheme's authorised investment managers. The strategic benchmark has been translated into benchmarks for the Scheme's investment managers which are consistent with the Scheme's overall strategy. The Scheme benchmark is consistent with the Pensions Committee views on the appropriate balance between maximising the long-term return on investments and minimising short-term volatility and risk.

The investment strategy takes due account of the maturity profile of the Scheme (in terms of the relative proportions of liabilities in respect of pensioners and active members), together with the level of disclosed surplus or deficit (relative to the funding bases used on an ongoing basis).

The Pensions Committee monitors strategy relative to its agreed asset allocation benchmark. It is intended that investment strategy will be reviewed at least every three years following actuarial valuations of the Scheme.

To achieve its objectives the Pensions Committee has agreed the following:

Choosing Investments: The Pensions Committee is responsible for the appointment of investment managers who are authorised under the Financial Services and Markets Act 2000 to undertake investment business. The Pensions Committee, after seeking appropriate investment advice, has given the managers specific directions as to the asset allocation, but investment choice has been delegated to the managers, subject to their specific benchmarks and asset guidelines.

Risk: The Pensions Committee provides a practical constraint on Scheme investments deviating greatly from its intended approach by adopting a specific asset allocation benchmark and by setting manager-specific benchmark guidelines. The Pensions Committee monitors the managers' adherence to benchmarks and guidelines. In appointing more than one investment manager, the Pensions Committee has considered the risk of underperformance of any single investment manager.

Kinds of investment to be held: The Scheme may invest in quoted and unquoted securities of UK and overseas markets including equities and fixed interest and index linked bonds, cash, property and pooled funds. The Scheme may also make use of derivatives and contracts for difference for the purpose of efficient portfolio management. The Pensions Committee considers all of these classes of investment to be suitable in the circumstances of the Scheme. The Fund's structure and benchmarks are set out in the table below.

Current Managers and Mandates		
Manager	**Mandate**	**Target**
Baillie Gifford	Global Equities Diversified Growth	Outperform benchmark by 2-3% over a rolling 3 year period 3.5% above UK Base Rate
GMO	Overseas Equities	Outperform benchmark by 1.5% over a rolling 3 year period
Investec	Pooled Bonds	3 month LIBOR +2% pa
Legal & General	UK Equities UK Index Linked	FTSE All share FTSE A Gov Index Linked >5yrs
Ruffer	Diversified Growth	Greater than the expected return on cash
Schroders	Property	Outperform benchmark by 0.75% over a rolling 3 year period

Balance between different kinds of investments: The Scheme's investment managers will hold a mix of investments which reflects their views relative to their respective benchmarks. Within each major market the managers will maintain diversified portfolios of investments through direct holdings or pooled vehicles. The asset allocation varies over time due to the impact of changing market conditions and manager performance creating an imbalance between target and actual allocation. When the Fund moves more than 5% away from target then consideration is given to rebalancing.

Expected return on investments: Over the long term, the overall level of investment returns is expected to exceed the rate of return assumed by the actuary in funding the Scheme. In the short term returns are measured against a peer group benchmark.

Realisation of investments: The majority of investments held within the Scheme may be realised quickly if required. As the Fund is cash flow positive there will not be a need to realise investments quickly at least in the medium term.

Social, Environmental and Ethical Considerations: The Council has a fiduciary responsibility to obtain the best level of investment return consistent with the defined risk parameters as embodied in the strategic benchmark. However, the Council recognises that Social, Ethical and Environmental issues are factors to be taken into consideration in assessing investments. The investment managers have confirmed they pay due attention to these factors in the selection, retention and realisation of investments. The Pensions Committee will monitor the managers’ statements and activities in this regard.

Exercise of Voting Rights: The Pensions Committee has delegated the exercise of voting rights to the investment managers on the basis that voting power will be exercised by them with the objective of preserving and enhancing long term shareholder value. Accordingly, the managers have produced written guidelines of their processes and practices in this regard. The managers are encouraged to vote in line with their guidelines in respect of all resolutions at annual and extraordinary general meetings of companies.

Stock Lending

The Fund does not currently participate in a stock lending arrangement.

Additional Voluntary Contributions (AVCs): The Pensions Committee gives members the opportunity to invest in a range of vehicles at the members' discretion.

Appendix 1

Principle	Compliance	Compliance
Principle 1: Effective Decision Making Administering authorities should ensure that: Decisions are taken by persons or organisations with the skills, knowledge, advice and resources to make them effectively and monitor their implementation; Those persons or organisations have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.	The Council has a Pensions Committee who meets on a quarterly basis for decision making purposes. The Fund's Governance Compliance Statement sets out the governance structure, Terms of Reference, delegations and representation. All members and officers of the Committee are required to undertake training on a periodic basis to ensure that they attain the necessary knowledge and skills with which to undertake their duties effectively. To ensure that they are fully aware of their statutory and fiduciary responsibilities new members are provided with a handbook containing the Committee's terms of reference, standing orders and operational procedures. Two training days per year are arranged for the committee members to deliver training. The committee intends to use the CIPFA knowledge and skills framework as the basis for a training programme to assess the training needs of its members and to actively monitor the progress made. The Fund contracts an actuary, a professional investment advisor and an independent investment advisor all of who attend committee meetings throughout the year and provide advice to committee members. Other expert advisors attend as required.	Compliant
Principle 2: Clear Objectives An overall investment objective should be set out for the fund that takes account of the scheme's	The Fund's aims and objectives are set out in its Funding Strategy Statement and Investment Management Agreements are in place on the segregated mandates held by the Fund. The funding strategy is reviewed at each triennial valuation and the actuarial position and financial impact on scheme employers and tax payers is considered when formulating the investment strategy.	Compliant

liabilities, the potential impact on local tax payers, the strength of the covenant for non-local authority employers, and the attitude to risk of both the administering authority and scheme employers, and these should be clearly communicated to advisors and investment managers.	All external procurement is conducted within EU procurement regulations and the authority's own procurement rules. The Fund is aware of the investment management fees charged by the investment managers and transaction related costs, and this is considered when letting and monitoring contracts for investment management.	
Principle 3: Risk and Liabilities In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities. These include the implications for local tax payers, the strength of the covenant for participating employers, the risk of their default and longevity risk.	Following each triennial valuation the Committee assesses the structure of the Fund's liabilities and, where necessary, amends its investment strategy to ensure that it remains appropriate to the Fund's liability profile. The same investment strategy is currently followed by all employers. The Fund's liabilities are long term in nature and the investment strategy reflects this liability profile by investing in long term generating assets. The Fund's benchmark includes a significant holding in equities in pursuit of long term higher returns. Allowances are made for periods of underperformance in the short term. The triennial valuation sets out the liability profile for each individual employer. The strength of covenant of each employing body and risk of default is taken into consideration when setting the employer contribution rate. The Fund has an active risk management programme in place. The risk management process is outlined in the Fund's Annual Report and Accounts. The Committee receives the external auditor's Annual Governance Report which states their assessment of the risk management process.	Compliant

Principle 4: Performance assessment Arrangements should be in place for the formal measurement of performance of the investments, investment managers and advisors. Administering authorities should also periodically make a formal assessment of their own effectiveness as a decision-making body and report on this to the scheme members.	The Fund's Pensions Committee meets quarterly to review the Fund's performance against its investment objective. In consultation with the Fund's investment advisors the Committee will assess the performance of the investment managers and consider whether any action is required. The fund managers attend the Pensions Committee meetings periodically. The Fund employs the WM company to measure the performance of its investment managers. The Fund's Annual Report is presented to the Committee explaining the Fund's activities and decisions taken during the year. This allows the Pensions Committee to reflect on the effectiveness of its strategy and also the management of the fund managers to deliver against agreed benchmarks.	Compliant
Principle 5: Responsible ownership Administering authorities should: Adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholders and agents, include a statement of their policy on responsible ownership in the statement of investment principles. Report periodically to scheme members on the discharge of such responsibilities.	The Fund requires its investment managers to adopt the Institute Shareholders Committee Statement of Principles. The extent to which these principles are taken into account in the selection, retention and realisation of investments is left to the manager's discretion. The manager's activities in this regard are reviewed by the Pensions Committee. The Fund's approach to responsible ownership is set out in its Statement of Investment Principles. Any significant issues arising over the year are reported in the Fund's Annual Report.	Compliant

Principle 6: Transparency and reporting Administering authorities act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives. Provide regular communication to scheme members in the form they consider most appropriate.	The Fund publishes a Governance Policy Statement, a Communications Strategy, a Funding Strategy Statement, and a Statement of Investment Principles. The statements are reviewed and updated when required and are approved by the Pensions Committee. Fund manager performance data is included in the Fund's Annual Report and Accounts. The statements form part of a suite of annual report documentation which may be found on the website http://http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392 An Annual Benefits Statement is sent hard copy to active and deferred members of the Fund. Pensioner members receive an annual newsletter detailing any information affecting pensions in payment.	Compliant

The London Borough of Tower Hamlets Pension Fund

Appendix 3

Funding Strategy Statement

FUNDING STRATEGY STATEMENT

1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the London Borough of Tower Hamlets Pension Fund ("the Fund"), which is administered by London Borough of Tower Hamlets, ("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 1st April 2014.

1.2 What is the London Borough of Tower Hamlets 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 London Borough of Tower Hamlets Fund, in effect the LGPS for the London Borough of Tower Hamlets 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 of 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 and cessations;
- 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 Anant Dodia in the first instance at e-mail address anant.dodia@towerhamlets.gov.uk or on telephone number 020 7364 4248.

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 which will be issued by 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 covenants, 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** ("CAB") or those providing a service on behalf of a scheme employer – **transferee admission bodies** ("TAB"). CABs will include housing associations and charities, TABs will generally be contractors. The Fund is able to set its criteria for participation by these employers and can refuse entry if the requirements as set out in the Fund's admissions policy are not met.

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**	**Police, Fire, Colleges etc**	**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)	No employers of this type	No	No	No	No
Maximum deficit recovery period – Note (c)	20 years	NA	14 years	20 years	Future working lifetime of remaining active members	Outstanding contract term

Deficit recovery payments – Note (d)	Monetary amount	NA	% of payroll	% of payroll	Monetary amount	% of payroll
Treatment of surplus	Covered by stabilisation arrangement	NA	Spread over recovery period	Preferred approach: contributions kept at future service rate. However, reductions may be permitted by the Admin. Authority		Preferred approach: contributions kept at future service rate. However, reductions may be permitted by the Admin. Authority
Phasing of contribution changes	Covered by stabilisation arrangement	NA	Maximum of 3 years	3 years - Note (e)	3 years - Note (e)	Maximum of 3 years
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	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 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 employer 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 to the London Borough of Tower Hamlets Council.

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

Employer	London Borough of Tower Hamlets
Max contribution increase	+£2m
Max contribution decrease	-£2m

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 approach 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.

Note (d) (Deficit Recovery Payments)

For employers where stabilisation is not being applied, the deficit recovery payments for each employer covering the three year period until the next valuation will often be set as a percentage of salaries. However, the Administering Authority reserves the right to amend these rates between valuations and/or to require these payments in monetary terms instead, for instance where:

(i) the employer is relatively mature, i.e. has a large deficit recovery contribution rate because of a small or decreasing payroll; or

(ii) the employer has closed the Fund to new entrants.

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.

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 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 calculated using market conditions, the council funding position and, membership data, all as at the day prior to conversion;

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, policy (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/outsourcing of some services from an existing employer (normally a Scheduled Body such as a council or academy) to another organisation (a “contractor”). This involves the TUPE transfer of some staff from the letting employer to the contractor. Consequently, for the duration of the contract, the contractor is a new participating employer in the Fund so that the transferring employees maintain their eligibility for LGPS membership. At the end of the contract the employees revert to the letting employer or to a replacement contractor.

Ordinarily, the TAB would be set up in the Fund as a new employer with responsibility for all the accrued benefits of the transferring employees; in this case, the contractor would usually be assigned an initial asset allocation equal to the past service liability value of the employees’ Fund benefits. The quid pro quo is that the contractor is then expected to ensure that its share of the Fund is also fully funded at the end of the contract: see Note (j).

Employers which “outsource” have flexibility in the way that they can deal with the pension risk potentially taken on by the contractor. In particular there are three different routes that such employers may wish to adopt. Clearly as the risk ultimately resides with the employer letting the contract, it is for them to agree the appropriate route with the contractor:

i) Pooling

Under this option the contractor is pooled with the letting employer. In this case, the contractor pays the same rate as the letting employer, which is may be under the stabilisation approach.

ii) Letting employer retains pre-contract risks

iii) 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;

a. 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;
b. 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;
- 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.

3.3 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. Transferee Admission Bodies are usually also ineligible for pooling.

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

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.

3.4 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.

3.5 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.

3.6 Ill health early retirement costs

Admitted Bodies will usually have an 'ill health allowance'; Scheduled Bodies may have this also, depending on their agreement terms with the Administering Authority. The Fund monitors each employer's ill health experience on an ongoing basis. If the cumulative cost of ill health retirement in any financial year exceeds the allowance at the previous valuation, the employer will be charged additional contributions on the same basis as apply for non ill-health cases.

3.7 Ill health insurance

If an employer provides satisfactory evidence to the Administering Authority of a current insurance policy covering ill health early retirement strains, then:

- the employer's contribution to the Fund each year is reduced by the amount of that year's insurance premium, so that the total contribution is unchanged, and
- there is no need for monitoring of allowances.

The employer must keep the Administering Authority notified of any changes in the insurance policy's coverage or premium terms, or if the policy is ceased.

3.8 Employers with no remaining active members

In general an employer ceasing in the Fund, due to the departure of the last active member, will pay a cessation debt on an appropriate basis (see 3.3, Note (j)) and consequently have no further obligation to the Fund. Thereafter it is expected that one of two situations will eventually arise:

a) The employer's asset share runs out before all its ex-employees' benefits have been paid. In this situation the other Fund employers will be required to contribute to pay all remaining benefits: this will be done by the Fund actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;

b) The last ex-employee or dependant dies before the employer's asset share has been fully utilised. In this situation the remaining assets would be apportioned pro-rata by the Fund's actuary to the other Fund employers.

c) In exceptional circumstances the Fund may permit an employer with no remaining active members to continue contributing to the Fund. This may 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.

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.

4.5 Does the Fund monitor its overall funding position?

The Administering Authority monitors the relative funding position, i.e. changes in the relationship between asset values and the liabilities value, on an ad-hoc basis.

Appendix A – Regulatory framework

A1 Why does the Fund need an FSS?

The Department for Communities and Local Government (DCLG) has stated that the purpose of the FSS is:

- *"to establish a **clear and transparent fund-specific strategy** which will identify how employers' pension liabilities are best met going forward;*
- *to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and*
- *to take a **prudent longer-term view** of funding those liabilities."*

These objectives are desirable individually, but may be mutually conflicting.

The requirement to maintain and publish a FSS is contained in LGPS Regulations which are updated from time to time. In publishing the FSS the Administering Authority has to have regard to any guidance published by Chartered Institute of Public Finance and Accountancy (CIPFA) (most recently in 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 issued to all participating employers on 27 January 2014 for comment;

b) Comments were requested within 22 days; and

c) Following the end of the consultation period the FSS was updated where required and the report will be published on 1st December.

A3 How is the FSS published?

The FSS is made available through the following routes:

- Published on the website, at http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392;

- A copy sent by [post/e-mail] to each participating employer in the Fund;
- A copy sent to [employee/pensioner] representatives;
- A summary issued to all Fund members;
- 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
http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392

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;
- advise the Actuary of any new or ceasing employers;
- 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 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. Inter-valuation roll-forward of liabilities between valuations at whole Fund level.
Inappropriate long-term investment strategy.	Overall investment strategy options considered as an integral part of the funding strategy. Used asset liability modelling to measure 4 key outcomes. Chosen option considered to provide the best balance.
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	Stabilisation modelling at whole Fund level allows for the probability of this within a longer term context. Inter-valuation monitoring, as above. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers

Risk	Summary of Control Mechanisms
	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. Inter-valuation monitoring, as above, gives early warning. Some investment in bonds also helps to mitigate this risk. Employers pay for their own salary awards and should be mindful of the geared effect on pension liabilities of any bias in pensionable pay rises towards longer-serving employees.
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	An explicit stabilisation mechanism has been agreed as part of the funding strategy. Other measures such as deficit spreading and phasing are also in place to limit sudden increases in contributions,
Orphaned employers give rise to added costs for the Fund	The Fund seeks a cessation debt (or security/guarantor) to minimise the risk of this happening in the future. If it occurs, the Actuary calculates the added cost spread pro-rata among all employers – (see 3.9).

C3 Demographic risks

Risk	Summary of Control Mechanisms
Pensioners living longer, thus increasing cost to Fund.	Set mortality assumptions with some allowance for future increases in life expectancy. The Fund Actuary has direct access to the experience of over 50 LGPS funds which allows early identification of changes in life expectancy that might in turn affect the assumptions underpinning the valuation.
Maturing Fund – i.e. proportion of actively contributing employees declines relative to retired employees.	Continue to monitor at each valuation, consider seeking monetary amounts rather than % of pay and consider alternative

Risk	Summary of Control Mechanisms
	investment strategies.
Deteriorating patterns of early retirements	Employers are charged the extra cost of non-ill-health retirements following each individual decision. Employer ill health retirement experience is monitored, and insurance is an option.
Reductions in payroll causing insufficient deficit recovery payments	In many cases this may not be sufficient cause for concern, and will in effect be caught at the next formal valuation. However, there are protections through employers paying 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 may be expressed as monetary amounts.

Risk	Summary of Control Mechanisms
Actuarial or investment advice is not sought, or is not heeded, or proves to be insufficient in some way	The Administering Authority maintains close contact with its specialist advisers. Advice is delivered via formal meetings involving Elected Members, and recorded appropriately. Actuarial advice is subject to professional requirements such as peer review.
Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.
An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure. The risk is mitigated by: Seeking a funding guarantee from another scheme employer, or external body, where-ever possible (see Notes (h) and (j) to 3.3). 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).

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

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.

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 (this a change from the 2010 valuation where 1.4% was used). 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 0.5% above the retail prices index (RPI) per annum. This is a change from the previous valuation, which assumed a three year restriction at 1% per annum followed by longer 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. This is a larger reduction than at 2010, which will serve to reduce the value placed on the Fund’s liabilities (all other things being equal).

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 “medium cohort” and a 1.25% per annum minimum underpin to future reductions in mortality rates. 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 0.5 years 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.

The London Borough of Tower Hamlets Pension Fund

Appendix 4

Communications Strategy Statement

CONTENTS

Introduction

This is the Communications Strategy Statement of London Borough of Tower Hamlets Pension Fund.

The Fund liaises with over 12 employers and approximately 15,000 scheme members in relation to the Local Government Pension Scheme. The delivery of the benefits involves communication with a number of other interested parties. This statement provides an overview of how we communicate and how we intend to measure whether our communications are successful.

Any enquiries in relation to this Communication Strategy Statement should be sent to:

London Borough of Tower Hamlets
Town Hall
Human Resources
Payroll & Pensions Services
Mulberry Place
5 Clove Crescent
London E14 2BG

Telephone: 020 7364 4251
Facsimile: 020 7364 4593

Email: pensions@towerhamlets.gov.uk

Regulatory Framework

This Policy Statement is required by the provisions of Regulation 106B of the Local Government Pension Scheme (LGPS) Regulations 1997. The provision requires us to:

"….prepare, maintain and publish a written statement setting out their policy concerning communications with:

(a) members.
(b) representatives of members.
(c) prospective members.
(d) employing authorities."

In addition it specifies that the Statement must include information relating to:

"(a) the provision of information and publicity about the Scheme to members, representatives of members and employing authorities;
(b) the format, frequency and method of distributing such information or publicity; and
(c) the promotion of the Scheme to prospective members and their employing authorities."

As a provider of an occupational pension scheme, we are already obliged to satisfy the requirements of the Occupational Pension Schemes (Disclosure of information) Regulations and other legislation, for example the Pensions Act 2004. Previously the disclosure requirements have been prescriptive, concentrating on timescales rather than quality. From 6 April 2006 more generalised disclosure requirements are to be introduced, supported by a Code of Practice. The type of information that pension schemes are required to disclose will remains very much the same as before, although the prescriptive timescales are being replaced with a more generic requirement to provide information within a *"reasonable period"*.

The draft Code of Practice[3] issued by the Pensions Regulator in September 2005 sets out suggested timescales in which the information should be provided. While the Code itself is not a statement of the law, and no penalties can be levied for failure to comply with it, the Courts or a tribunal must take account of it when determining if any legal requirements have not been met. A summary of our expected timescales for meeting the various disclosure of information requirements are set out in the Performance Management section of this document, alongside those proposed by the Pension Regulator in the draft Code of Practice.

Responsibilities and Resources
Within the Pension Section, the responsibility for communication material is performed by our Pensions Manager with the assistance of two Principal Pensions Officers.
Although, the team write all communications within the section, all design work is carried out by the Council's Creative & Technical team. The Pensions team are also responsible for arranging all forums, workshops and meetings covered within this Statement.
All printing is carried out by an external supplier, which is usually decided upon by the Council's Creative & Technical team.

Communication with key audience groups
Our audience

We communicate with a number of stakeholders. For the purposes of this Communication Policy Statement, we are considering our communications with the following audience groups:

- active members;
- deferred members;
- pensioner members;
- prospective members;
- employing authorities (scheme employers and admitted bodies);
- senior managers;
- union representatives;
- elected members/the Pension Panel;
- Pensions Section staff;

In addition there are a number of other stakeholders with whom we communicate on a regular basis, such as Her Majesty's Revenue and Customs, the Department for Communities and Local Government, solicitors, the Pensions Advisory Service, and other pension providers. We also consider as part of this policy how we communicate with these interested parties.

How we communicate
General communication

We will continue to use paper based communication as our main means of communicating, for example, by sending letters to our scheme members. However, we will compliment this by

[3] Code of Practice – Reasonable periods for the purposes of the Occupational Pension Schemes (Disclosure of Information) Regulations 2006 issued September 2005

use of electronic means such as our intranet. We will accept communications electronically, for example by e-mail and, where we do so, we will respond electronically where possible.

Our pension section staffs are responsible for specific tasks. Any phone calls or visitors are then passed to the relevant person within the section. Direct line phone numbers are advertised to allow easier access to the correct person.

Branding
As the Pension Fund is administered by London Borough of Tower Hamlets, all literature and communications will conform to the branding of the Council.

Accessibility
We recognise that individuals may have specific needs in relation to the format of our information or the language in which it is provided. Demand for alternative formats/languages is not high enough to allow us to prepare alternative format/language material automatically. However, on all communication from the Pension Fund office we will include a statement offering the communication in large print, Braille, on cassette or in another language on request.

Policy on Communication with Active, Deferred and Pensioner Members
Our objectives with regard to communication with members are:

- for the LGPS to be used as a tool in the attraction and retention of employees.
- for better education on the benefits of the LGPS.
- to provide more opportunities for face to face communication.
- as a result of improved communication, for queries and complaints to be reduced.
- for our employers to be employers of choice.
- to increase take up of the LGPS employees.
- to reassure stakeholders.

Our objectives will be met by providing the following communications, which are over and above individual communications with members (for example, the notifications of scheme benefits or responses to individual queries). The communications are explained in more detail beneath the table:

Scheme booklet	Paper based and on intranet	At joining and major scheme changes	Post to home address/via employers	Active
Newsletters	Paper based and on intranet	Annually and after any scheme changes	Via employers for Actives. Post to home address for deferred & pensioners	Separately for active, deferred and pensioners
Pension Fund Report and Accounts	Paper based and on intranet	Annually	On request	All
Pension Fund Accounts – Summary	Paper based	Annually	Via employers for actives. Post to home address for deferred and pensioners	All
Estimated Benefit Statements	Paper based/via intranet	Annually	Post to home address/via employers for active members. To home address for deferred members.	Active and Deferred.
Factsheets	Paper based and on intranet	On request	On request	Active, deferred & pensioners
Intranet	Electronic	Continually available	Advertised on all communications	All
Road shows/ Workshops	Face to face	Annually	Advertised in newsletters, via posters and pensioners payslips	All
Face to face education sessions	Face to face	On request	On request	All
Joiner packs	Paper based	On joining	Post to home addresses	Active members
Pay advice slip/P60	Paper based	Conditional	Post to home address	Pensioners

Explanation of communications

Scheme booklet - A booklet providing a relatively detailed overview of the LGPS, including who can join, how much it costs, the retirement and death benefits and how to increase the value of benefits.

Newsletters - An annual/biannual newsletter which provides updates in relation to changes to the LGPS as well as other related news, such as national changes to pensions, forthcoming road shows, a summary of the accounts for the year, contact details, etc.

Pension Fund Report and Accounts – Details of the value of the Pension Fund during the financial year, income and expenditure as well as other related details, for example, the current employing authorities and scheme membership numbers. This is a somewhat detailed and lengthy document and, therefore, it will not be routinely distributed except on request. A summary document, as detailed below, will be distributed.

Pension Fund Report and Accounts Summary – provides a handy summary of the position of the Pension Fund during the financial year, income and expenditure as well as other related details.

Estimated Benefit Statements – For active members these include the current value of benefits as well as the projected benefits as at their earliest retirement date and at age 65. The associated death benefits are also shown as well as details of any individuals the member has nominated to receive the lump sum death grant. State benefits are also included. In relation to deferred members, the benefit statement includes the current value of the deferred benefits and the earliest payment date of the benefits as well as the associated death benefits.

Factsheets – These are leaflets that provide some detail in relation to specific topics, such as topping up pension rights, transfer values in and out of the scheme, death benefits and, for pensioners, annual pension's increases.

Intranet – The intranet will provide scheme specific information, forms that can be printed or downloaded, access to documents (such as newsletters and report and accounts), frequently asked questions and answers, links to related sites and contact information.

Road shows/Workshops – Every year a number of staff will visit the schools/offices around the Borough, providing the opportunity to have a face to face conversation about your pension rights

Face to face education sessions – These are education sessions that are available on request for small groups of members. For example, where an employer is going through a restructuring, it may be beneficial for the employees to understand the impact any pay reduction may have on their pension rights.

Joiner packs – These complement the joiner booklet and enclose information on AVCs and the paperwork needed to join the scheme.

Pay advice slip/P60 – The Pay advice slips are sent when the address, pension or tax code changes. The P60 information is communicated using this medium on an annual basis.

Policy on promotion of the scheme to Prospective Members and their Employing Authorities

Our objectives with regard to communication with prospective members are:

- to improve take up of the LGPS.
- for the LGPS to be used as a tool in the attraction of employees.
- for our employers to be employers of choice.
- for public relations purposes.

As we, in the Pension Team Section, do not have direct access to prospective members, we will work in partnership with the employing authorities in the Fund to meet these objectives. We will do this by providing the following communications:

Overview of the LGPS leaflet	Paper based	On commencing employment	Via employers	New employees
Educational sessions	As part of induction workshops	On commencing employment	Face to face	New employees
Promotional newsletters/flyers	Paper based	Annually	Via employers	Existing employees
Posters	Paper based	Ongoing	Via employers	New and existing employees

Explanation of communications

Overview of the LGPS leaflet - A short leaflet that summarises the costs of joining the LGPS and the benefits of doing so.

Educational sessions – A talk providing an overview of the benefits of joining the LGPS.

Promotional newsletters/flyers – These will be designed to help those who are not in the LGPS to understand the benefits of participating in the Scheme and provide guidance on how to join the Scheme.

Posters – These will be designed to help those who are not in the LGPS understand the benefits of participating in the scheme and provide guidance on how to join the Scheme.

Policy on communication with Employing Authorities

Our objectives with regard to communication with employers are:

- to improve relationships.
- to assist them in understanding costs/funding issues.
- to work together to maintain accurate data.
- to ensure smooth transfers of staff.
- to ensure they understand the benefits of being an LGPS employer.

- to assist them in making the most of the discretionary areas within the LGPS.

Our objectives will be met by providing the following communications:

Employers' Guide	Paper based and intranet	At joining and updated as necessary	Post or via email	Main contact for all employers
Newsletters	Electronic (e-mail) and intranet	Annually or more frequent if necessary	E-mail	All contacts for all employers
Employers' focus groups	Face to face	At least quarterly/half yearly	Invitations by e-mail	Either main contacts or specific groups (e.g. HR or payroll) depending on topics
Pension Fund Report and Accounts	Paper based and employer website	Annually	Post	Main contact for all employers
Meeting with adviser	Face to face	On request	Invite sent by post or email	Senior management involved in funding and HR issues.

Explanation of communications

Employers' Guide – is a detailed guide that provides guidance on the employer responsibilities, including the forms and other necessary communications with the Pensions Section and Scheme members.

Newsletters – A technical briefing newsletter that will include recent changes to the scheme, the way the Pensions Section is run and other relevant information so as to keep employers fully up to date.

Employers' focus groups – Generally workgroup style sessions set up to debate current issues within the LGPS.

Pensions Fund Report and Accounts – Details of the value of the Pension Fund during the financial year, income and expenditure as well as other related details, for example, the current employing authorities and scheme membership numbers.
Adviser meeting – Gives employers the opportunity to discuss their involvement in the Scheme with advisers.

Policy on communication with senior managers
Our objectives with regard to communication with senior managers are:

- to ensure they are fully aware of developments within the LGPS
- to ensure that they understand costs/funding issues
- to promote the benefits of the Scheme as a recruitment/retention tool.

Our objectives will be met by providing the following communications:

Method of communication	Media	Frequency of Issue	Method of Distribution	Audience Group
Briefing papers	Paper based and electronic	As and when required	Email or hard copy	All
Committee papers	Paper based and electronic	In advance of Committee	Email or hard copy	All

Explanation of communications
Briefing papers – a briefing that highlights key issues or developments relating to the LGPS and the Fund, which can be used by senior managers when attending meetings

Committee paper – a formal document setting out relevant issues in respect of the LGPS, in many cases seeking specific decisions or directions from elected members

Policy on communication with union representatives
Our objectives with regard to communication with union representatives are:

- to foster close working relationships in communicating the benefits of the Scheme to their members
- to ensure they are aware of the Pension Fund's policy in relation to any decisions that need to be taken concerning the Scheme
- to engage in discussions over the future of the Scheme
- to provide opportunities to Education Union representatives on the provisions of the Scheme

Our objectives will be met by providing the following communications:

Method of communication	Media	Frequency of Issue	Method of Distribution	Audience Group
Briefing papers	Paper based and electronic	As and when required	Email or hard copy	All
Face to face education sessions	Face to face	On request	On request	All
Pension Committee	Meeting	Quarterly	Via invitation when appropriate	All

Explanation of communications

Briefing papers – a briefing that highlights key issues and developments relating to the LGPS and the Fund.

Face to face education sessions – these are education sessions that are available on request for union representatives and activists, for example to improve their understanding of the basic principles of the Scheme, or to explain possible changes to policies.

Pensions Committee – a formal meeting of elected members, attended by senior managers, at which local decisions in relation to the Scheme (policies, etc) are taken.

Policy on communication with elected members/Pensions Committee

Our objectives with regard to communication with elected members/Pensions Committee are:

- to ensure they are aware of their responsibilities in relation to the Scheme
- to seek their approval to the development or amendment of discretionary policies, where required
- to seek their approval to formal responses to government consultation in relation to the Scheme.

Our objectives will be met by providing the following communications:

Method of Communication	Media	Frequency of Issue	Method of Distribution	Audience Group
Training sessions	Face to face	When there is a new Pensions Committee and as and when required	Face to face or via the Employers Organisation for local government	All members of the Pensions Committee as well as other elected members
Briefing papers	Paper based and electronic	As and when required	Email or hard copy	All members of the Pensions Committee
Pension Committee	Meeting	Quarterly	Members elected onto Pension Committee	All members of the Pensions Committee

Explanation of communications
Training sessions – to provide a broad overview of the main provisions of the LGPS to elected members and their responsibilities within it.

Briefing papers - a briefing that highlights key issues and developments to the LGPS and the Fund.

Pension Committee - a formal meeting of elected members, attended by senior managers, at which local decisions in relation to the Scheme (policies, etc.) are taken.

Policy on communication with pension section staff
Our objectives with regard to communication with Pension Section's staff are:

- ensure they are aware of changes and proposed changes to the scheme
- to provide on the job training to new staff
- to develop improvements to services, and changes to processes as required
- to agree and monitor service standards

Our objectives will be met by providing the following communications:

Method of Communication	Media	Frequency of Issue	Method of Distribution	Audience Group
Face to face training sessions	Face to face	As required	By arrangement	All
Staff meetings	Face to face	As required, but no less frequently than monthly	By arrangement	All
Attendance at seminars	Externally provided	As and when advertised	By email, paper based	All
Software User Group meetings	Face to face	Quarterly	By email, paper based.	Principal Administrators
Regional Officer Group meetings	Face to face	Quarterly	By email, paper based.	Pension Manager/ Principal Administrators

Explanation of communications

Face to face training sessions – which enable new staff to understand the basics of the Scheme, or provide more in depth training to existing staff, either as part of their career development or to explain changes to the provisions of the Scheme

Staff meetings – to discuss any matters concerning the local administration of the Scheme, including for example improvements to services or timescales

Attendance at seminars – to provide more tailored training on specific issues

Software User Group meeting – to discuss any issues concerning the computer software used to administer the scheme, including future upgrades and improvements

Regional Officer Group meetings - discussion group of principal officers from other administering authorities.

Policy on communication with tax payers

Our objectives with regard to communication with tax payers are:

- to provide access to key information in relation to the management of the scheme
- to outline the management of the scheme

Our objectives will be met by providing the following communications:

Method of Communication	Media	Frequency of Issue	Method of Distribution	Audience Group
Pension Fund Report and Accounts	Paper based and on website	Annually	Post	All, on request
Pension Fund Committee Papers	Paper based and on website	As and when available	Post	All, on request

Explanation of communications

Pension Fund Report and Accounts – details of the value of the Pension Fund during the financial year, income and expenditure as well as other related details, for example, the current employing authorities and scheme membership numbers.

Pension Fund Committee Papers - a formal document setting out relevant issues in respect of the LGPS, in many cases seeking specific decisions or directions from elected members.

Policy on communication with other stakeholders/interested parties

Our objectives with regard to communication with other stakeholder/interested parties are:

- to meet our obligations under various legislative requirements
- to ensure the proper administration of the scheme
- to deal with the resolution of pension disputes
- to administer the Fund's Additional Voluntary Contributions (AVC) scheme

Our objectives will be met by providing the following communications:

Method of Communication	Media	Frequency of Issue	Method of Distribution	Audience Group
Pension Fund valuation reports • Rates and Adjustments (R&A) certificates • Revised R&A certificates • Cessation valuations	Electronic	Every three years	Via email	Government Departments)/ Her Majesty's Revenue and Customs HMRC)/all Scheme employers
Details of new employers entered into the Fund	Hard copy	As new employers are entered into the Fund	Post	Government Departments /HMRC
Formal resolution of pension disputes	Hard copy or electronic	As and when a dispute requires resolution	Via email or post	Scheme member or their representative s, the Pensions Advisory Service/the Pensions Ombudsman
Completion of questionnaires	Electronic or hard copy	As and when required	Via email or post	Government Departments /HMRC/the Pensions Regulator

Explanation of communications

Pension Fund Valuation Reports – a report issued every three years setting out the estimated assets and liabilities of the Fund as a whole, as well as setting out individual employer contribution rates for a three year period commencing one year from the valuation date

Details of new employers – a legal requirement to notify both organisations of the name and type of employer entered into the Fund (i.e. following the admission of third party service providers into the scheme)

Resolution of pension disputes – a formal notification of pension dispute resolution, together with any additional correspondence relating to the dispute

Completion of questionnaires – various questionnaires that my received, requesting specific information in relation to the structure of the LGPS or the make up of the Fund

Performance Measurement

So as to measure the success of our communications with active, deferred and pensioner members, we will use the following methods:

Timeliness

We will measure against the following target delivery timescales:

Scheme booklet	New joiners to the LGPS	Within two months of joining	Within two weeks of joining the LGPS
Estimated Benefit Statements as at 31 March	Active members	On request	31 July each year
Telephone calls	All	Not applicable	95% of phone calls to be answered within 30 seconds
Issue of retirement benefits	Active and deferred members retiring	Within two months of retirement	95% of retirement benefits to be issued within 10 working days of retirement
Issue of deferred benefits	Leavers	Within two months of withdrawal	Within one month of notification
Transfers in	Joiners/active members	Within two months of request	Within one month of request
Issue of forms i.e. expression of wish	Active/deferred members	N/A	Within five working days
Changes to Scheme rules	Active/deferred and pensioner	Within two months of the change	Within one month of change coming

	members, as required	coming into effect	into effect
Annual Pension Fund Report and Accounts	All	Within two months of request	Within ten working days

Quality

Active and deferred members	Paper based survey with annual benefit statements	All services	
All member types	Annual paper based survey on completion of specific tasks	Service received during that task	One task to be chosen each quarter from: retirements new starts and transfers in transfers out deferred leavers
All member types	Focus group meeting on half yearly basis	All services and identify improvement areas/new services	Representative group of all member types. To include union representatives.
Employers	Focus Groups	Their issues	Regular feedback sessions.

Results

Details of the performance figures are reported to the Head of Pay, Pension, & e-HR on a quarterly basis. Feedback is received from the Service Head and from various focus /discussion groups.

Review Process

We will review our Communication Policy to ensure it meets audience needs and regulatory requirements at least annually. A current version of the Policy Statement will always be available on our intranet and paper copies will be available on request.

The London Borough of Tower Hamlets Pension Fund

Appendix 5

Governance Compliance Statement

Governance and Compliance Statement

The London Borough of Tower Hamlets Council is the Administering Authority of the London Borough of Tower Hamlets Pension Fund and administers the Local Government Pension Scheme on behalf of participating employers.

Regulation 55 of the Local Government Pension Scheme Regulations 2013 requires Local Government Pension Scheme (LGPS) Administering Authorities to publish Governance Compliance Statements setting out information relating to how the Administering Authority delegates its functions under those regulations and whether it complies with guidance given by the Secretary of State for Communities and Local Government. It also requires the Authority to keep the statement under to review and to make revisions as appropriate and where such revisions are made to publish a revised statement.

Aims and Objectives
Tower Hamlets Council recognises the significance of its role as Administering Authority to the London Borough of Tower Hamlets Pension Fund on behalf of its stakeholders which include:

- around 15,000 current and former members of the Fund, and their dependants
- over 20 employers within the Tower Hamlets Council area or with close links to Tower Hamlets Council
- the local taxpayers within the London Borough of Tower Hamlets.

In relation to the governance of the Fund, our objectives are to ensure that:

- all staff and Pensions Committee Members charged with the financial administration and decision-making with regard to the Fund are fully equipped with the knowledge and skills to discharge the duties and responsibilities allocated to them
- the Fund is aware that good governance means an organisation is open in its dealings and readily provides information to interested parties
- all relevant legislation is understood and complied with
- the Fund aims to be at the forefront of best practice for LGPS funds
- the Fund manages Conflicts of Interest appropriately

Structure
The Constitution of the Council sets out how the Council operates, how decisions are made and the procedures which are followed to ensure that these are efficient, transparent and that those who made the decisions are accountable to local people.
The Constitution sets out the framework under which the Pension Fund is to be administered as described below.

The Council delegates its responsibility for administering the Fund to the Pensions Committee. The terms of this delegation are as set out in the Council Constitution and provide that the Committee is responsible for consideration of all pension matters and discharging the obligations and duties of the Council under the Superannuation Act 1972 and various statutory matters relating to investment issues.

The governance structure is supported by:

- The Pensions Committee

- Officers of the Council; and
- Professional Advisors

Terms of Reference for the Pensions Committee

The Constitution allows for the appointment of a Pensions Committee which has responsibility for the discharge of all non-executive functions assigned to it.

The following are the terms of reference for the Pensions Committee:

To act as Trustees of the Council's Pension Fund, consider pension matters and meet the obligations and duties of the Council under the Superannuation Act 1972, the Public Service Pensions Act 2013, and other pension legislation.

1) To make arrangements for the appointment of and to appoint suitably qualified pension fund administrators, actuaries, advisers, investment managers and custodian's and periodically to review those arrangements.
2) To formulate and publish a Statement of Investment Principles.
3) To set the overall strategic objectives for the Pension Fund, having taken appropriate expert advice, and to develop a medium term plan to deliver the objectives.
4) To determine the strategic asset allocation policy, the mandates to be given to the investment managers and the performance measures to be set for them.
5) To make arrangements for the triennial actuarial valuation, to monitor liabilities and to undertake any asset/liability and other relevant studies as required.
6) To monitor the performance and effectiveness of the investment managers and their compliance with the Statement of Investment Principles.
7) To set an annual budget for the operation of the Pension Fund and to monitor income and expenditure against budget.
8) To receive and approve an Annual Report on the activities of the Fund prior to publication.
9) To make arrangements to keep members of the Pension Fund informed of performance and developments relating to the Pension Fund on an annual basis.
10) To keep the terms of reference under review.
11) To determine all matters relating to admission body issues.
12) To focus on strategic and investment related matters at two Pensions Committee meetings.
13) To review the Pension Fund's policy and strategy documents on a regular basis and review performance against the Fund's objectives within the business plan
14) To maintain an overview of pensions training for Members.

In addition the Pensions Committee will also co-opt a non-voting employer representative and a non-voting scheme member representative.

Membership of the Pensions Committee

The Council decides the composition and makes appointments to the Pensions Committee. Currently the membership of the Pensions Committee is a minimum of 7 elected Members from Tower Hamlets Council on a politically proportionate basis and the Pensions Committee will elect a Chair and Vice Chair. All Tower Hamlets Council elected Members have voting rights on the Committee and three voting members of the Committee are required to be able to deem the meeting quorate.

In addition there are two co-opted non-voting members representing employer and Scheme member interests. Although the co-opted representatives do not have voting rights they are treated as equal members of the Committee, they have access to all Committee Advisers, officers, meetings and training as if they were Council Members and have the opportunity to contribute to the decision making process.

Voting rights are restricted to elected Members as they are deemed to be fulfilling the role of Trustees as the Pension Fund with all the legal responsibilities that this entails, it was not felt appropriate to apply the same legal definition to the lay members of the Committee and hence their role as non-voting members.

Members of the Pensions Committee, including co-opted members, are required to declare any interests that they have in relation to the Pension Fund or items on the agenda at the commencement of the meeting.

The Fund is aware that good governance means an organisation is open in its dealings and readily provides information to interested parties; meetings are open to members of the public who are welcome to attend. However, there may be occasions when members of the public are excluded from meetings when it is likely in view of the nature of the business to be transacted or the nature of the proceedings that confidential information would be disclosed.

Meetings

The Pensions Committee shall meet at least four times a year in the ordinary course of business and additional meetings may be arranged as required to facilitate its work. Work for the year will be agreed with the Committee to include dedicated training sessions for Committee members.

Agendas for meetings will be agreed with the Chair and will be circulated with supporting papers to all members of the Committee, Officers of the Council as appropriate and the Fund's Investment Advisor.

The Council will give at least five clear working days' notice of any meeting by posting details of the meeting at the Tower Hamlets Town Hall and on the Council's website. The Council will make copies of the agenda and reports open to the public available for inspection at least five clear working days before the meeting. If an item is added to the agenda later, the revised agenda will be open to inspection from the time the item was added to the agenda. The reason for lateness will be specified in the report.

There may on occasions be items which may be exempt from the agenda, reports and minutes of the meetings when it is likely in view of the nature of the business to be transacted or the nature of the proceedings that confidential information would be disclosed. Items which are most likely to be excluded are issues where to disclose information would contravene an individual's privacy or where there are financial interests which may be compromised as a result of disclosure for example discussions surrounding contracts.

The Council will make available copies of the minutes of the meeting and records of decisions taken for six years after a meeting. Minutes of meetings and records of decisions are available for inspection on the Council's website:
http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392.

Other Delegations of Powers

The Pensions Committee act as quasi trustees and oversee the management of the Pension Fund. As quasi trustees the Committee has a clear fiduciary duty in the performance of their functions, they have to ensure that the Fund is managed in accordance with the regulations and to do so prudently and impartially and to ensure the best possible outcomes for the Pension Fund, its participating employers, local taxpayers and Scheme members. Whilst trustees can delegate some of their powers, they cannot delegate their responsibilities as trustees. Appendix B outlines the areas that the Pensions Committee has currently delegated though these may be added to from time to time.

Under the Council's Constitution delegated powers have been given to the Corporate Director of Resources in relation to all other pension fund matters, in addition to his role as Chief Financial Officer (often called S151 Officer). As Chief Financial Officer he is responsible for the preparation of the Pension Fund Annual Report & Accounts and ensuring the proper financial administration of the Fund. As appropriate the Corporate Director of Resources will delegate aspects of the role to other officers of the Council including the Investment & Treasury Manager and to professional advisors within the scope of the LGPS Regulations.

Pension Board

With effect from 1 April 2015, each Administering Authority is required to establish a local Pension Board to assist them with:

- securing compliance with the LGPS Regulations and any other legislation relating to the governance and administration of the Scheme, and requirements imposed in relation to the LGPS by the Pensions Regulator
- ensuring the effective and efficient governance and administration of the Pension Fund

Such Pension Boards are not local authority committees; as such the Constitution of Tower Hamlets Council does not apply to the Pension Board unless it is expressly referred to in the Board's terms of reference. The Tower Hamlets Pension Board established by Tower Hamlets Council and the full terms of reference of the Board can be found within the Council's Constitution. The key points are summarised below.

Role of the Pension Board

The Council has charged the Pension Board with providing oversight of the matters outlined above. The Pension Board, however, is not a decision making body in relation to the management of the Pension Fund and the Pension Fund's management powers and responsibilities which have been delegated by the Council to the Pensions Committee or otherwise remain solely the powers and responsibilities of them, including but not limited to the setting and delivery of the Fund's strategies, the allocation of the Fund's assets and the appointment of contractors, advisors and fund managers.

Membership of the Pension Board

The Pension Board consists of 7 members as follows:

- Three Employer Representatives
- Three Scheme Member Representatives
- One Independent Member (non-voting) to act as chair of the Pension Board

Pension Board members, (excluding any Independent Member), have individual voting rights but it is expected the Pension Board will as far as possible reach a consensus.

A meeting of the Pension Board is only quorate when two of the six Employer and Scheme Member Representatives are present, and where the Board has an Independent Member they must also be present.

Members of the Pension Board are required to declare any interests that they have in relation to the Pension Fund or items on the agenda at the commencement of the meeting.

Meetings

The Pension Board meets at least twice a year in the ordinary course of business and additional meetings may be arranged as required to facilitate its work. The Pension Board will be treated in the same way as a Committee of Tower Hamlets Council and, as such, members of the public may attend and papers will be made public in the same was as described above for the Pension Committee.

Policy Documents

In addition to the foregoing, there are a number of other documents which are relevant to the Governance and management of the Pension Fund. Brief details of these are listed below and the full copies of all documents can either be found on the Pension Fund Website http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392 or by writing to the address given at the end of this document.

Funding Strategy Statement

The Funding Strategy Statement forms part of the framework for the funding and management of the Pension Fund. It sets out how the Fund will approach its liabilities and contains a schedule of the minimum contribution rates that are required of individual employers within the Fund. The Funding Strategy Statement (FSS) is drawn up by the Administering Authority in collaboration with the Fund's actuary and after consultation with the Fund's employers. The FSS forms part of a broader framework which covers the Pension Fund and applies to all employers participating in the Fund. The FSS represents a summary of the Fund's approach to funding the liabilities of the Pension Fund.

Statement of Investment Principles

The Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 2009 require pension fund administering authorities to prepare,

maintain and publish a statement of the principles governing their decisions on the investment of the pension fund.
The areas covered in the statement of investment principles are as follows:

- Types of investments to be held.
- Balance between different types of investments.
- Risk.
- Expected return on investments.
- Realisation of investments.
- The extent to which social, ethical and environmental considerations are taken into account.
- The extent to which the Council complies with the 6 Myners principles of investment practice (2008).

Governance Compliance Statement
This sets out the Pension Fund's compliance with the Secretary of State's Statutory Guidance on Governance in the LGPS. This is attached as Appendix A and shows where the Fund is compliant or not compliant with best practice and the reasons why it may not be compliant.

Training Policy
Tower Hamlets Council has a Training Policy which has been put in place to assist the Fund in achieving its governance objectives and all Pensions Committee members, Pension Board members and senior officers are expected to continually demonstrate their own personal commitment to training and to ensuring that the governance objectives are met.
To assist in achieving these objectives, the London Borough of Tower Hamlets Pension Fund aims to comply with:

- the CIPFA Knowledge and Skills Frameworks and
- the knowledge and skills elements of the Public Service Pensions Act 2013 and
- the Pensions Regulator's (TPR) Code of Practice for Public Service Schemes.

As well as any other LGPS specific guidance relating to the knowledge and skills of Pensions Committee members, Pension Board members or pension fund officers which may be issued from time to time.

Members of the Pensions Committee, Pension Board and officers involved in the management of the Fund will receive training to ensure that they meet the aims of the Training Policy with training schedules drawn up and reviewed on at least on annual basis.

Annual Report and Accounts
As part of the financial standing orders it is the duty of the Chief Financial Officer to ensure that record keeping and accounts are maintained by the Pension Fund. The Pension Fund accounts are produced in accordance with the accounting recommendations of the Financial Reports of Pension Schemes - Statement of Recommended Practice. The financial statements summarise the transactions of the Scheme and deal with the net assets of the Scheme. The statement of accounts is reviewed by both the Pensions Committee and the Audit Committee and incorporated in the Statement of Accounts for the Council. Full copies of the Report and Accounts are distributed to employers in the Fund and other interested parties and a copy placed on the website http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392

Communication Policy
This document sets out the communications policy of the administering authority and sets out the strategy for ensuring that all interested parties are kept informed of developments in the Pension Fund. This helps to ensure transparency and an effective communication process for all interested parties. A copy of the policy can be found on the Pensions website http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392

Discretions Policies
Under the Local Government Pension Scheme regulations, the Administering Authority has a level of discretion in relation to a number of areas. The Administering Authority reviews these policies as appropriate and will notify interested parties of any significant changes. Employing Authorities are also required to set out their discretions policies in respect of areas under the Regulations where they have a discretionary power. Copies of both the Administering Authority and the London Borough of Tower Hamlets' Employing Authority Discretions can be found on the website: http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392

Pension Administration Strategy and Employer Guide
In order to assist with the management and efficient running of the Pension Fund, the Pension Administration Strategy and Employer Guide encompassing administrative procedures and responsibilities for the Pension Fund for both the Administering Authority and Employing Authorities has been distributed to employers within the Fund following consultation and can be found on the website
http://moderngov.towerhamlets.gov.uk/ieListMeetings.aspx?CommitteeId=392.

This represents part of the process for ensuring the ongoing efficient management of the Fund and maintenance of accurate data and forms part of the overall governance procedures for the Fund.

Approval, Review and Consultation
This Governance Policy and Statement was approved at the London Borough of Tower Hamlets Pensions Committee meeting on 23 July 2015 following consultation with all the participating employers in the Fund and other interested parties. It will be formally reviewed and updated at least every year or sooner if the governance arrangements or other matters included within it merit reconsideration.

Contact Information
Further information on the London Borough of Tower Hamlets Pension Fund can be found as shown below:
London Borough of Tower Hamlets Pension Fund
Mulberry Place
5 Clove Crescent
London
E14 2BG

Email: pensions@towerhamlets.gov.uk
Website: http://moderngov.towerhamlets.gov.uk/mgCommitteeDetails.aspx?ID=392

PRINCIPLE	REQUIREMENT	COMPLIANCE	COMMENT
STRUCTURE	The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing council	Compliant	The Council's Constitution states that the Pensions Committee is responsible for the management of the Pension Fund
	That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.	Compliant	Trade union representatives and representatives of admitted bodies sit on the Pension Committee.
	That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	Compliant	A report of the Pensions Committee is presented at the following Pensions Committee. All key recommendations of the Pensions Committee are ratified by the Pensions Committee.
	That where a secondary committee or panel has been established, at least one seat on the main committee is allocated for a member from the secondary committee or panel.	Compliant	All members of the Pensions Committee are also members of the Pensions Committee.
REPRESENTATION	That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include :- • employing authorities (including non-scheme employers, e.g. admitted bodies), • scheme members (including deferred and pensioner scheme members), • independent professional observers, • expert advisors (on an ad-hoc basis).	Compliant	Trade unions and admitted bodies are represented on the Pensions Committee.

PRINCIPLE	REQUIREMENT	COMPLIANCE	COMMENT
	That where lay members sit on a main or secondary committee, they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.	Compliant	Papers for Committee and the Pensions Committee are made available to all members of both bodies at the same time and are published well in advance of the meetings in line with the council's committee agenda publication framework.
SELECTION & ROLE OF LAY MEMBERS	That committee or panel members are made fully aware of the status, role and function they are required to perform on either a main or secondary committee.	Compliant	Members of the Pensions Committee/ Pensions Committee have access to the terms of reference of each body and are aware of their roles and responsibilities as members of these bodies/ Panel.
VOTING	The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	Compliant	The Pensions Committee/ Pensions Committee does not currently confer voting rights on non-Councillors in line with common practice across the local government sector.
TRAINING/FACILITY TIME/EXPENSES	That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.	Compliant	Regular training is arranged for members of the Pensions Committee. In addition members are encouraged to attend external training courses. The cost of any such courses attended will be met by the Fund.
	That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.	Compliant	The rule on training provision is applied equally across all members of the Pensions Committee.

PRINCIPLE	REQUIREMENT	COMPLIANCE	COMMENT
MEETINGS (FREQUENCY/ QUORUM)	That an administering authority's main committee or committees meet at least quarterly.	Compliant	Meetings of the Pensions Committee are arranged to take place quarterly.
	That an administering authority's secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committee sits.	Compliant	Meetings of the Pensions Committee are arranged to take place quarterly.
	That administering authorities who do not include lay members in their formal governance arrangements, provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.	Compliant	Union representatives on the Pensions Committee are lay members. Other stakeholders of the Fund are able to make representations at the Annual General Meeting of the Pension Fund.
ACCESS	That subject to any rules in the Council's Constitution, all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.	Compliant	Panel meeting papers are circulated at the same time to all members of the Pensions Committee/ Pensions Committee.
SCOPE	That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Compliant	Pensions Committee considers are range of issues at its meetings and therefore has taken steps to bring wider scheme issues within the scope of the governance arrangements.
PUBLICITY	That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements.	Compliant	This Governance Compliance Statement is a public document that is attached as an appendix to the annual pension fund report.

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Non-Executive Report of the: **Pensions Committee** 25th November 2015	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
Pension Fund Investment Performance Review for Quarter End 30 September 2015	

Originating Officer(s)	Bola Tobun, Investment & Treasury Manager
Wards affected	All wards

Summary

This report informs Members of the performance of the Fund and its investment managers for the quarter ending 30 September 2015.

For the quarter, the Fund underperformed the benchmark by -1.1%, delivering a negative absolute return of -4.0% against benchmark return of -2.9%.

The Fund is slightly behind its benchmark for the last twelve months to end of September 2015, the Fund returned 1.6%, and it's behind the benchmark by 0.7%.

For longer term performance the Fund outperformed the benchmark by posting three year returns of 8.3% ahead benchmark return of 7.9% and posted five year returns of 6.7% marginally behind benchmark return of 6.8%.

For this quarter end, four out of the eight mandates matched or achieved returns above the benchmark. The Fund performance being below the benchmark over the quarter was mainly due to poor returns from Ruffer, Baillie Gifford (DGF), GMO and Investec.
The Fund is still in line with its long term strategic equity asset allocation and the distribution of the Fund's assets amongst the different asset classes is broadly in line with the strategic benchmark weight.

Recommendations:

Members are recommended to note the contents of this report.

1. REASONS FOR THE DECISIONS

1.1 The report is written to inform committee members of the performance of pension fund managers and the overall performance of the Tower Hamlets Pension Fund.

2. ALTERNATIVE OPTIONS

2.1 The Pension Fund Regulations require that the Council establishes arrangements for monitoring the investments of the Pension Fund.

3. DETAILS OF REPORT

3.1 The Pension Fund Regulations require that the Council establish arrangements for monitoring the investments of the Fund. It considers the activities of the investment managers and ensures that proper advice is obtained on investment issues.

3.2 Officers and fund advisers meet regularly with investment managers to discuss their strategy and performance and may recommend that investment managers are invited to explain further to the Pensions Committee.

3.3 This report informs Members of the performance of the Fund and its investment managers for the quarter 30 September 2015.

3.4 Baillie Gifford & Co

3.4.1 Baillie Gifford manages two distinct mandates; global equity mandate and diversified growth fund mandate. The global equity fund had a value of £118.9m at the start of the mandate in July 2007. The market value of the assets as of 30 September 2015 was £189.3m. The performance target for this mandate is +2% to 3% above the benchmark MSCI AC World Index gross of fees over a rolling 3-5 year periods.

3.4.2 The diversified growth fund mandate was opened in February 2011 with contract value of £40m. £6.409m was added to this portfolio during the month of June 2015. The market value of assets as at 30 September 2015 was £55.5m. The performance target for this mandate is to outperform the benchmark (UK base rate) net of fees over rolling 5 years with annual volatility of less than 10%.

3.5 GMO

3.5.1 GMO manages a Global Equity Mandate which at 30 September 2015 had a market value of £226.6m. On 25 November 2014, £20.8m was redeemed from the portfolio; further £10.674 was redeemed from the portfolio on 29 May 2015 in order to keep the strategic asset allocation weight in line with the investment policy. The initial value of assets taken on at the commencement (29 April 2005) of the contract was £201.8m.

3.5.2 The performance target is to outperform a balanced global equity benchmark by 1.5% per annum net of fees over a rolling three year period.

3.6 Investec Asset Management

3.6.1 Investec manages a Global Bond Mandate which at 30 September 2015 had a market value of £98.7m. The initial value of the assets taken on at the commencement (26 April 2010) of the contract was £97m.

3.6.2 The performance target is to outperform the benchmark (3 Month LIBOR) by 2.0% per annum net of fees over a rolling three year period.

3.7 Legal & General Investment Management

3.7.1 Legal & General was appointed (2 August 2010) to manage passively UK Equity and UK Index-Linked Mandates, which at 30 September 2015 had a market value of £221.8m. The value of the assets taken on at the commencement of the contract was £204.7m.

3.7.2 The performance target is to track the FTSE All Share index for the UK Equity mandate and FTSE A Gov Index-Linked > 5 years benchmark for the UK Index-Linked Mandates.

3.8 Ruffer Investment Management

3.8.1 Ruffer manages an Absolute Return Fund; the value of this contract on the 28 February 2011 was £40m. £6.474m was added to this portfolio on 02 June 2015. The value of assets under management as of 30 September 2015 was £53.6m.

3.8.2 Their overall objective is firstly to preserve the capital over rolling 12 month periods and secondly to grow portfolio at a higher rate after fees than could reasonably be expected from the alternative of depositing the cash value of the portfolio in a reputable UK bank.

3.9 Schroder Investment Management

3.9.1 Schroder manages a property mandate. The value of this mandate on 20 September 2004 was £90m. The market value of assets at 30 September 2015 was £125.6m.

3.9.2 The performance target for this mandate is to outperform the IPD UK Pooled Property Fund Indices All Balanced Funds Median by 0.75% net of fees over a rolling three year period.

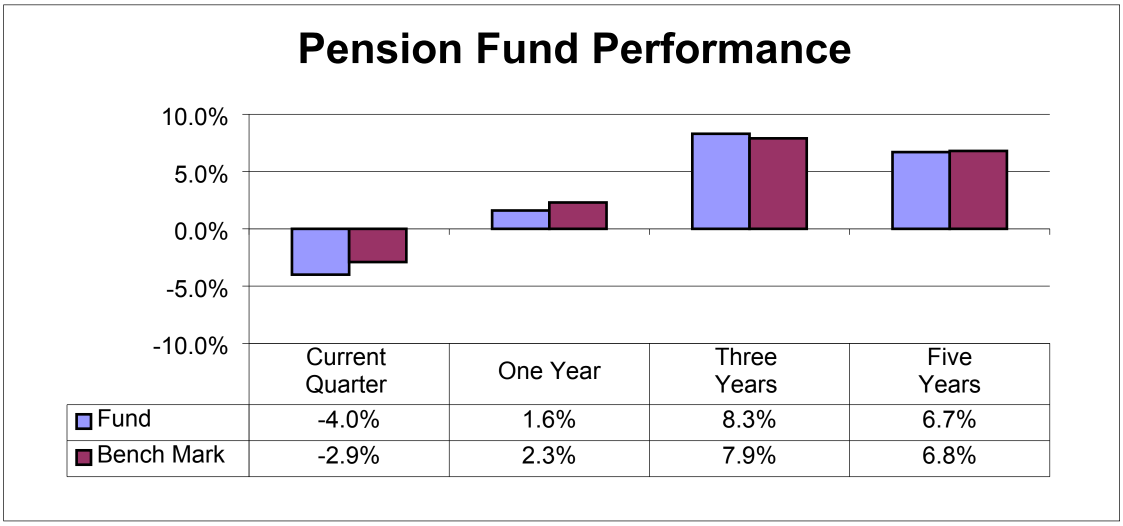
3.10. INVESTMENT PERFORMANCE

3.10.1 The Fund's overall value has reduced by £44m from £1,115.6m as of 30 September 2015 to £1,071.6m as of 30 September 2015.

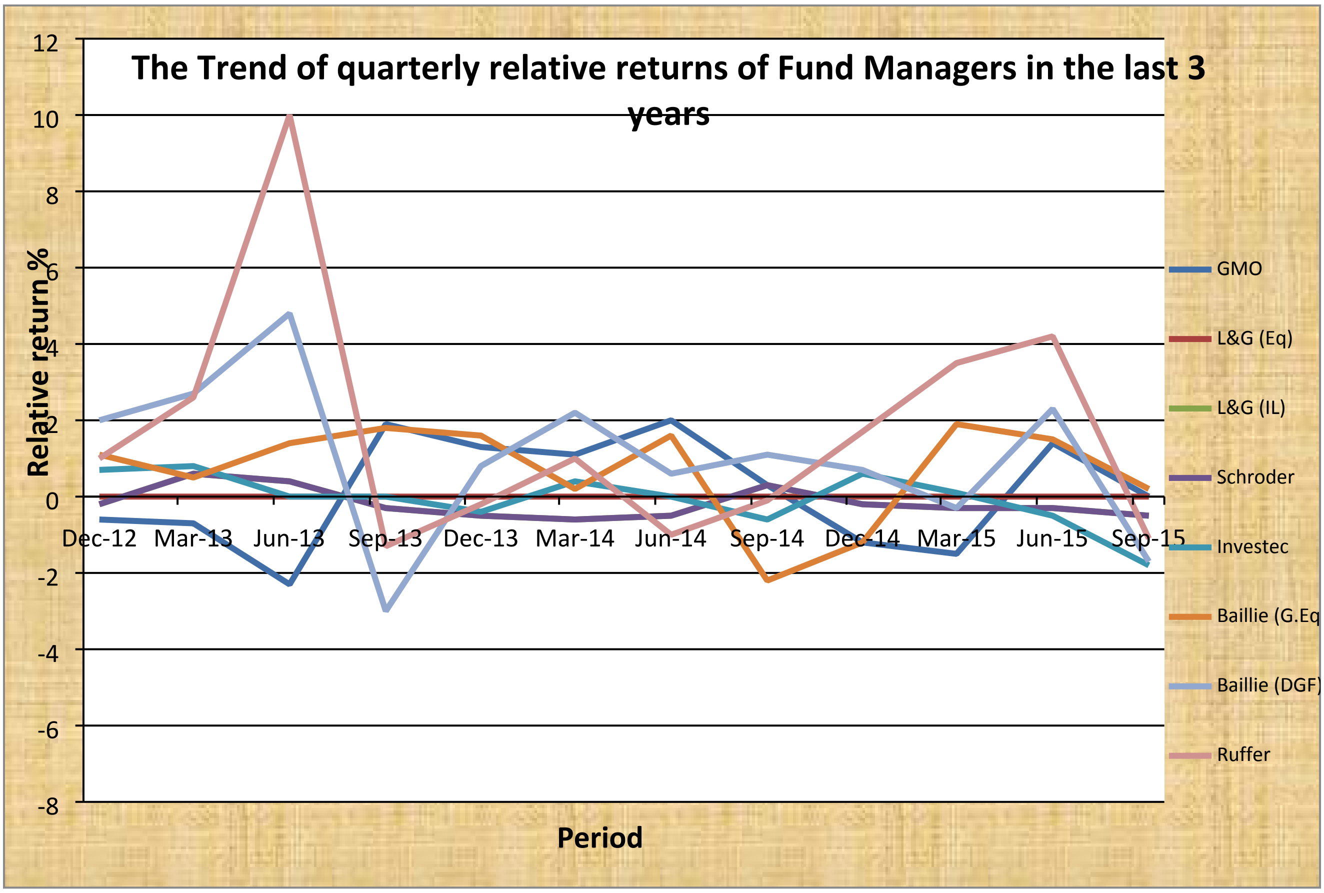
3.10.2 The fund underperformed the benchmark this quarter with a return of -4.0% compared to the benchmark return of -2.9%. The twelve month period sees the fund underperforming the benchmark by 0.7%.

3.10.3 The performance of the fund over the longer term is as set out in the chart below.

Table 1 – Pension Fund Performance



3.10.4 The graph below demonstrates the volatility and cyclical nature of financial markets, but the outcomes are within the range of expectations used by the Fund actuary in assessing the funding position. The Fund can take a long term perspective on investment issues principally because a high proportion of its pension liabilities are up to sixty years in the future.



3.11 MANAGERS

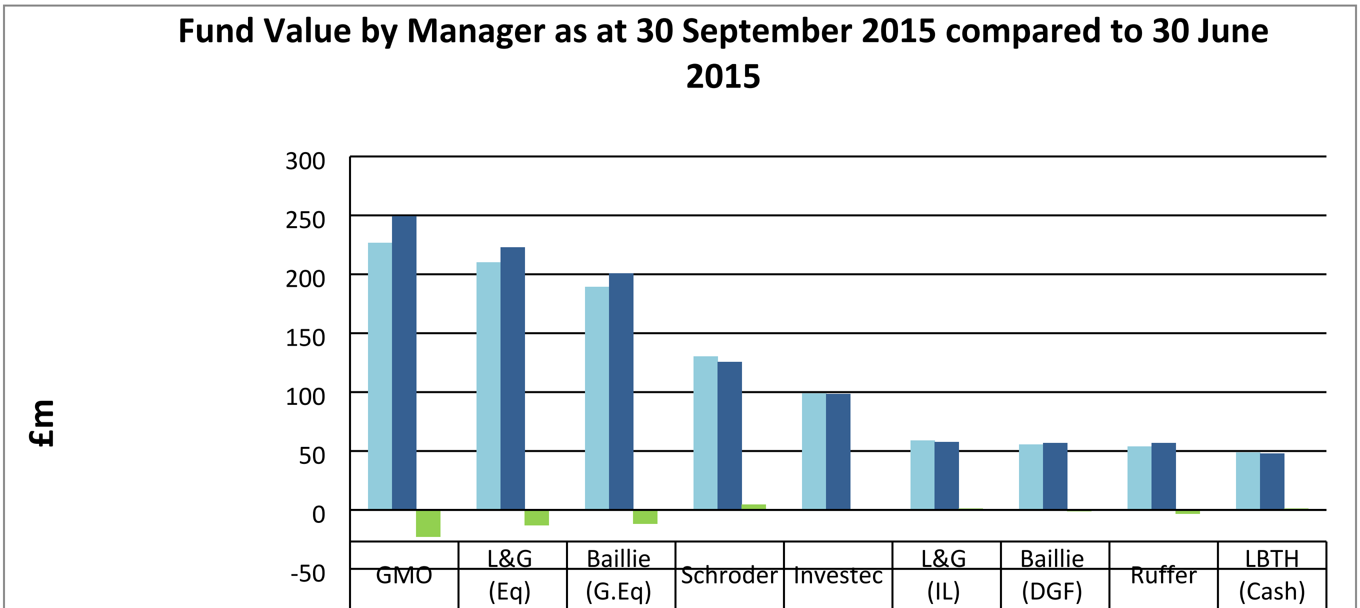
3.11.1 The Fund employs six specialist managers with eight mandates. The managers, mandate and funds held under management are set out below:

Table 2: Management Structure

Manager	Mandate	Value £M	Target % of Fund	Actual % of Fund	Difference %	Date Appointed
GMO	Global Equity	226.6	23.0%	21.1%	-1.9%	29 Apr 2005
Baillie Gifford	Global Equity	189.3	18.0%	17.7%	-0.3%	5 Jul 2007
L & G UK Equity	UK Equity	210.0	20.0%	19.6%	-0.4%	2 Aug 2010
Baillie Gifford Diversified Growth	Absolute Return	55.5	5.0%	5.2%	0.2%	22 Feb 2011
Ruffer Total Return Fund	Absolute Return	53.7	5.0%	5.0%	0.0%	8 Mar 2011
L & G Index Linked-Gilts	UK Index Linked	58.9	3.0%	5.5%	2.5%	2 Aug 2010
Investec Bonds	Bonds	98.7	14.0%	9.2%	-4.8%	26 Apr 2010
Schroder	Property	130.1	12.0%	12.1%	0.1%	30 Sep 2004
Cash	Internal cash management	48.8	0.0%	4.6%	4.6%	
Total		**1,071.6**	**100.0%**	**100.0%**	**0.0%**	

3.11.2 The Fund was valued at £1,071.6million as at 30 September 2015. This includes cash held and being managed internally (LBTH Treasury Management), this stands at 4.6% of the total assets value.

3.11.3 Market performance for the quarter is illustrated below by depicting the fund value by manager for this reporting quarter compared to the last quarter.



	GMO	L&G (Eq)	Baillie (G.Eq)	Schroder	Investec	L&G (IL)	Baillie (DGF)	Ruffer	LBTH (Cash)
Value at 30/09/2015	226.6	210.0	189.3	130.1	98.7	58.9	55.5	53.7	48.8
Value at 30/06/2015	249.2	222.8	200.8	125.6	98.4	57.6	56.7	56.8	47.7
Gain/(Loss) in Value	(22.6)	(12.8)	(11.5)	4.50	0.30	1.30	(1.2)	(3.1)	1.10

3.11.4 The performance, gross of fees of the individual managers relative to the appropriate benchmarks over the past five years is as set out in table 3.

Table 3: Manager Investment Performance relative to benchmark

Manager	Current Quarter	One Year	Three Years	Five Years
GMO Global Equities	-3.10%	-3.70%	-0.60%	-0.60%
Baillie Gifford Global Equities	0.10%	3.70%	2.6%	1.70%
L & G UK Equity	0.00%	0.00%	0.10%	0.10%
Baillie Gifford Diversified Growth	-3.00%	-2.80%	0.70%	N/A
Ruffer Total Return Fund	-6.10%	0.20%	3.10%	N/A
L & G Index Linked-Gilts	0.00%	0.00%	0.00%	0.00%
Investec Bonds	-0.50%	-2.80%	-1.70%	-2.10%
Schroder	0.60%	-0.50%	-0.50%	-0.60%
Total Variance (Relative)	**-0.50%**	**0.20%**	**0.70%**	**0.20%**

3.12 **GMO** - The portfolio performed discouragingly by posting a massive negative return of 9.0% against a target return of -5.9% over the quarter

3.12.1 The Emerging Markets overweight accounts for the majority of the underperformance in this reporting quarter. The underweight position of the portfolio to the US also hurt relative performance, although this was counterbalanced by strong stock selection in the US.

3.12.2 Stock selection in the rest of the portfolio was detrimental, driven by the holdings in Canada, France and Germany. From a sector perspective, the overweight to Energy was a drag on performance as was stock selection in IT, Utilities and Healthcare.

3.12.3 Global equities generally posted strong negative returns in U.S. dollar terms during the reporting quarter. Few markets were safe from the escalating concerns about a global growth slowdown.

3.12.4 Unexpected currency devaluation and weak economic signs from China, weakening commodity prices, and guessing how and when the Fed would actually take action all helped to pull the bottom out from under the equity markets. MSCI ACWI fell by 9.4%.

3.12.5 Regional performance was negative with the S&P 500 down 6.4%, MSCI Europe down 8.7% and MSCI Japan down 11.8%. Emerging equities bore the brunt of the impact from heightened concerns about China and the extent of any contagion. MSCI Emerging Markets fell by 17.9%.

3.13 **Baillie Gifford** – the portfolio slightly outperformed the benchmark of -5.9% over the quarter, delivering a return of -5.8% resulting in relative outperformance of 0.1%. The portfolio is relatively concentrated and seeks to generate strong absolute returns over the long-term through the use of an unconstrained bottom-up approach. The portfolio also delivered on this over the longer term, as performance remains ahead of the benchmark over 3 years and 5 years.

3.13.1 One of the largest contributors to performance was Royal Caribbean Cruises, Ryanair, Amazon and Naspers. These companies have seen significant price appreciation over the past year.

3.13.2 Within all of its portfolios, Baillie Gifford has had a notable overweight to consumer discretionary and technology/internet retailing stocks which have benefitted returns greatly in the past.

3.13.3 At stock level, contributors included Royal Caribbean Cruises, Ryanair and Amazon, whilst Baidu, Alibaba, Inpex and Ultra Petroleum detracted.

3.14 **Legal & General - L & G (UK Equity)** – The portfolio returned -5.7% matching the index return over the quarter.

3.14.1 At the quarterly review Sophos Group, PureTech Health and Kainos Group were added to the index. No deletions were made. Acquisitions for cash by non-index constituents were: TSB Banking Group by Banco de Sabadell (Spain), CSR by Qualcomm (USA), Anite by Keysight Technologies (USA) and Colt Group by Lightening Investors (USA).

3.14.2 HMRC sold down stakes in Royal Bank of Scotland and Lloyds Banking Group, resulting in holdings of 73% and 13% respectively. Capital raisings for acquisitions and growth were made by Renewables Infrastructure Group, P2P Global Investments, Britvic, GKN, Ladbrokes, Woodford Patient Capital and VPC Specialty Lending Investments. Raisings for debt repayments included Glencore, Empiric Student Property and NextEnergy Solar Fund.

3.15 **L & G Index Linked Gilts** – The portfolio returned 2.3% matching the index return over the quarter.

3.15.1 The UK economy continues to rove along nicely, with RPI inflation only edging up slightly in August to 1.1% year-on-year and preliminary estimates of Q3 GDP falling only modestly to 2.6%. The UK base rate remains at 0.5%, but the time is fast approaching for lift off, particularly if the US Federal Reserve decides to raise US rates this year

3.15.2 During the quarter there were two auctions and a single syndication. The auctions were used to tap the existing 2058 maturity bond as the DMO looks to build this to benchmark weight. A second auction was held to launch a brand new 10-year 2026 maturity bond. The syndication was held to tap the ultra-long 2068 maturity bond; these operations collectively raised approximately £7bn for government funding.

3.15.3 The Fund held all 22 stocks contained within the benchmark index. The Fund and index had a modified duration of 23.93 years at the end of the quarter and the real yield was -0.83% (yield curve basis).

3.15.4 **Investec (Bonds)** – The portfolio delivered a return of 0.10% against a performance comparison index return of 0.6%. The currency management added strongly to relative returns, this was more than offset by the combined effect of the other risk exposures detracting. However, the underperformance was marginal, reflective of the fairly limited drawdown from each of the other detractors individually.

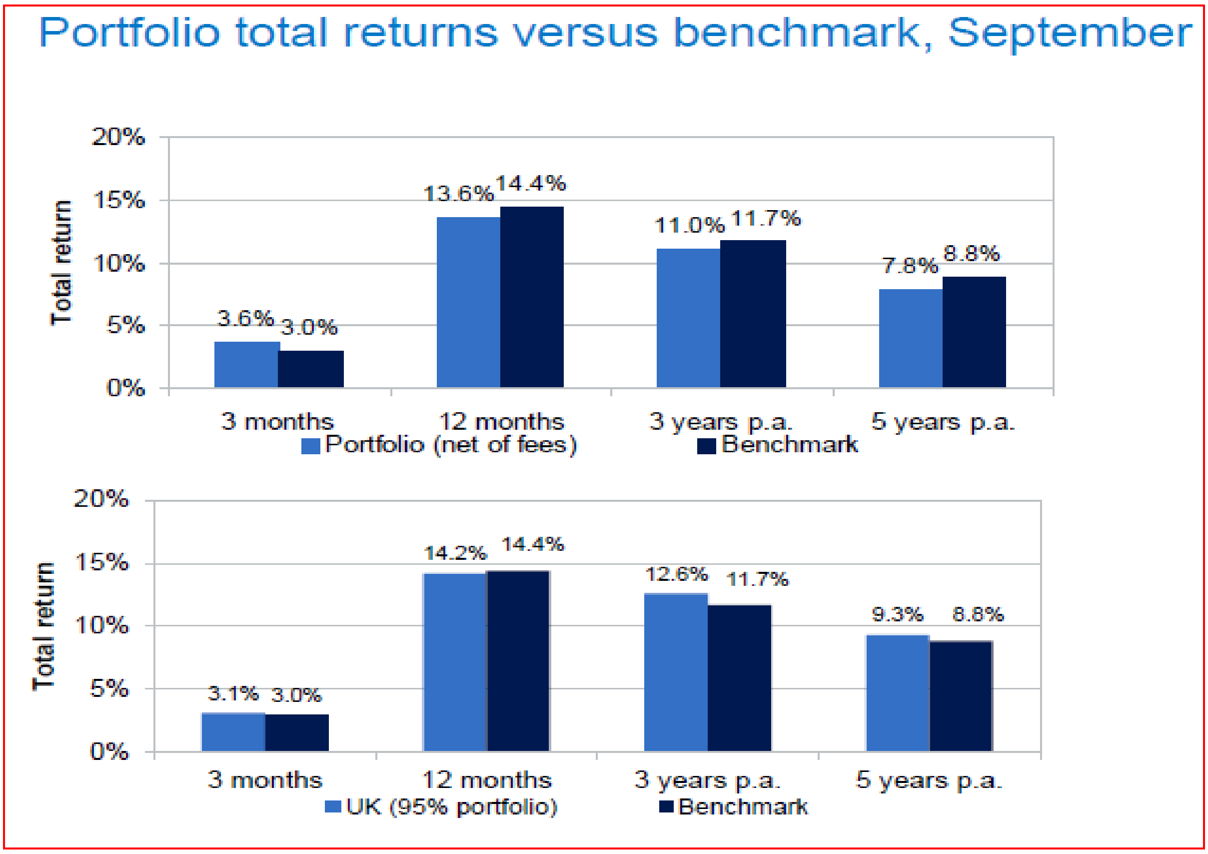
3.15.5 A key component of the contribution from the currency management was the long-held, strategic position in the US dollar which once again rallied after a weaker second quarter. The dollar benefited from the wave of risk aversion from investors, and the decision by the US Federal Reserve (Fed) to keep rates on hold did not lead to any material depreciation.

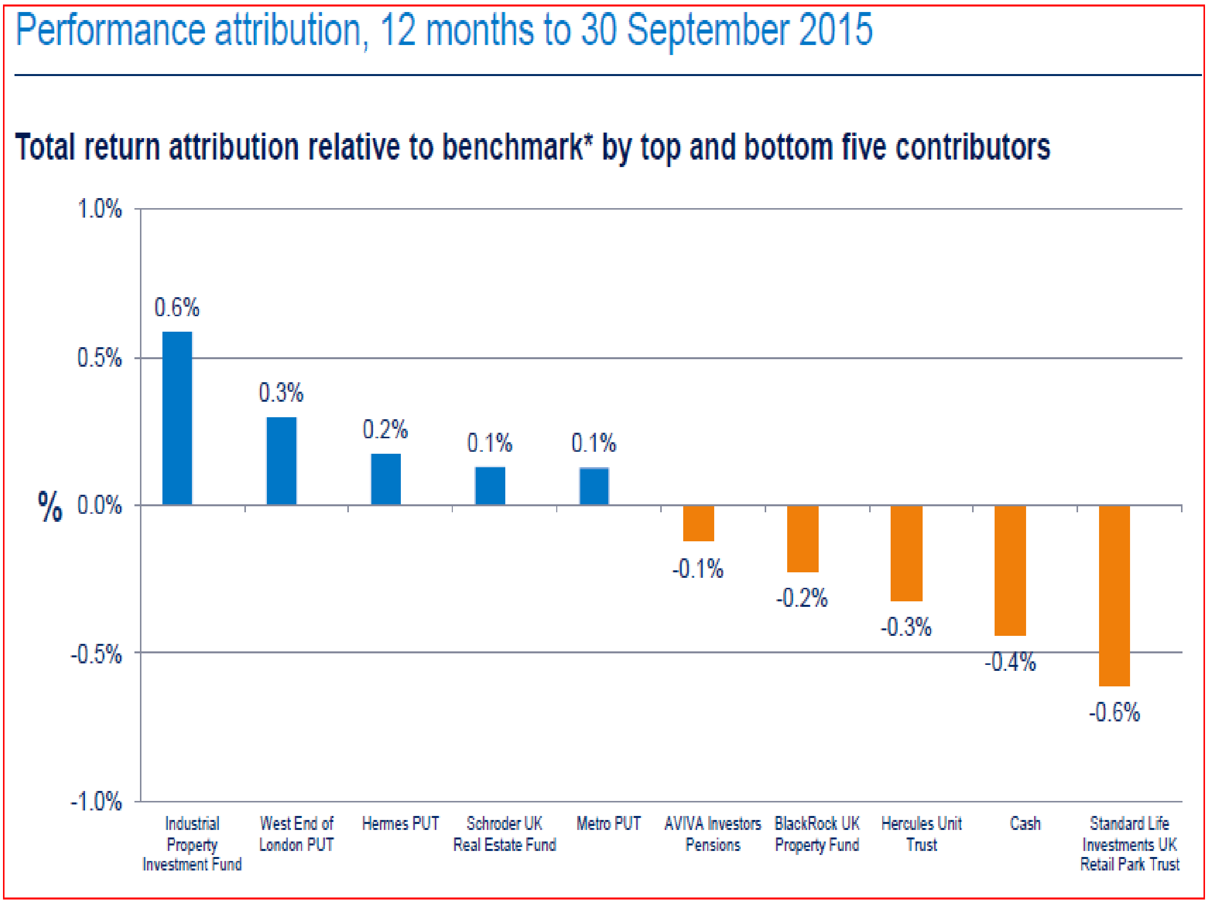
3.16 **Schroder (Property) –** The portfolio outperformed the benchmark over the quarter by +0.6%, although the longer term performance continues to lag the benchmark; with an underperformance 0.6% p.a. over the 5 years to 30 September 2015.

3.16.1 The Continental European Fund 1 (CEF 1) (5% of portfolio) made the strongest contribution to performance over the quarter delivering an absolute return of 31.1%. CEF 1's performance was boosted by the timing of a distribution that occurred in the last quarter but was not booked until this quarter.

3.16.2 Capital appreciation and a favourable currency movement also made a positive contribution to returns. Metro PUT and Mayfair Capital PUT were amongst the top performing strategies.

3.16.3 Please see below graphs which show the performance in detail.





3.17 **Baillie Gifford Diversified Growth Fund** generated a return of -2.1% for the quarter, underperformed the benchmark of 1.0% by -3.1%.

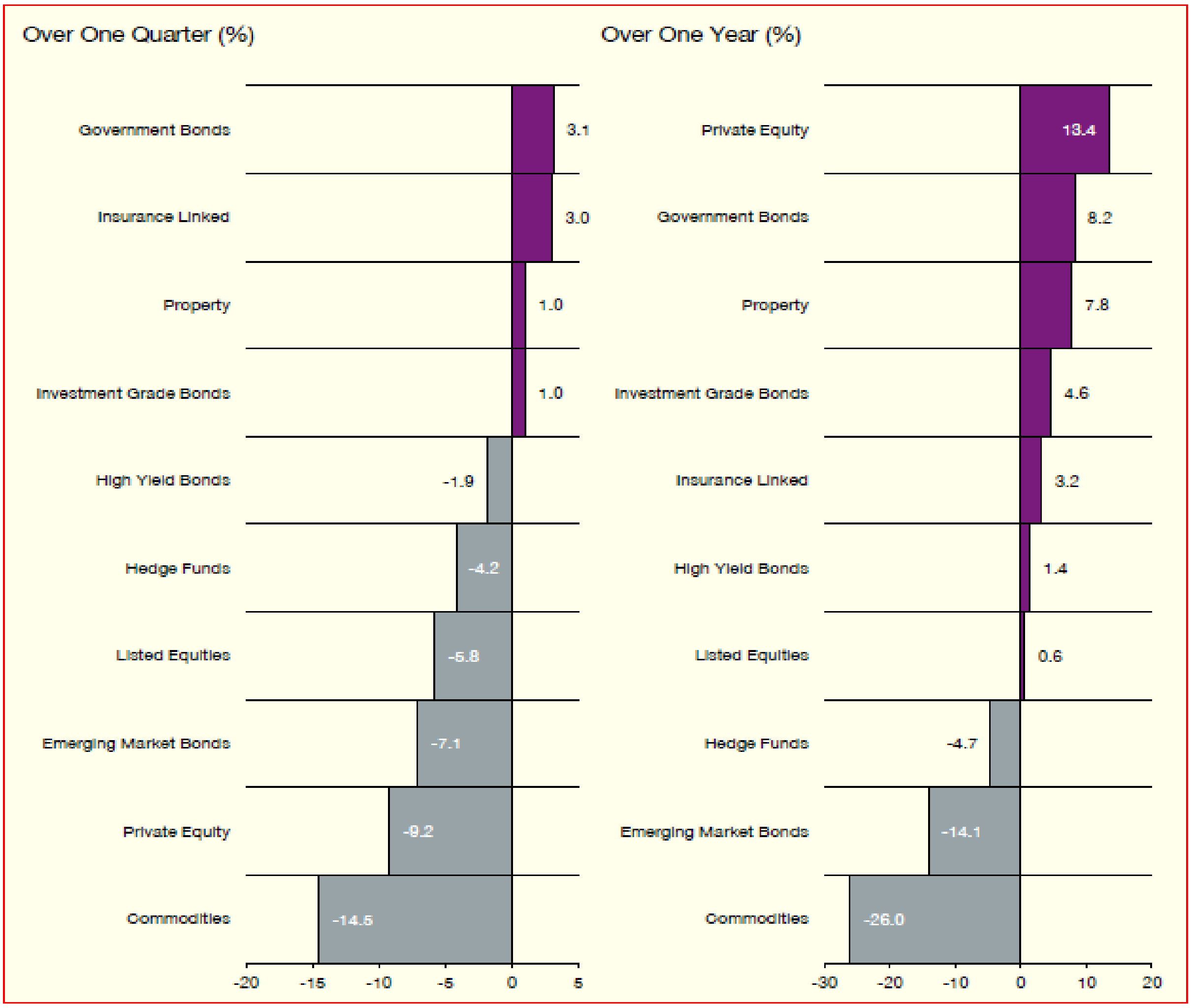
3.17.1 The large weightings in listed equities, emerging market bonds and high yield credit, all of which sold off during the period, were the largest negative contributors to performance. However, the diversified nature of the Fund meant that a number of asset classes with low correlation to equity markets provided some protection, among them active currency, absolute return and insurance linked securities.

3.17.2 Within active currency, the short positions in a number of emerging market currencies, such as the Malaysian ringgit and South African rand were helpful. Within absolute return, the trend-following funds continued to benefit from a lower oil price and strong government bond performance.

3.17.3 This latest quarter has been a relatively challenging period, but the Fund's ability to invest in a broad range of assets means that overall performance held up better than investing solely in equities.

3.17.4 The long term performance - The last 12 months to 30 September 2015, the portfolio return was 1.1%, lagging the benchmark return of 4.0% by 2.9% and the last 3 years return was 0.7% above the benchmark return of 4.0%.

3.17.5 Please see below charts which illustrate contributions to performance per asset class for the quarter end and 12 months to 30 September 2015.



3.18 **Ruffer Total Return Fund (Absolute Return)** – The portfolio performed discouragingly by posting a massive negative return of 5.5% against a target return of 0.6% over the quarter.

3.18.1 **Index-linked gilts** - UK index-linked helped as yields fell on rising fear; however US inflation-linked treasuries did not. US real yields rose in the face of the potential September interest rate rise, which ultimately didn't materialise.

3.18.2 Ruffer Illiquid Multi Strategies Fund, this new vehicle performed as intended against the correlated fall in equity and bond markets. Its investments in credit default swaps benefited as spreads on corporate bonds rose to reflect risks in those markets.

3.18.3 **Japan equities** - with turmoil emanating from China, Japan was an easier, liquid proxy by which to sell Asian exposure. The portfolio's holdings in financial stocks were especially hard hit.

3.18.4 Options VIX call options provided strong protection in August; the manager took some profit, but the position held over into September in case of further stress was lost as market volatility subsided.

3.18.5 Volkswagen – the manager sold the portfolio's position as soon as the emissions scandal erupted. While this crystallised a loss, at the end of reporting quarter, the share price is now 25% lower.

3.18.6 The long term performance, are ahead of the benchmark. The last 12 months are ahead by 0.2% and the last 3 years by 3.1% above the benchmark returns.

3.19 Internal Cash Management

3.19.1 Cash is held by the managers at their discretion in accordance with limits set in their investment guidelines, and internally by LBTH to meet working cash flows requirements, although transfers can be made to Fund managers to top up or rebalance the Fund.

3.19.2 The Pension Fund invests in accordance with the Council's Treasury Management strategy agreed by Full Council in February 2015, which is delegated to the Corporate Director of Resources to manage on a day to day basis within set parameters.

3.19.3 The cash balance as at 30 September 2015, was £48.8m. This constitutes £15m internal cash flow balance from 2013/14, £25m redeemed from GMO portfolio between November 2014. In addition to current internal cash balance of £8.8m as at 30 September 2015. £45m of this cash is cash awaiting investment into fixed income mandate.

3.19.4 Members will continue to be updated quarterly of the Pension Fund in house cash investment strategy. Security of the Fund's cash remains the overriding priority, ahead of yield.

3.21 ASSET ALLOCATION

Allocations are therefore considered to be broadly in line with the benchmark. Individual managers have discretion within defined limits to vary the asset distribution. The overweight position in equities has helped the fund's performance in recent months

The benchmark asset distribution and the fund position at 30 September 2015 are as set out below:

Table 4: Asset Allocation

Asset Class	Benchmark	Fund Position as at 30 September 2015	Variance as at 30 September 2015
UK Equities	24.0%	19.6%	-4.4%
Global Equities	37.0%	38.8%	1.8%
Total Equities	**61.0%**	**58.4%**	**-2.6%**
Property	12.0%	12.1%	0.1%
Bonds	14.0%	9.2%	-4.8%
UK Index Linked	3.0%	5.5%	2.5%
Alternatives	10.0%	10.2%	0.2%
Cash	0.0%	4.6%	4.6%
Currency	0.0%	0.0%	0.0%
Total Equities	**100.0%**	**100.0%**	

3.21.1 The original allocation of investments between the different asset classes was determined in conjunction with the Council's professional advisors in 2004 and is subject to periodic review by the Investment Panel – the latest review was carried out in January 2014.

Asset allocation is determined by a number of factors including:-

- The risk profile. Generally there is a trade-off between the returns obtainable on investments and the level of risk. Equities have higher potential returns but this is achieved with higher volatility. However, as the Fund remains open to new members and able to tolerate this it can seek long term benefits of the increased returns.
- The age profile of the Fund. The younger the members of the Fund, the longer the period before pensions become payable and investments have to be realised for this purpose. This enables the Fund to invest in more volatile asset classes because it has the capacity to ride out adverse movements in the investment cycle.
- The deficit recovery term. All Council funds are in deficit because of falling investment returns and increasing life expectancy. The actuary determines the period over which the deficit is to be recovered and considers the need to stabilise the employer's contribution rate. The actuary has set a twenty year deficit recovery term for this Council which enables a longer term investment perspective to be taken.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 The comments of the Corporate Director Resources are incorporated in the report

5. LEGAL COMMENTS

5.1 Regulation 11(3) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 requires the Council, as an administering authority, to invest fund money that is not needed immediately to make payments from the Pensions Fund. Regulation 11(1) requires the Council to have a policy in relation to its investments. The investment policy should cover the following matters:

(a) the advisability of investing money in a wide variety of investments; and

(b) the suitability of particular investments and types of investments. The Council is also required to have a Statement of Investment Principles in accordance with regulation 12 (1) which cover the following matters:

(a) the types of investment to be held;

(b) the balance between different types of investments;

(c) risk, including the ways in which risks are to be measured and managed;

(d) the expected return on investments;

(e) the realisation of investments;

(f) the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments;

(g) the exercise of the rights (including voting rights) attaching to investments, if the authority has any such policy; and

(h) stock lending.

5.2 The Council must take proper advice at reasonable intervals about its investments and must consider such advice when taking any steps in relation to its investments.

5.3 The Council does not have to invest the fund money itself and may appoint one or more investment managers. Where the Council appoints an investment manager, it must keep the manager's performance under review. At least once every three months the Council must review the investments that the manager has made and, periodically, the Council must consider whether or not to retain that manager.

5.4 One of the functions of the Pensions Committee is to meet the Council's duties in respect of investment matters. It is appropriate, having regard to these matters, for the Committee to receive information about asset allocation and the performance of appointed investment managers. The Committee's consideration of the information in the report contributes towards the achievement of the Council's statutory duties.

5.5 When reviewing the Pension Fund Investment Performance, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don't (the public sector duty). The Committee may take the view that good, sound investment of the Pension Fund monies will support compliance with the Council's statutory duties in respect of proper management of the Pension Fund.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The employer's contribution is a significant element of the Council's budget and consequently any improvement in investment performance will reduce the contribution and increase the funds available for other corporate priorities.

6.2 A viable pension scheme also represents an asset for the recruitment and retention of staff to deliver services to the residents.

7. BEST VALUE (BV) IMPLICATIONS

7.1 This report helps in addressing value for money through benchmarking the Council's performance against the WM Local Authority Universe of Funds.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There is no Sustainable Action for A Greener Environment implication arising from this report.

9. RISK MANAGEMENT IMPLICATIONS

9.1 Any form of investment inevitably involves a degree of risk.

9.2 To minimise risk the Investment Panel attempts to achieve a diversification portfolio. Diversification relates to asset classes and management styles.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report

- [None]

Appendices

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report
Investment Managers Quarterly reports (Investec, GMO, Schroder, Baillie Gifford, LGIM and Ruffer) and WM Quarterly Performance Review. (To be email if required)

Officer contact details for documents:

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