TOWER HAMLETS

PENSIONS COMMITTEE

Wednesday, 7 December 2016 at 6.00 p.m.

Idea Store Canary Wharf, Churchill Place, London E14 5RB

This meeting is open to the public to attend.

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

Councillor Gulam Kibria Choudhury, Councillor Md. Maium Miah, Councillor Abdul Mukit MBE, Councillor Candida Ronald and Councillor Andrew Wood

Tony Childs (Co-optee Admitted Bodies Representative) and Kehinde Akintunde (Unions Representative)

Substitutes:
Councillor Marc Francis, Councillor Ayas Miah and Councillor Rajib Ahmed

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

Contact for further enquiries:
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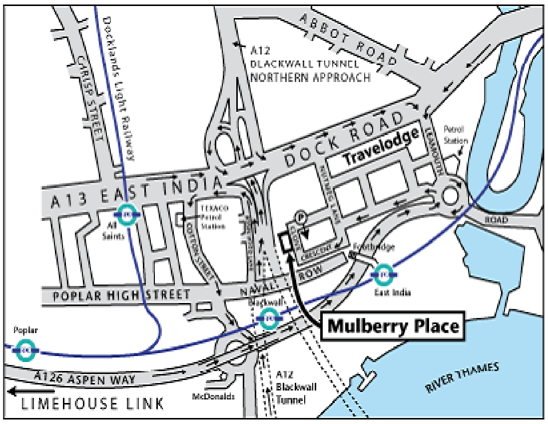

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		PAGE NUMBER(S)
	APOLOGIES FOR ABSENCE	
1.	**DECLARATIONS OF DISCLOSABLE PECUNIARY INTEREST (Pages 1 - 4)**	
	To note any declarations of interest made by Members, including those restricting Members from voting on the questions detailed in Section 106 of the Local Government Finance Act, 1992. See attached note from the Monitoring Officer.	
2.	**MINUTES OF THE PREVIOUS MEETING(S) (Pages 5 - 10)**	
	To confirm as a correct record the minutes of the meeting of the Committee held on 22 September 2016.	
3.	**PETITIONS**	
	To receive any petitions relating to matters for which the Committee is responsible.	
4.	**SUBMISSIONS / REFERRALS FROM PENSION BOARD**	
5.	**REPORTS FOR CONSIDERATION**	
5 .1	**Presentation from Divest Tower Hamlets**	
5 .2	**Presentation by Paul Spedding from Carbon Tracker**	
5 .3	**Presentation by Clifford Sims (Partner, Squire, Patton, Boggs (LLP)**	
5 .4	**Presentation by Ian Williams (151 Hackney)**	
6.	**EXAMINATION OF APPROACHES FOR MANAGING FOSSIL FUELS AND CLIMATE CHANGE ISSUES AS PART OF THE FUND ETHICAL, SOCIAL AND GOVERNANCE (ESG) POLICY**	**11 - 22**
7.	**TRIENNIAL VALUATION- INITIAL RESULTS AND PUBLIC SERVICE PENSIONS ACT- SECTION 13 VALUATION**	**23 - 90**

8.	**VERBAL UPDATE ON MARKET OUTLOOK AND INVESTMENT BY THE INDEPENDENT ADVISOR**	
9.	**INVESTMENT PERFORMANCE REVIEW FOR QUARTER END 30 SEPTEMBER 2016**	**91 - 106**
10.	**2015/16 PENSION FUND ANNUAL REPORT AND AUDIT REPORT (ISA 260 REPORT)**	**107 - 324**
11.	**ADMISSION OF ENERGY KIDZ INTO THE LONDON BOROUGH OF TOWER HAMLETS PENSION FUND**	
12.	**TRAINING EVENTS**	
13.	**ANY OTHER BUSINESS CONSIDERED TO BE URGENT**	

14. 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.

14 .1 Maximum Deficit Recovery Period for Academies (To follow)

14 .2 London Collective Investment Vehicle (CIV) and FCA MiFID II

Next Meeting of the Committee:
Thursday, 16 March 2017 at 7.00 p.m. to be held in Room C1, Town Hall, Mulberry Place, 5 Clove Crescent, London E14 2BG.

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, Corporate 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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LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE PENSIONS COMMITTEE

HELD AT TIME NOT SPECIFIED ON THURSDAY, 22 SEPTEMBER 2016

MP702, 7TH FLOOR TOWN HALL, MULBERRY PLACE, 5 CLOVE CRESCENT, LONDON E14 2BG

Members Present:

Councillor Andrew Cregan (Chair)
Councillor Clare Harrisson (Vice-Chair)
Councillor Gulam Kibria Choudhury
Councillor Abdul Mukit MBE
Councillor Candida Ronald
Councillor Andrew Wood

Union and Admitted Bodies, Non-Voting Members Present:

–

Other Councillors Present:

Apologies:

Kehinde Akintunde
Councillor Md. Maium Miah

Others Present:

–

Officers Present:

Ngozi Adedeji	– (Team Leader Housing Services, Legal Services, Law Probity & Governance)
Kevin Miles	– (Chief Accountant, Resources)
Bola Tobun	– (Investments and Treasury Manager, Resources)
Nishaat Ismail	–

1. DECLARATIONS OF DISCLOSABLE PECUNIARY INTEREST

None declared.

2. MINUTES OF THE PREVIOUS MEETING(S)

The Pensions Committee minutes of the 30th June 2016 were approved as a correct record of proceedings with the following amendments;

- Ngozi Adedeji, requested the minutes of the Pensions Committee on the 30th June be amended to reflect her attendance.
-

3. PETITIONS

No petitions were received relating to matters which the Committee is responsible.

4. SUBMISSIONS / REFERRALS FROM PENSION BOARD

An update was given informing the Committee of referrals made by the Pensions Board. The Committee heard that;

- The Pensions Board received a presentation from London CIV
- The Board Members noted the absence of employee representation in the London CIV.
- Misgivings around ESG engagement
- Committee members requested to receive pensions board meeting feedback of John Jones by email before the Pensions Committee meeting.

5. REPORTS FOR CONSIDERATION

6. ACTUARIAL VALUATION UPDATE - PRESENTATION FROM HYMANS ROBERTSON

The Committee received a presentation from Hymans and were given an update on the Actuarial valuation. The main points highlighted were;

- The deficit has gone down by £120 million
- At the last valuation it was at 73.4%
- At the last valuation there was a slightly bigger risk premium
- Assets have grown by almost £200 million and performance has been stronger.
- £45 million has been profited on assets with reduced liabilities.
- Deficit contributions were around 15% last time and gone down to 9½%

It was
RESOLVED
That the contents of the presentation be noted.

7. PRESENTATION FROM LONDON COLLECTIVE INVESTMENT VEHICLE (CIV)

Jill Davy's from London CIV delivered a presentation to the Members of the Pensions Committee and the main points highlighted were;

- The London CIV Board is part of the decision making process
- On a local level the Fund still has a considerable amount of responsibility.
- To ensure the delivery of value for money as more people move to pooling, the Committee were told by Ms Davy's the level of asset management will have to be increased with the Fund.
- At the moment London CIV do not have in house expertise or resources to employ their own Fund Managers.

It was
RESOLVED
That Members of the Committee note the content of the presentation.

8. REVIEW OF PENSION FUND INVESTMENT STRATEGY

The Investment and Treasury Manager presented this report to the Committee which provided a summary of the need to review the current investment strategy following the 2016 Triennial Actuarial Valuation outcome and other relevant issues such as the current investment climate.

The Committee heard that the review will encompass an asset liability study which assesses the suitability of alternative investment strategies for the Pension Fund's liability profile.

The Committee were told that no alternatives have been considered at this stage. The Committee could decide to continue with its existing strategy however, it would be considered best practice to at least carry out an assessment of the Fund's position following the triennial valuation, even if the conclusion was to remain with the current strategy thereafter.

It was
RESOLVED
That the contents of the report be noted.

9. ACADEMY CONVERSION- MULBERRY SCHOOL AND IAN MIKARDO HIGH SCHOOL, PENSION CONTRIBUTION RATES

The Committee heard from the Investment and Treasury Manager that Mulberry School for Girls and Ian Mikardo High School (IMHS), within the London Borough of Tower Hamlets (LBTH) have received an Academy Order from the Secretary of State for Education and plan to convert to academy status by 1st November 2016.

The Committee were told that the final Pension contribution rate for IMHS is 51% and for Mulberry School for Girls the total contribution rate is 40.1%. The Committee were told that these figures were based on 2013 valuation to be consistent with schools that had already converted as academies and is just for the four month period November 2016 to March 2017 and they will be revised from 1st April 2017 based on the March 2016 Valuation.

In response to Members questions, the Committee heard that;

- A 20 year recovery period is common but the reason why the Council took 14 year period is due to the risk faced by local authorities.
- Cllr Harrisson requested for data to be provided at the next Committee regarding the conversion of St Pauls Way Trust School.
- Payroll for IMHS is approximately £330,000 and Mulberry School for Girl's payroll is £1.3 million
- As they are scheduled bodies, the authority is required to admit new academies into the Scheme.

It was
RESOLVED

- That the Committee confirm in line with the Pensions Committee resolution at its meeting of 17 November 2011 (and subsequent decisions on individual Academy conversions) that there should be a recovery period of 14 years to determine the amount of Pension deficit attributable to Mulberry School for Girls and Ian Mikardo High School
- And the final contribution rate for each school mentioned above be noted.

10. MARKET UPDATE

Mr Raymond Haines, the Independent Investment Advisor updated the Committee on recent market activities. Members heard;

- There are other factors impacting the market aside from Brexit
- Equity markets would benefit from currency move, providing portfolio is unhedged.
- Bonds were looking to be incredibly expensive and there is no reason to expect for it to become cheaper.
- Money was continuing to go into equities
- After a meeting with 4 Fund Managers, the Committee were told that there were negative returns from US equities.
- The Committee were told that a period of uncertainty would last for a while post Brexit but our portfolio is predominantly based in non-domestic equities.

It was
RESOLVED
That Members note the verbal market update report.

11. PENSION FUND MANAGERS INVESTMENT PERFORMANCE REVIEW FOR QUARTER END 30 JUNE 2016

The Investment Treasury Manager presented the report on the Investment Performance Review for Quarter End 30 June 2016.

This report informed Members of the performance of the Fund and its investment managers for the quarter ending 30th June 2016.

The Committee heard that for this quarter the Fund underperformed the benchmark by 0.4% delivering a positive absolute return of 4.8% against benchmark return of 5.2%

The Committee also heard that for this quarter end, four out of eight mandates matched or achieved returns above the benchmark. The Fund performance lagged behind the benchmark over the quarter due to poor returns from LCIV (Baillie Gifford) Global Equity and LCIV (Baillie Gifford) Diversified Growth Fund and GMO.

It was
RESOLVED
That the contents of the report be noted.

12. PENSION FUND ANNUAL REPORT 2015/16 AND REVIEW OF FUND MANAGERS INTERNAL CONTROLS (TO FOLLOW)

The Investment and Treasury Manager tabled the report at the meeting and presented it to the Committee. This report presented the Pension Fund Annual Report and Statement of Accounts for 2015/16 and 2015/16 Pension Fund Audit Report (ISA 260 Report) following the audit by KPMG.

The Committee heard that the review of fund managers SAS70/SSAE16 reports has identified no significant changes in the internal control environment from last year. The Fund managers' internal control reports have been audited and approved by external auditors and they are satisfied that adequate controls are in place for managing and reporting of the Fund's assets.

The committee delegated the approval of the Pension Fund Annual Report and Statement of Accounts for 2015/16 to the chair and the vice chair once they received the audit letter and the final version of the annual report via email.

It was
RESOLVED
- That the contents of the report be noted
- The Pension Fund Statement of Accounts be approved
- And the Pension Fund Annual Report be approved by Members of the Committee.

13. PENSION FUND PROCUREMENT PLANS 2016/17

The Investment Treasury Manager presented the Pension Fund Procurement Plans 2016/17

The Committee were told about the procurement plans covering the fund's independent consultant, global custodian and actuarial services.

The Committee heard that the contracts in place for all the above mentioned service providers have been in place for over ten years or do not exist formally and they are therefore long overdue for formal review.

The Committee heard that the Council has an overarching responsibility to maintain the Pension Fund. It is essential that the Council has a Global Custodian, Investment Consultant, Independent Advisor and a Scheme Actuary to assist in the proper management of the Fund. The responsibility for the strategic oversight of all aspects of the Pension Fund is worth the Pensions Committee.

It was
RESOLVED
That the contents of the report be noted.

14. TRAINING EVENTS

None.

15. ANY OTHER BUSINESS CONSIDERED TO BE URGENT

It was agreed that the next Pensions Committee to be held on December 7th be moved to 6:00 P.M. and the location of the meeting be changed to the Idea Store Canary Wharf.

The Committee Clerk (Nishaat Ismail) to check availability of a meeting room at Idea Store Canary Wharf.

16. EXCLUSION OF THE PRESS AND PUBLIC

17. RESTRICTED MINUTES

The restricted minutes of the Pensions Committee held on 30th June 2016 were approved as a correct record of proceedings.

The meeting ended at 21:28

Chair, Councillor Andrew Cregan
Pensions Committee

Non-Executive Report of the: **PENSIONS COMMITTEE** **07 December 2016**	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:**
Examination of Approaches for Managing Fossil Fuels and Climate Change Issues as part of the Fund Ethical, Social and Governance (ESG) Policy	

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

Introduction

The purpose of this report is to provide recommendations to be considered and approved by the committee in relation to the Fund's approach to climate change issues and fossil fuel investment in order to formulate the Fund's Ethical, Social and Governance (ESG) Policy. It also provides information on work to be undertaken with indicative timescales, if the committee approves the recommendations.

The London Borough of Tower Hamlets is the Administering Authority for the Pension Fund and delegated powers under the Council Constitution have been given to the Pension Committee to oversee the management of the Pension Fund. This includes monitoring of investments, making decisions on asset allocation, appointing advisors, overseeing pension administration, setting budgets and receiving the annual report and accounts for the Pension Fund. Factors which could impact on the long term financing of the Fund therefore need to be given full consideration as potential high level risks.

The Pensions Committee has on a number of occasions considered its approach to responsible investment practices and also at ways to increase their level of engagement on environmental, social and governance issues in relation to the management of the Fund investments. The Fund itself is a member of the Local Authority Pension Fund Forum (LAPFF) and has used this primarily as a route to ensuring that the Fund's voice is heard in conjunction with other investors. Like most LGPS funds, the Fund has preferred to use the route of engagement with its managers and companies rather than taking a particular stance of divesting in companies or market sectors. The Committee has to take into account the financial risks of such a course of action, recognising its fiduciary responsibilities to ensure that it is able to meet its financial commitments over the longer term. Restricting the external managers from investing in specific stocks could impact on the returns that they are able to deliver to the Fund and has therefore not been an approach that the Committee has previously wanted to adopt.

There are a wide range of evidence setting out the risks of climate change and 97% of the world's climate scientists agree that human emission of greenhouse gases are responsible for climate change. This report looks briefly at some of the issues and rather than try to provide an extensive summary of some of the research, a number of the research papers are attached to this report to provide Members with an opportunity to review some of the discussion papers.

In summary climate-sensitive industry sectors should be the primary focus. Investors also have numerous engagement options, as they can engage with investment managers and the companies in their portfolio to ensure appropriate climate risk management and associated reporting are in place. They can also engage with policymakers to help shape regulations.

Recommendations:

The Pensions Committee is recommended to note this report and to consider and to approve recommendations set below:

a. *Commit to the UK Stewardship Code.*
b. *Develop a policy statement regarding the London Borough of Tower Hamlets' approach to fossil fuel investment with a view to inclusion as a section within the new Investment Strategy Statement (ISS), which is the new name for the current Statement of Investment Principles.*
c. *Review options for switching some of the UK passive mandate into a low carbon target index fund.*
d. *Consider options for an initial **active investment** of approximately 5% of the Fund in a sustainability/low carbon or clean energy fund(s). Given the right risk/return profile, investment in such a fund would demonstrate the Fund's commitment to invest in clean and sustainable companies.*
e. *Monitor carbon risk within the London Borough of Tower Hamlets Pension Fund and to appoint a specialist contractor to conduct a carbon footprint review of the Fund at an estimated cost of between of £5k to £20k.*
f. *Continue engagement activities with the Fund's investment managers on their approach to fossil fuel and to promote consideration of climate change issues with managers when making investment decisions.*
g. *Maintain an active approach to climate change issues with investee companies and look for further opportunities to work with others on issues of ESG importance.*

1. REASONS FOR THE DECISIONS

1.1 The Pensions Committee act in the role of quasi trustees for the Pension Fund and are therefore responsible for the management of £1.27 billion worth of assets and for ensuring the effective and efficient running of the Pension Fund. The management of the Fund's investment portfolio and the investment returns that the Fund is able to deliver have significant financial implications, not just for the Fund itself but also on the Fund's employers in terms of the level of contributions they are required to make to meet the Fund's pension undertakings, which are underwritten by statute.

1.2 The Fund recognises that investment in fossil fuels and the associated exposure to potential 'stranded assets' scenarios may pose material financial risks. These risks apply not only to the Fund's investment portfolio but also, when considered on a wider scale, to long term global economic growth.

1.3 In recognising the risks that climate change and stranded assets scenarios could pose to the Fund, the Committee needs to understand where these risks might apply and how they can best be mitigated within the investment management framework within which LGPS funds operate. The recommendations provided on this report are aimed at developing both a greater understanding of the risks and a set of strategies to help mitigate them.

1.4 The costs involved will very much depend on future decisions made around investment strategy. Climate change risk will be integrated into the forthcoming new Investment Strategy Statement to ensure that it is considered as part of the Committee's asset allocation decisions, rather than in isolation. Potential costs that could be incurred through development of the recommendations above include additional fees for use of low carbon indices; however, any such costs would need to be considered against the potential for risk mitigation and the performance of the mandate as a whole.

2. ALTERNATIVE OPTIONS

2.1 No alternative.

3. DETAILS OF REPORT

3.1 The Pension Fund Statement of Investment Principles (SIP) is required under the old regulations to set out its approach to socially responsible investments. Recognising that the Committee acts as quasi trustees of the Pension Fund, the policy followed by the Fund stated in the current SIP is:

"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".

3.2 In order for the Committee to make an appropriate legal decisions, the new Local Government Pension Scheme Guidance on Preparing and Maintaining an Investment Strategy Statement states in Regulation 7(2)(e) - How social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments.

3.3 When making investment decisions, administering authorities must take proper advice and act prudently. In the context of the local government pension scheme, a prudent approach to investment can be described as a duty to discharge statutory responsibilities with care, skill, prudence and diligence. This approach is the standard that those responsible for making investment decisions must operate.

3.4 Although administering authorities are not subject to trust law, those responsible for making investment decisions must comply with general legal principles governing the administration of scheme investments. They must also act in accordance with ordinary public law principles, in particular, the ordinary public law of reasonableness. They risk challenge if a decision they make is so unreasonable that no person acting reasonably could have made it.

3.5 The law is generally clear that schemes should consider any factors that are financially material to the performance of their investments, including social, environmental and corporate governance factors, and over the long term, dependent on the time horizon over which their liabilities arise.

3.6 However, the Government has made clear that using pension policies to pursue boycotts, divestment and sanctions against foreign nations and UK defence industries are inappropriate, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government.

3.7 Although schemes should make the pursuit of a financial return their predominant concern, they may also take purely non-financial considerations into account provided that doing so would not involve significant risk of financial detriment to the scheme and where they have good reason to think that scheme members would support their decision.

3.8 Investments that deliver social impact as well as a financial return are often described as "social investments". In some cases, the social impact is simply in addition to the financial return; for these investments the positive social impact will always be compatible with a prudent approach to investing. In other cases, some part of the financial return may be forgone in order to generate the social impact. These investments will also be compatible with the prudent approach providing administering authorities have good reason to think scheme members share the concern for social impact, and there is no risk of significant financial detriment to the fund.

3.9 Members will recognise that approximately 25% of the Fund's assets are held as a passive UK equity mandate with performance target of tracking the FTSE All Share index. This portfolio does have 11.6% weightings in Oil and Gas Industry at 30th September. This portfolio is due for review, to consider the appropriateness of allocating 25% of the Fund to passive UK Equity mandate. Attached as an appendix is the passive manager's organisational approach to Climate Change, ESG and voting. Legal and General Investments is the Council's passive manager.

3.10 Officers meet with a wide range of managers on a regular basis to gather intelligence and to explore investment ideas. Some of the managers have assisted officers in building their understanding of the facts, figures and risks around climate change and fossil fuel investments

Climate change and fossil fuel investments

3.11 Climates are changing globally. Scientists are now 'unequivocal' in their opinion that greenhouse gases emitted as a result of human activities are causing global warming. The global temperature increase we will experience in the coming decades will profoundly impact people's lives and, therefore, our economies. In order to minimise the most damaging consequences, global leaders have agreed to limit the temperature increase to 1.5 – 2°c above the pre-industrial levels. It is an ambitious but achievable target if we can meaningfully shift our methods of generating and consuming energy globally.

3.12 Climate change, and its direct and indirect impact, poses a significant systemic risk for long-term investors. Due to the unpredictable and inconsistent nature of weather patterns, it is difficult to assess the exact level of its impact. The magnitude and likelihood of risks and the scope and scale for solutions are also highly dependent on the policy support for mitigating excess emission levels and adapting to more extreme and changing weather patterns.

3.13 It is widely acknowledged that the “The Stern Review on The Economics of Climate Change”, published in 2006, commissioned by the Chancellor as a contribution to assessing evidence and building understanding, was one of the earliest, most extensive and discussed pieces of research into the impact of climate change on the global economy. The full document runs to 700 pages. Stern concluded that, depending on the range of risks taken into account, climate change could cost the global economy between 5 to 20% of GDP in perpetuity unless action is taken to mitigate global warming.

In brief some of the key points were:

- Climate change is global in its causes and consequences
- Ignoring climate change will eventually damage economic growth
- All countries will be affected by climate change, but the poorest countries will suffer earliest and most
- Average temperatures could rise by 5°C from pre-industrial levels if climate change goes unchecked and could lead to untold consequences for people in terms of access to water, food and health
- Emissions have been and continue to be driven by economic growth but stabilisation of greenhouse gas is feasible if actions are taking to mitigate without significantly damaging economic growth
- Significant new opportunities could arise across a wide range of industries and services and markets for low carbon energy products are likely to be worth at least $500bn p.a. by 2050.
- Collective action could lead to an effective response to climate change, this could include carbon pricing, technology policy, innovation and financing and improvements to energy efficiency. “There is still time to avoid the worst impacts of climate change if strong collective action starts now”.
- “No-one can predict the consequence of climate change with complete certainty, but we now know enough to understand the risks.”

Investment Manager Research and Index Providers

3.12 With the increasing emphasis that investors are placing on the risks around climate change, investment managers and index providers themselves are starting to address investor concerns to varying degrees. Some managers have undoubtedly been participating earlier in the debate than others and for some climate change falls under the broad remit of environmental, social and governance (ESG) research.

Carbon Tracker Research

3.13 Carbon Tracker is a not for profit financial think tank aimed at enabling a climate secure global energy market by aligning capital market actions with climate reality. Climate tracker has published a number of research pieces, which can be found on their website: http://www.carbontracker.org/

Global Investor Coalition on Climate Change

3.14 Global Investor looked at the issues from the perspective of investors and it is relevant in any discussion on this subject to include a recent report provided by this group titled: Climate Change Investment Solutions: A Guide for Asset Owners which is included as an appendix to this report.

The guide is presented in 4 sections each of which sets out a range of suggested actions that asset owners can take.

- Section 1: Strategic review – Presents actions to integrate climate change into investment beliefs and investment policies that are actionable and transparent.
- Section 2: Strategic asset allocation – Discusses actions for measuring and managing the risks and opportunities of climate change, both within the existing asset allocation structure and through evolving the asset mix over time.
- Section 3: Mitigation investment actions – Presents actions for reducing the carbon intensity of existing assets, along with opportunities to invest in low carbon, clean energy and energy efficient assets.
- Section 4: Adaptation investment actions – Discusses actions to reduce the vulnerability of existing assets to the physical impacts of climate change, as well as building exposure to adaptation opportunities.

3.15 **Investment consultancy firm, Mercer**, has undertaken two studies with a number of partners, including asset owners. Mercer Reports are;

a) *Climate Change Scenarios – Implications for Strategic Asset Allocation (2011)*
b) *Investing in a Time of Climate Change (2015).*

Both studies are focused on the investment implications for climate change and consider ways that investors should address these issues.

3.16 The most recent study, which is the second study completed in 2015 – This study looks to address a number of questions having modelled a number of scenarios and how these might play out in the investment returns that are achieved in various sectors

a). How big a risk/return impact could climate change have on a portfolio and when might that happen?

i. Climate change, under the scenarios modelled, will inevitably have an impact on investment returns, so investors need to view it as a new return variable.
ii. Industry sector impacts will be the most meaningful. For example, depending on the climate scenario which plays out, the average annual returns from the coal sub-sector could fall by anywhere between 18% and

74% over the next 35 years, with effects more pronounced over the coming decade (eroding between 26% and 138% of average annual returns). Conversely, the renewables subsector could see average annual returns increase by between 6% and 54% over a 35 year time horizon (or between 4% and 97% over a 10-year periods).

iii. Asset class return impacts could also be material – varying widely by climate change scenario. For example, a 2°C scenario could see return benefits for emerging market equities, infrastructure, real estate, timber and agriculture. A 4°C scenario could negatively impact emerging market equities, real estate, timber and agriculture. Growth assets are more sensitive to climate risks than defensive assets.

iv. A 2°C scenario does not have negative return implications for long-term diversified investors at a total portfolio level over the period modelled (to 2050), and is expected to better protect long-term returns beyond this timeframe.

b). What are the key downside risks and upside opportunities and how do we manage these considerations within the current investment process?

i. Key downside risks come either from structural change during the transition to a low-carbon economy, where investors are unprepared for change, or from higher physical damages. In the first instance, under a 2°C, or Transformation scenario, investors could see a negative impact on returns from developed market equity and private equity, especially in the most affected sectors. On the flip side, this scenario would be likely to lead to gains in infrastructure, emerging market equity, and low-carbon industry sectors.

ii. Under a 4°C, or Fragmentation (Higher Damages) scenario, chronic weather patterns (long-term changes in temperature and precipitation) pose risks to the performance of asset classes such as agriculture, timberland, real estate, and emerging market equities. In the case of real asset investments, these risks can be mitigated through geographic risk assessments undertaken at the portfolio level. To embed these considerations in the investment process, the first step is to develop climate-related investment beliefs alongside other investment beliefs.

iii. These can then be reflected in a policy statement, with related investment processes evolved accordingly. The next step is portfolio oriented activity, including risk assessments, new investment selection/weights and, finally, enhanced investment management and monitoring.

C). What plan of action can ensure an investor is best positioned for resilience to climate change?

i. Investors have two key levers in their portfolio decisions — investment and engagement. From an investment perspective, resilience begins with an understanding that climate change risk can have an impact at the level of asset classes, of industry sectors and of sub-sectors.

3.17 The Fund currently asked the fund managers to supply information on their engagement in reducing carbon foot prints of the fund and this information will be made available on a quarterly or yearly basis at the Pensions Committee quarterly meeting.

3.18 The Fund through its participation with Local Authority Pension Fund Forum (LAPFF) supported progress towards an orderly transition to a low carbon economy. This is by actively working with other asset owners, fund managers, companies, academia, policy makers and others in investment industry.

3.19 **Listed below is what other funds are doing:**

- In June 2015, the Environment Agency Pension Fund committed £280m into the MSCI World Low Carbon Target Index Fund
- In July 2015, the London Assembly recommended that the London Pensions Fund Authority (LPFA) change fossil fuel investments to more responsible positions.
- In January this year, Haringey Local Government Pension Fund announced it would shift one-third of its equity funds – equating to about £200m – into the MSCI World Low Carbon Target Index Fund, run by LGIM.
- This September, Waltham Forest Local Government Pension Fund announced it would “exclude fossil fuels from its strategy over the next five years”.

3.20 Officers are in collaboration with London Collective Investment Vehicle (LCIV) to develop policies on Responsible Investment and ESG matters, Sustainable Equities, Stewardship Code, Voting Policy and Low Carbon approach to investment.

<u>Future Work on Recommendations</u>

3.21 Set below are plans and indicative timescales for future work on recommendations set in this report as the Fund’s approach to management of fossil fuel investment and management of the financial risks posed by climate change.

a. Commit to UK Stewardship Code – For the Committee to agree to become a signatory of the Stewardship Code. The principal aim of the Code is to encourage institutional investors, who manage other people's money, to be active owners and engage with their investee companies so as to encourage them to act in the interests of their beneficiaries. In the UK context these are primarily shareholders, but UK company law extends corporate responsibilities to wider stakeholders. The Code was revised and updated in September 2016. The seven principles of the Code are that Institutional investors should:

   i. Publicly disclose their policy on how they will discharge their stewardship responsibilities.
   ii. Have a robust policy on managing conflicts of interest in relation to stewardship with this policy being publicly disclosed.
   iii. Monitor their investee companies.
   iv. Establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.
   v. Be willing to act collectively with other investors where appropriate.
   vi. Have a clear policy on voting and disclosure of voting activity.

vii. Report periodically on their stewardship and voting activities.

b. Develop a policy statement regarding the London Borough of Tower Hamlets' approach to fossil fuel investment with a view to inclusion as a section within the new Investment Strategy Statement (ISS), which will replace the current Statement of Investment Principles. It is intended that the development of such a statement for inclusion within the ISS will both demonstrate a commitment to managing carbon risk and set targets that are both quantifiable and measurable where this is appropriate. The timetable for development of the policy statement is linked to both the Fund's triennial valuation and a planned update to the LGPS (Management and Investment of Funds) Regulations, as this will set out the required format and content for new ISS. The new ISS will be in place in April 2017.

c. Review the option of switching the Pension Fund's passive UK equity mandate. The Fund's passive UK equity mandate is a standard market capitalisation weighted index, currently managed by Legal & General Investment Management (LGIM), which tracks the FTSE All share. About five or six LGPS funds have converted some of their passive Equity funds to low carbon mandate and these portfolios are being managed by LGIM. Low carbon passive strategies are made available with reduced fee arrangements negotiated by the London CIV. Officers could work with the fund manager, investment adviser and investment consultant over the coming months to identify suitable approach and strategies in an efficient cost effective manner to commence this arrangement with a view of this portfolio being in place by June 2018.

d. Consider options for an initial **active investment** of approximately 5% of the Fund in a sustainability/low carbon or clean energy fund(s). Given the right risk/return profile, investment in such a fund would demonstrate the Fund's commitment to invest in clean and sustainable companies. Again, this is an area in which work is being done along the London CIV officers, to ensure that any strategy decision is made in line with the move to asset pooling. During August, the CIV commenced a search for active global equity managers and interviewed successful managers between October and November 2016 and one of the sub fund or strategy of this search is Global Sustainable Equity. The Tower Hamlets Fund is playing an active role in this procurement through representation on the Global Equity Working Group. This group is part of the wider Investment Advisory Committee (on which the Fund is also represented) and is supporting the CIV in the procurement exercise through reviewing submissions and attending manager interviews. Once the procurement is complete, we aim to identify a suitable strategy through the Global Sustainable Equity lot, with intention to fund probably by June 2016.

e. Monitor carbon risk within the London Borough of Tower Hamlets Pension Fund and to appoint a specialist contractor to conduct a carbon footprint of the Fund at an estimated cost of between of £5k to £20k. Measuring emissions and climate risks in the portfolio will allow the Fund to establish a base of data from which to examine its investment assumptions and test investment processes. It will also enable the Fund to make an assessment on an ongoing basis as to how its exposure to climate change risks progresses over time. This work can start December 2016 and the initial results could be presented at the March 2017 Committee.

f. Continue engagement activities with the Fund's investment managers on their approach to fossil fuel and to promote consideration of climate change issues with managers when making investment decisions. This is an area in which further work will be undertaken over the coming months. We have been in contact with a number of our managers to request more detailed reporting on environmental issues, and will be looking at this in more detail in the near future.

g. Maintain an active approach to climate change issues with investee companies and look for further opportunities to work with others on issues of ESG importance. The Fund continues to monitor ESG issues through the alerts issued by the LAPFF, a collection of Local Authority funds who, by acting collectively, are able to apply pressure to the management of companies. LAPFF has previously been involved with voting climate-change related resolutions, and has invited its members to co-file. So far, these engagements have not affected companies we hold directly; however, where we are able (i.e. we have direct holdings in the company concerned), we will co-file these resolutions as part of LAPFF. Where our holdings in a company are through a pooled fund, we will make a public expression of support. LAPFF guidance on Fossil Fuel and Stranded Assets is attached as an appendix to this report.

3.22 Stranded assets are those which suffer unanticipated or premature write-offs, downward valuations, or are converted to liabilities. Assets may become stranded by one-off transformational shifts in valuation, or over time, as a result of appropriate risks not being analysed and priced into the future anticipated value of the assets.

3.24 This stranded assets issue has raised the profile in challenging its managers to take these factors into consideration when investing on behalf of the Fund and now includes questions on manager approaches to ESG when considering new investment mandates. The Committee also requested that an additional section be included in the quarterly monitoring report which specifically covered the engagement activities undertaken by LAPFF and also the Fund's managers' responses to issues raised. Managers have been challenged and will continue to be challenged on their voting policies and also the extent to which they are factoring in ESG in the company selections and increasing their approach to climate change issues.

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

5.1 The Committee has legal responsibilities for the prudent and effective stewardship of the Pension Fund and a clear fiduciary duty in the performance of its functions. The LGPS (Management and Investment of Funds) Regulations 2016 require Administering Authorities to state the extent to which they comply with the Guidance given by the Secretary of State. In accordance with regulation 7(2)(e) the authority must set out in its Investment Strategy Statement, its policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments.

5.2 Updated Statutory Guidance on preparing and maintaining an investment strategy statement was published on the 15th September 2016. Having a policy in place covering the authority's approach to ethical, social and governance issues will enable to authority to meet its statutory duties in this regard. The recommendations discussed in this report are in line with both the Committee's terms of reference and legal responsibilities.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 The management of the Fund's investment portfolio and the investment returns that the Fund is able to deliver have significant financial implications, not just for the Fund itself but also on the Fund's employers in terms of the level of contributions they are required to make to meet the Fund's pension undertakings, which are underwritten by statute.

6.2 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.

6.3 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 The costs involved will very much depend on future decisions made around investment strategy. Climate change risk will be integrated into the forthcoming new Investment Strategy Statement to ensure that it is considered as part of the Committee's asset allocation decisions, rather than in isolation.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 The Fund through its participation with Local Authority Pension Fund Forum (LAPFF) supported progress towards an orderly transition to a low carbon economy. This is by actively working with other asset owners, fund managers, companies, academia, policy makers and others in investment industry.

9. RISK MANAGEMENT IMPLICATIONS

9.1 The Fund recognises that investment in fossil fuels and the associated exposure to potential ‘stranded assets’ scenarios may pose material financial risks. These risks apply not only to the Fund’s investment portfolio but also, when considered on a wider scale, to long term global economic growth.

9.2 In recognising the risks that climate change and stranded assets scenarios could pose to the Fund, the Committee needs to understand where these risks might apply and how they can best be mitigated within the investment management framework within which LGPS funds operate. The recommendations provided on this report are aimed at developing both a greater understanding of the risks and a set of strategies to help mitigate them.

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 (To be email on request)

- LAPFF Guidance on Fossil Fuel and Stranded Assets
- Blackrock – The Price of Climate Change, Global Warming’s Impact on Portfolios (October 2015)
- Schroders: Global Climate Change Investment Themes
- Schroders - Responding to Climate Change Risk in Portfolio Management (February 2015)
- Schroders - Understanding portfolio carbon foot printing an introduction (October 2015)
- MSCI - Beyond Divestment Using Low Carbon Indices (March 2015)
- Global Investor Coalition on Climate Change - Climate Change Investment Solutions: A Guide for Asset Owners
- Carbon Tracker - How the energy sector is missing potential demand destruction
- LGIM climate change policy
- LGIM - Corporate Governance & Responsible Investment Policy – UK

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

- As listed above as appendices

Officer contact details for documents:

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Non-Executive Report of the: **Pensions Board & Pensions Committee** 05 & 07 December 2016	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted

31st March 2016 Triennial Valuation – Initial Results and Public Service Pensions Act - Section 13 Valuation

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

Summary

This report provides the Committee with a summary of progress to date on the 2016 actuarial valuation. Whilst a full report is not yet available for distribution, preliminary work gives a guide to the outcome of the valuation. The result of this preliminary work was presented at the Committee by the Fund's actuary, Hymans Robertson. The Actuarial Valuation is undertaken every three years and is an assessment of the assets and liabilities of the pension fund, which then determines the funding level. The final valuation will determine the contribution rates payable by all employers participating in the Fund, which includes the Council.

An initial presentation of the provisional overall funding position was given by Hymans Robertson at the meeting of 22nd September. Members were updated with the initial results and presented with a range of discussion points. The initial outcome of the 2016 valuation was that the monetary deficit amount decreased from £365m to £235m, the Fund saw its funding level increase from 71.8% to 82.7%.

This report also provides Members with information on the 'dry run' Section 13 analysis completed by the Government Actuary's Department (GAD) using the 2013 valuations.

The Government Actuary has been appointed by the Department of Communities and Local Government (DCLG) to report under section 13 of the Public Service Pensions Act 2013 in connection with the Local Government Pension Scheme ("LGPS" or "the Scheme") in England and Wales.

Recommendations:

The Pensions Committee is recommended to:

1) Agree the assumptions and methodology used by the Actuary to determine the actuarial funding level and a standardised basis for setting employer contribution rates.
2) Note the content of this report and the draft results of the triennial valuation of the Fund.

1. REASONS FOR THE DECISIONS

1.1 The Council is required by law to undertake an actuarial valuation of the Fund's assets and liabilities. The Pensions Committee under delegated authority should agree the underlying assumptions of the valuation with the actuary.

1.2 The understanding of the Pension Fund in terms of its investments, the Fund's liabilities both short and long term and the profile of its members between actuarial valuations determines the financial status of the pension fund, its funding level and the contributions that employers need to make into the Fund for the following three years.

1.3 The level of funding for the Pension Fund and the requirement to fund employee pension benefits, both past and current can directly impact on the level of resources available for other Council services. The valuation outcome is sensitive to both the actuarial and financial assumptions made within the valuation and any significant variations to those assumptions could impact upon Fund's financial position.

1.4 The contribution rate currently paid by the Council is 35.5% of payroll; this applies equally to the Council and to its schools.

2. ALTERNATIVE OPTIONS

2.1 There are no alternative options.

3. DETAILS OF REPORT

3.1 The Pension Fund is required to undertake a formal actuarial valuation of the Fund's assets and liabilities every three years to establish its funding position and to set the contribution rate for the following three years. The Pensions Committee under delegated authority should agree the underlying assumptions of the valuation with the actuary.

3.2 The last formal actuarial valuation of the London Borough of Tower Hamlets Pension Fund was carried out as at 31st March 2013, which showed a slight improvement in the funding level from 71.2% to 71.8% and set the contribution rates for the three years commencing 1st April 2014.

3.3 The Fund's actuary, Hymans Robertson, has been reviewing the data supplied to them by the Administering Authority, Tower Hamlets, over the summer and is in the process of assessing the current funding position and contributions payable by both the Council and other employers in the Fund.

3.4 The actuary has produced an initial overall fund results; however, issues around the quality of data provided by employers have meant that a number of assumptions have been required to produce these. These assumptions are not believed to have a material impact on the whole fund results, but do mean that additional work is likely to be required for some individual employers. Data quality is an important issue which has been raised by the Pensions

Regulator (tPR); the Fund has been working hard to improve the quality of data provided but this work remains ongoing.

3.5 The assets are the amalgamation of all the asset classes which the Fund manages, including equities, bonds, property, etc. valued as at 31st March 2016. The liabilities are a summation of all the pension payments which are due to all scheme members, pensioners, deferred members and active members over the remaining lifetime of all members, which could stretch out beyond 60 years. The actuary then calculates the contributions which would be required in order for the Fund to meet its liabilities and to recover any deficit which has arisen. The actuary is looking at different options whereby the Committee has to make a decision to either continue with a relatively cautious approach or to reduce the deficit recovery period from 20 to 17 years.

3.6 The background to other employers varies significantly depending on what their formal status is within the fund – this will depend on their contract lifespan and funding position. Some employers arise from TUPE transfer situations when the Council outsources contracts which involve the transfer of staff. These are either Community Admission Bodies or Transferee Admission Bodies. As a general rule, when staff are TUPE'd across to new admission bodies, any historic deficit remains with the Council and the new employer is set up with a 100% funding position i.e. it has sufficient assets to cover any liabilities as at the date of transfer. Scheduled bodies, such as academies, receive a share of the deficit on transfer where these arise as a result of TUPE. A number of the earlier academies in Tower Hamlets were established as completely new entities and therefore did not result in TUPE transfers; hence the contribution rates can vary significantly between academies. The contribution rate which is set for such an employer is such that it should be sufficient to ensure that at the end of the contract life, the employer is 100% funded. Any deficit which arises during the contract life should therefore be met during the period of the contract, however, if at the end of the contract a deficit position has arisen then an admitted body employer is expected to make good that deficit.

3.7 The triennial valuations adjust contribution rates that employers are required to pay to try to ensure that any deficit at end of contract is kept to a minimum and employers will be informed of indicative contribution rates payable during the month of December. Employers will also be given the opportunity to meet with the Fund actuary to discuss the valuation following the Employer Forum to be held in December.

3.8 At the time of writing, the actuarial work is still underway but it is anticipated that the contribution rates will be available to discuss with Members at the Committee meeting itself.

Overall Fund Initial Results

3.9 A summary of the results are shown as Appendix 1. The highlights are:

- The funding level has improved from 71.8% to 82.7%.

- In monetary terms the deficit has reduced by £130m to £235m from £365m as at March 2013. This funding position was based on the Fund having assets of £1,126m and liabilities of £1,361m

3.10 The table shown below analyses the change in deficit. This table is in Page 7 of Appendix 1 of the actuarial report. The main reasons for the reduced deficit are as follows; contributions greater than cost of accrual, better than expected performance of the markets/return on investments and membership experience being better in terms of financial impact on the Fund.

Analysis		(£m)
Surplus / (deficit) at 31 March 2013		(365)
Interest on surplus / (deficit)	(53)	
Investment returns greater than expected	46	
Contributions greater than cost of accrual	38	
Membership experience over the period	66	
Change in demographic assumptions	6	
Change in base mortality assumption	16	
Change in longevity improvements assumption	1	
Change in financial assumptions	33	
Impact of LGPS 50/50 take up	(7)	
Other experience items	(16)	
Surplus / (deficit) at 31 March 2016		(235)

3.11 It is noticeable from above table, that the outcomes for the valuation assumptions that are controllable by the Council (investment returns, retirements & salary increases) have positively impacted the results; whereas the assumptions that are outside the Council's control (gilt yields and inflation during the valuation period) have had a negative impact on the results. For the first time in recent times, mortality rate has trended downwards – this has had a positive impact on Fund liabilities.

Future Contribution Rates

3.12 The Actuary determines contribution rates separately and specifically for each employer, including the Council. For 2013 valuation, the Council's rate was 15.8% of payroll for future service rate contribution. Other employers, pay rates ranged between 15.9% and 41.4% and in most cases also paid annual lump sums to cover past service deficits. The Council is paying £22m in 2016/17 to cover the past service deficit. The employer risk profile analysis will assist the actuary in determining the appropriate recovery period and consequently contribution rate for each of the employer in the Fund.

3.13 Following consultation with other employers, the Actuary may be asked to undertake additional modelling to test the impact of changing the contribution rates that they pay during the next valuation cycle.

Next Steps

3.14 The subsequent steps in the valuation process are summarised below.
December 2016

- Receive feedback from individual employers on their estimated funding level and contribution rates.
- Carry out any additional contribution rate modelling.
- Finalise Funding Strategy Statement ("FSS").

March 2017

- Present final Actuarial report including schedule of contributions from April 2017 to March 2020 together with the FSS to the Pensions Committee.

3.15 **Section 13 Valuation**

1. This piece of primary legislation requires that an appointed person, in this case, the Government Actuary's Department ("GAD"), reports on whether the LGPS formal funding valuations adhere to the following criteria:

    a. **Compliance**
    b. **Consistency**
    c. **Solvency**
    d. **Long term cost efficiency**

2. GAD will calculate a number of metrics for each of the LGPS funds using consistent actuarial assumptions. Funds will be ranked in a league table based on these metrics and assigned a RAG (Red/Amber/Green) status against each metric to identify those funds that may need to take action. The absolute value of the assumptions in the chosen actuarial basis is not important – the important fact is that all LGPS funds are measured on the same assumptions, allowing comparison across funds.

3. If GAD has concerns about LGPS funds under any of these measures then they can recommend remedial actions which may ultimately be enforced by DCLG using powers granted under this legislation. That is the resulting report may recommend remedial action where appropriate; the scheme manager (in this case the administering authority) must take and report on any remedial action they consider appropriate, although the law does provide for the Government to direct the scheme manager if they consider it necessary.
4. Six months to 31st August 2016, all the four LGPS actuaries (AON, Hymans Robertson, Barnett Waddingham and Mercer) have been engaging with GAD as they have carried out a review of LGPS 2013 valuations against the above listed criteria. This exercise is now complete. GAD has published their report and hosted a series of seminars to discuss their findings and recommendations. The 2013 valuations pre-date the effective date of the legislation. As such, the work on the 2013 valuations has no legal force but serves as a "dry run" to familiarise all parties with the process and sets expectations as to how the 2016 valuation review might be implemented.

<u>The 'dry run' report found:</u>

5. The analysis identified no evidence of material non-compliance

6. There are some inconsistencies between the LGPS local valuations in terms of approach taken, assumptions used and disclosures. These made meaningful comparison of local valuations difficult. Issues highlighted include differences of approach in terms of the derivation of discount rates, and the interpretation of the common contribution rate.

7. From the 2013 local valuation data, the funding level of the Tower Hamlets Fund improves considerably when presented on a SAB standardised basis, ***from 2013 formal valuation funding level of 72% to 85% under Section 13 SAB valuation*** is attached as appendix Z of this report.

8. **Long Term Cost Efficiency Measures** - A small number of flags (as shown in table below) triggered on the metrics used to assess long term cost efficiency. These are split into relative considerations, that compare funds to other LGPS funds (Deficit repaid, deficit period, required return and repayment shortfall) and absolute considerations, which are concerned with funds on a standalone basis (return scope, deficit extension and interest cover). ***The Tower Hamlets Fund did not trigger any flags on this measure.***

Table 6.2: Open funds with amber or red long term cost efficiency measures

PENSION FUND	MATURITY (RANK)	LONG TERM COST EFFICIENCY MEASURES						
		RELATIVE CONSIDERATIONS				ABSOLUTE CONSIDERATIONS		
		DEFICIT REPAID	DEFICIT PERIOD	REQUIRED RETURN	REPAYMENT SHORTFALL	RETURN SCOPE	DEFICIT EXTENSION	INTEREST COVER
BERKSHIRE	5.9 (78)	4%	34	6%	-2%	-0.5%	-3	No
BROMLEY	6.8 (33)	>50%	2	3%	13%	3.1%	3	Yes
ENVIRONMENT AGENCY ACTIVE[21]	5.8 (85)	IN SURPLUS	IN SURPLUS	N/A	N/A	N/A	3	N/A
GWENT	5.9 (79)	13%	8	5%	5%	1.5%	5	Yes
SOMERSET	5.9 (80)	5%	24	6%	-1%	0.0%	0	No
STAFFORDSHIRE	6.2 (59)	23%	5	4%	9%	2.4%	5	Yes
WORCESTERSHIRE	6.3 (57)	14%	7	4%	7%	2.0%	2	Yes

9. **Solvency Measures** - a series of 6 solvency measures were used to analyse funds and there were some possible risks to sponsoring employers. This solvency measures are split into ***risks already present*** (SAB funding level, open fund and non-statutory employees) and ***emerging risks*** (liability shock, asset shock and employer default). A fund is allocated a red colour code if its result is greater than 7.5%, an amber colour code if it's between 5% and 7.5% and a green colour code otherwise.

PENSION FUND	MATURITY (RANK)	SOLVENCY MEASURES					
		RISKS ALREADY PRESENT			EMERGING RISKS		
		SAB FUNDING LEVEL	OPEN FUND	NON-STATUTORY EMPLOYEES	LIABILITY SHOCK	ASSET SHOCK	EMPLOYER DEFAULT
LONDON PENSIONS FUND	9.6 (4)	92%	YES	0%	+6%	+4%	+0%
MERSEYSIDE	7.3 (17)	92%	YES	13%	+4%	+5%	+0%
MERTON	7.1 (25)	91%	YES	3%	+4%	+4%	+0%
NEWHAM	7.3 (19)	75%	YES	N/A	+4%	+4%	N/A
NORFOLK	6.6 (40)	91%	YES	9%	+4%	+4%	+0%
NORTH YORKSHIRE	5.3 (89)	87%	YES	3%	+3%	+3%	+0%
NORTHAMPTONSHIRE	6.2 (60)	85%	YES	4%	+4%	+4%	+0%
NORTHUMBERLAND	8.2 (8)	84%	YES	6%	+5%	+5%	+0%
NOTTINGHAMSHIRE	6.3 (54)	85%	YES	6%	+4%	+4%	+0%
OXFORDSHIRE	5.9 (75)	85%	YES	36%	+3%	+4%	+2%
POWYS	6.4 (46)	82%	YES	3%	+4%	+3%	+0%
REDBRIDGE	6.3 (51)	83%	YES	9%	+4%	+3%	+0%
RHONDDA CYNON TAF	6.1 (68)	77%	YES	5%	+3%	+3%	+0%
RICHMOND	7.1 (24)	97%	YES	3%	+4%	+5%	-0%
SHROPSHIRE	6.5 (43)	88%	YES	10%	+4%	+4%	+0%
SOMERSET	5.9 (80)	74%	YES	13%	+3%	+3%	+1%
SOUTH YORKSHIRE	6.4 (47)	94%	YES	10%	+4%	+4%	+0%
SOUTH YORKSHIRE PTA	25.2 (1)	114%	NO	100%	+5%	+3%	N/A
SOUTHWARK	7.3 (20)	84%	YES	2%	+4%	+4%	+0%
STAFFORDSHIRE	6.2 (59)	87%	YES	6%	+4%	+4%	+0%
SUFFOLK	6.2 (62)	93%	YES	19%	+4%	+3%	+0%
SURREY	5.9 (81)	86%	YES	5%	+3%	+4%	+0%
SUTTON	6.5 (42)	81%	YES	3%	+4%	+3%	+0%
SWANSEA	6.2 (61)	80%	YES	4%	+4%	+4%	+0%
TEESSIDE	6.8 (29)	103%	YES	13%	+4%	+5%	-0%
TOWER HAMLETS	8.1 (9)	85%	YES	0%	+5%	+5%	+0%
TYNE AND WEAR	7.1 (23)	87%	YES	11%	+4%	+4%	+0%
WALTHAM FOREST	7 (26)	73%	YES	5%	+4%	+4%	+1%

10. ***Tower Hamlets raised two amber flags under this assessment*** as shown in the table above for:

a. Liability shock – This a change in average employer contribution rates as a percentage of payroll after a 10% increase in liabilities. As a continued solvency of a fund depends on the ongoing ability of employers to pay the required contributions into the fund.
b. Asset shock – this a potential change in employer contribution rates required after a 15% fall in the value of return seeking assets. In effect a one-off decrease in asset values results in an increase fund deficits.

11. GAD reported that they had found both presentational and evidential inconsistencies in the valuation approach adopted by LGPS funds, and in assumptions used and disclosure of results. GAD named two funds with whom they would have wanted to have further discussion over the long term cost efficiency of their funding plans. GAD clarified that meeting solvency and long term cost-efficiency requirements takes precedence in the regulatory framework over the desirability of stable contributions.

12. The S13 report can be used to provide stakeholders with reassurance that the LGPS as a whole is able to meet the liabilities owed to its members, and to highlight where individual funds appear to be outliers from the main pack. On the basis of the 2013, the Tower Hamlets Fund has not raised any concerns which GAD felt would justify an engagement with the Fund and compares well with its peers when its funding level is considered on a standardised basis.

13. The Fund will continue to conduct its local triennial valuation in a way that allows it to meet its specific liabilities given its own local circumstances; the S13 report is not intended to force a standardised basis for valuations or to be used as a minimum funding requirement.

Section 13 - 2016 SAB Valuation Result

14. Under Section 13, SAB valuation assumptions for 2016, Tower Hamlets funding ratio is 93.4%. And the Fund local formal triennial valuation indicates funding level of 83%. The reason for this is because the valuations were carried out under different assumptions.

15. The SAB basis is weaker and GAD has stated that this basis is not suitable for funding as it is a best estimate basis and the Regulations require a prudent assessment. The assumptions set out in the certificate are prescribed by the Scheme Advisory Board and will allow each Fund to be compared on a like for like basis.

16. The figures being requested by SAB will have no impact on the results of the 2016 formal valuation. They are being requested to allow comparisons on certain metrics between funds. They will lead to greater transparency and should help to improve the governance and performance of the LGPS.

17. The table below highlights the valuation assumptions used by the two different valuation methodologies.

Assumptions	2016 Local Valuation	2016 - Section 13 GAD Valuation
Discount Rate	4.20%	5.06%
Pensions Increases	2.10%	2.00%
Long Term Salary Grov	2.65%	3.50%
Longetivity	CMI 2013 + 1.25%	CMI 2015 + 1.5%

Conclusion

At the next meeting the Pension Committee will need to make a decision and approve the new contribution rates for employers to be effective from 1st April 2017 for the next three years up to 31st March 2020. The Committee has to bear in mind, when making this decision on employer contributions, the outcome of the 2013 Section 13 Valuation, which indicates the Fund funding level of 85% (13% more than the formal actuarial valuation for 2013). In spite of this significant improved position, the Fund had two amber flags on solvency measures on asset shock and liability shock which basically demonstrate the ability of employers to pay the required future contributions into the fund plus funding the deficits.

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 The Local Government Pension Scheme Regulations 2013, Regulation 62, requires an Administering Authority to obtain an actuarial valuation of its fund as at 31st March 2016, and as at 31st March every third year thereafter. The documents obtained by the administering authority must include a report by an actuary in respect of the valuation, and a rates and adjustments certificate provided by the actuary. The report must contain a statement of the demographic assumptions used in producing the valuation, and how these assumptions relate to events which have actually occurred in relation to the scheme membership. These documents must be received before the first anniversary of the valuation date.

5.2 Regulation 66 also requires the Administering Authority to supply copies of any valuation report, rates and contributions certificates to be supplied to the Secretary of State, employing authorities participating in the Fund and any other bodies liable to make payments to it.

5.3 There are no immediate legal implications arising from this report.

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 level of funding for the Pension Fund and the requirement to fund employee pension benefits, both past and current can directly impact on the level of resources available for other Council services. The valuation outcome is sensitive to both the actuarial and financial assumptions made within the valuation and any significant variations to those assumptions could impact upon Fund's financial position.

7.2 The understanding of the Pension Fund in terms of its investments, the Fund's liabilities both short and long term and the profile of its members between actuarial valuations determines the financial status of the pension fund, its funding level and the contributions that employers need to make into the Fund for the following three years.

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 valuation outcome is sensitive to both the actuarial and financial assumptions made within the valuation and any significant variations to those assumptions could impact upon Fund's financial position. Therefore a prudent approach is crucial in minimising the key risks involved in managing the Pension Fund.

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 1 – 20160930 LBTH - 2016 Formal Funding Valuation
- Appendix 2 – Section 13 Dry Run

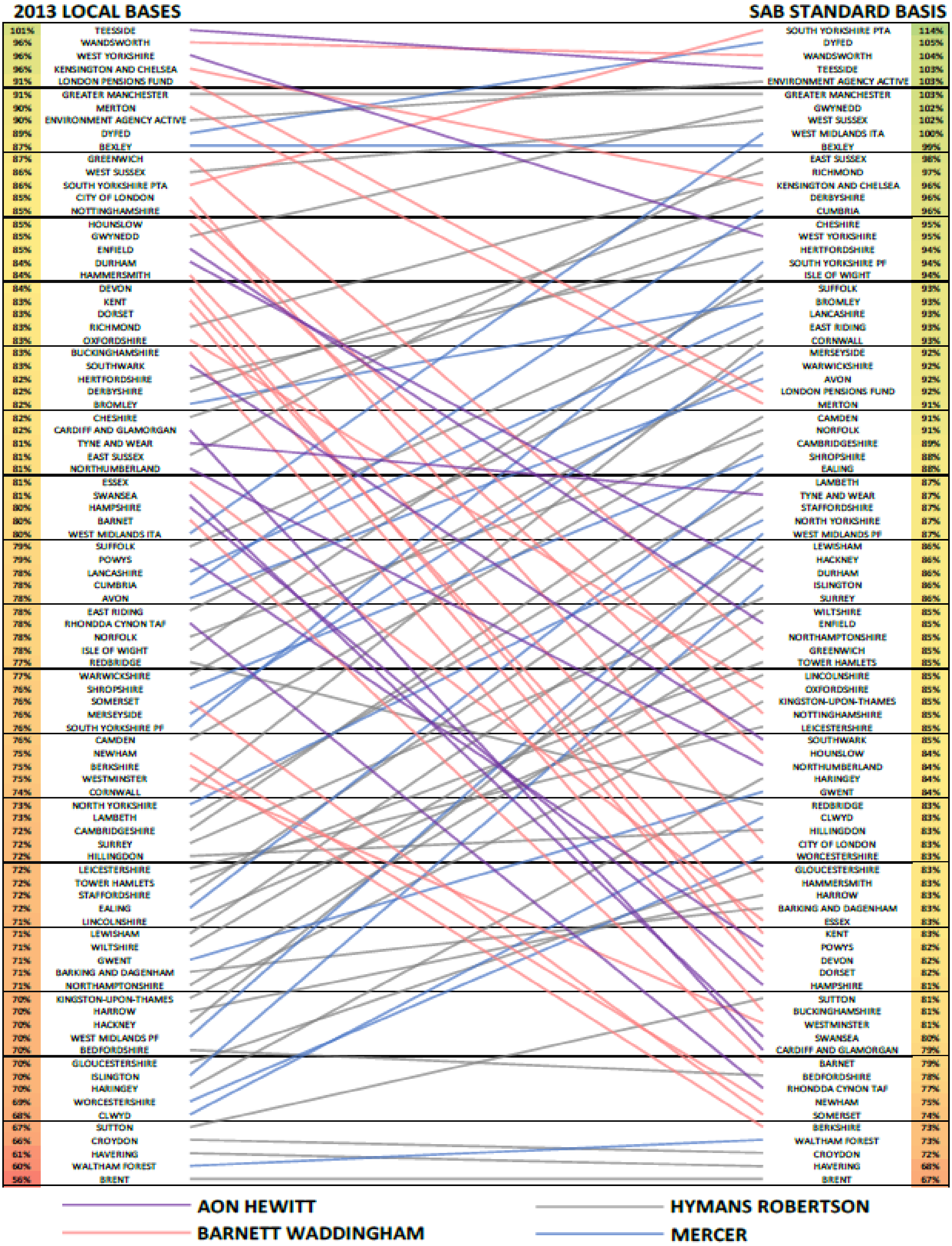
Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report

- As shown in appendices above.

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

Appendix Z

Chart 4.6: Standardising local valuation results



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HYMANS ROBERTSON

2016 Formal Funding Valuation
Initial Results

London Borough of Tower Hamlets Pension Fund

Barry McKay

Barry McKay FFA

For and on behalf of Hymans Robertson LLP

30 September 2016

Executive Summary

Initial results

The initial draft whole fund results of the valuation are set out below based on your proposed funding basis: The results at the 2013 formal valuation are shown for comparison.

Valuation Date	31 March 2013	31 March 2016
Past Service Liabilities	**(£m)**	**(£m)**
Employees	451	414
Deferred Pensioners	297	320
Pensioners	546	627
Total Liabilities	**1,293**	**1,361**
Assets	**928**	**1,126**
Surplus / (Deficit)	**(365)**	**(235)**
Funding Level	**71.8%**	**82.7%**

Assumptions

The key financial and demographic assumptions proposed for the 2016 valuation are set out below:

	31 March 2013	31 March 2016
Financial		
Discount rate	4.6%	4.2%
Benefit increases	2.5%	2.1%
Salary increases	3.8%	2.0%
Demographic		
Baseline Longevity	Club Vita	Club Vita
Future Improvements	CMI2010, Peaked, 1.25% p.a. long term	CMI2013, Peaked, 1.25% p.a. long term

Solvency

The funding level on your proposed funding basis has improved from 71.7% in 2013 to 82.7% in 2016. Additionally, the funding deficit has decreased. The main reasons for the change in the funding level over the period were:

- better than anticipated investment returns;
- changed financial assumptions; and
- membership experience.

Contribution rates

Every employer has their own tailored funding plan and valuation results will vary depending on their own membership, funding plan and experience since the last valuation (or since they joined the Fund). The change in the financial assumptions and the positive investment returns and membership experience will allow contributions to be stable in many cases, however this will be heavily dependent on the period of participation in the Fund.

Next steps

The purpose of this report is to present the initial whole fund solvency results and summarise the experience over the intervaluation period. This report is useful to identify any areas of potential risk that the Fund may want to consider and explore possible avenues of risk mitigation during the valuation process.

The next milestone in the valuation process is to agree the funding target (assumptions) at Whole Fund level and prepare draft individual employer results.

Contents

1. Introduction

We have been commissioned by London Borough of Tower Hamlets (“the Administering Authority”) to carry out a full actuarial valuation of the London Borough of Tower Hamlets Pension Fund (“the Fund”) as at 31 March 2016 as required under Regulation 62 of the Local Government Pension Scheme Regulations 2013 (“the Regulations”). This report has been prepared to communicate the initial results of the 2016 valuation at whole fund level. It sets out the following:

- an analysis of Fund experience over the valuation period;
- your proposed funding assumptions;
- whole Fund valuation results; and
- analysis to help inform the Fund’s understanding of its risk exposure.

This report is addressed to London Borough of Tower Hamlets in its role as Administering Authority to the London Borough of Tower Hamlets Pension Fund. It should not be shared with any third parties without our prior written consent. Where consent is given, the report should be supplied in full including any related reliances and limitations.

Please note that Hymans Robertson LLP accept no liability to any third parties. The reliances and limitations in the body and appendices of this report apply equally to all users of this report.

2. Intervaluation Experience

Since the previous valuation, various events have taken place which affect the funding position of the Fund.

Investment returns	Expected	Actual	Difference	Impact
Over 3 year period	14.4%	19.7%	5.3%	Positive
Annual	4.6%	6.2%	1.6%	Positive

Assumption/measure	2013	2016	Difference	Impact
Long-dated gilt yields (p.a.)	3.0%	2.2%	(0.8%)	Negative
Expected inflation	3.3%	3.2%	(0.1%)	Positive

Investment returns

The Fund has experienced better than anticipated investment returns. The return in excess of the 2013 valuation discount rate serves to 'pay back' a greater portion of the deficit than expected (all other things being equal). Therefore, all other things being equal, this improves the funding position and reduces the reliance on contributions to repair funding deficits.

Gilts and inflation

There has been a significant drop in gilt yields over the inter-valuation period which is reflected in a reduction in anticipated investment returns and therefore a reduction in the discount rate used to place a value on the liabilities. This increases the liabilities and puts upwards pressure on employer contribution rates.

However, long term expectations for Retail Prices Inflation (RPI) and Consumer Price Inflation (CPI) have fallen since 2013 and this will offset the increases caused by the fall in gilt yields.

Fund expenses

The Fund's expenses (in relation to non-investment activities) over the last 3 years have totalled £2.9m. This figure is equivalent to 0.6% when expressed as a percentage of pensionable pay. Unless otherwise instructed, we propose to make allowance for the Fund's expenses by adding an allowance of 0.6% of pay to employer contribution rates payable from 1 April 2017.

Membership experience

The areas of membership experience that have had the greatest effect on the results of the valuation are set out below:

	Expected	Actual	Difference	Impact
Pre-retirement experience				
Early leavers (no.of lives)	3,019	2,333	(686)	Negative
Ill-health retirements* (no.of lives)	93	66	(27)	Positive
Salary increases (p.a.)	4.3%	1.8%	(2.6%)	Positive
Post-retirement experience				
Benefit increases (p.a.)	2.5%	1.3%	(1.2%)	Positive
Pensions ceasing (£m)	2.7	2.3	(0.4)	Negative

**Tier1 and Tier 2 ill-health retirements only*

The impact of less members withdrawing than expected depends on the age and liability distribution of withdrawing members. Although in number terms there were considerably fewer withdrawals than expected, the impact on the funding position was only very slightly negative for the Fund.

The pensioner mortality experience has been very close to expectations helped by the Fund's use of Club Vita to inform the longevity assumption. Membership experience overall has been positive over the intervaluation period. The most significant items of experience to note are:

- Salary increases have been less than assumed;

- Pension increases have been less than assumed; and

50/50 take-up has been significantly lower than expected, but take-up has been concentrated amongst those with the most significant liabilities.

Regulatory experience

The Fund is subject to risks beyond its control. In particular, since 2013:

- A new benefit structure has come into force;
- Funds have come under greater scrutiny from the Government Actuary's Department, the Scheme Advisory Board and the Department for Communities and Local Government (DCLG); and
- Cost controls may alter member benefits (but will have no effect on the 2016 valuation).

3. Data and Assumptions

Data

We have relied on the data provided by the Administering Authority when carrying out our calculations. The accuracy of our results is limited by the quality of the data provided. We are carrying out validations on the data provided to ensure it is fit for the purpose of the valuation. Further details can be found in our paper entitled "Data report for 2016 valuation", which will be issued shortly. Once fully validated we believe the membership data will be of an acceptable standard for the purposes of this valuation.

Financial assumptions

Your proposed financial assumptions are set out below, along with the assumptions adopted for the 2013 formal valuation:

Financial assumptions	31 March 2013	31 March 2016
Discount rate		
Return on long-dated gilts	3.0%	2.2%
Asset Outperformance Assumption	1.6%**	2.0%***
Discount rate	**4.6%**	**4.2%**
Benefit increases		
Retail Prices Inflation (RPI)	3.3%	3.2%
Assumed RPI/CPI* gap	(0.8%)**	(1.0%)***
Benefit increase assumption (CPI)	**2.5%**	**2.1%**
Salary increases		
Retail Prices Inflation (RPI)	3.3%	3.2%
Increases in excess of RPI	0.5%**	(1.2%)***
Salary increase assumption	**3.8%**	**2.0%**

** Consumer Prices Index*

*** Arithmetic deduction*

**** Geometric deduction*

Longevity assumptions

Your proposed longevity assumptions result in the following typical future life expectancies from age 65 (figures for 2013 shown for comparison):

	31 March 2013	31 March 2016
Male		
Pensioners	22.2 years	22.1 years
Non-pensioners	24.3 years	23.9 years
Female		
Pensioners	24.2 years	24.1 years
Non-pensioners	26.4 years	25.8 years

Non-pensioners are assumed to be aged 45 at 31 March 2016

Additional assumptions

Retirement age pattern

We have adopted the retirement age pattern assumption as specified by the Scheme Advisory Board for preparing Key Performance Indicators. Further details about this assumption are available on request.

50/50 option

Following analysis of both the Fund's actual take up rate, and national statistics, the Fund has assumed that 1% of members will take up the 50/50 option in the future.

Other assumptions

All other assumptions have been updated to reflect the latest experience of LGPS funds. Further details regarding the assumptions adopted can be found in notes 6 and 7 of the '2016 valuation toolkit'. Full details will be provided in our formal valuation report.

4. Initial Results - Solvency

The solvency of the Fund as at 31 March 2016 based on your proposed assumptions is set out below. The results at the 2013 formal valuation are shown for comparison.

Valuation Date	31 March 2013	31 March 2016
Past Service Liabilities	**(£m)**	**(£m)**
Employees	451	414
Deferred Pensioners	297	320
Pensioners	546	627
Total Liabilities	**1,293**	**1,361**
Assets	**928**	**1,126**
Surplus / (Deficit)	**(365)**	**(235)**
Funding Level	**71.8%**	**82.7%**

We have valued the benefits defined under the Regulations based on the assumptions outlined earlier. These results are sensitive to the underlying financial and demographic assumptions as well as the quality of the underlying data.

Liabilities

The main items driving the increase in the liabilities have been membership movements, the cost of the new benefits accruing and the interest on the previous deficit.

Assets

The assets have also grown substantially over the inter-valuation period as a result of better than assumed asset returns and contribution made towards the deficit.

Funding level/deficit

The overall result has been an improvement in the reported funding level of the Fund alongside a reduction in the funding deficit.

Analysis of change in solvency

The table below illustrates the various factors that have led to the change in funding position between the 2013 and 2016 valuations.

Analysis		(£m)
Surplus / (deficit) at 31 March 2013		**(365)**
Interest on surplus / (deficit)	(53)	
Investment returns greater than expected	46	
Contributions greater than cost of accrual	38	
Membership experience over the period	66	
Change in demographic assumptions	6	
Change in base mortality assumption	16	
Change in longevity improvements assumption	1	
Change in financial assumptions	33	
Impact of LGPS 50/50 take up	(7)	
Other experience items	(16)	
Surplus / (deficit) at 31 March 2016		**(235)**

Comment on employers

Every employer is valued separately based on their own membership data as a part of the valuation and their change in funding position will therefore vary compared to that of the whole fund.

5. Initial Results – Contributions

Changes to terminology

The Regulations have introduced new terminology in respect of contribution rates. We have set out our interpretation of these terms below based on CIPFA guidance on preparing a Funding Strategy Statement.

Primary Contribution Rate

This refers to the cost of new benefits being earned by members. This was previously referred to as the Future Service Rate.

Secondary Contribution Rate

This refers to the contributions required to repair an employer's deficit (surplus). This was previously referred to as Deficit Recovery Contributions.

Common Contribution Rate

The Regulations no longer require the reporting of the Common (Whole Fund) Contribution Rate. This has been replaced by Whole Fund Primary and Secondary Contribution Rates calculated as the payroll weighted average of the Primary and Secondary Contribution Rates for employer. These rates will be calculated and disclosed in the final valuation report.

Typical employer results

The net discount rate for benefits accruing under the CARE scheme is unchanged and so the Primary Contribution Rates will remain stable. Employer deficit results are more difficult to predict due to the variable changes in funding levels. Therefore, we anticipate for most employers that there will be upward but manageable pressure on employer contribution rates for the majority of employers in the Fund.

Employer categorisation

Every employer in the Fund is different. For instance, they have different funding levels, sources of funds for paying contributions, covenants, maturity profiles, and timeframes for their participation in the Fund.

As a result, when setting contribution rates, employers are categorised based on their individual characteristics in order to build a credible funding plan that fits their own needs while recognising the risk they pose the Fund and other participating employers.

Setting credible funding plans

Set a funding target

For the vast majority of employers, the target is to be fully funded on the Fund's ongoing funding assumptions. There may be instances where alternative assumptions are used such as where an employer is approaching cessation.

Choosing an appropriate time horizon

Once a target has been chosen, the time employers are given to reach that target needs to be determined. For long-term secure employers, this is up to 20 years. For employers that pose a greater risk to the Fund, this may be much shorter. In general, a shorter time horizon results in more volatile contributions compared to employers with longer time horizons.

Probability of reaching the target

The final stage involves determining the probability required for each employer to reach its funding target within its time horizon. In general, higher probabilities of success are achieved by paying higher contributions and relying less on volatile investment returns. The probability required for each employer is largely based on each employer's assessed covenant. For instance, a lower probability of success (e.g. 66%) may be required for a secure body as they may be considered to be able to pay higher contributions (or current rates for longer) should they not reach their funding target over their time horizon.

6. Risk Analysis

The valuation results depend critically on the actuarial assumptions that are made about the future of the Fund. If all of the assumptions made at this valuation were exactly borne out in practice then the results presented in this document would represent the true cost of providing benefits from the Fund as it currently stands at 31 March 2016.

However, no one can predict the future with certainty and future experience will not exactly match all of our assumptions. The future therefore presents a variety of risks to the Fund which should be **identified** and, where possible, the financial significance should be **quantified**. Thereafter the Fund can assess how (or if) these risks can then be **controlled** or **mitigated** and put in place **monitoring** to assess whether any mitigation is actually working.

Financial risks

The two main areas of financial risk of interest to your Fund are the investment performance and level of benefit increases. To help understand the impact of these two factors being different from assumed, we have shown the effects on the solvency measure of varying the discount rate (investment performance) and benefit increase assumptions below.

		Benefit Increases			
Discount Rates		2.0%	2.1%	2.2%	
	4.3%	(196) 85%	(215) 84%	(235) 83%	(Deficit) Funding Level
	4.2%	(215) 84%	(235) 83%	(255) 82%	(Deficit) Funding Level
	4.1%	(234) 83%	(255) 82%	(275) 80%	(Deficit) Funding Level

The above analysis focuses on financial risk to the solvency level. Our approach to setting contribution rates at the 2016 valuation seeks to recognise the uncertainty around future investment returns and benefit increases. Further information about this method will be provided with the employer results.

Demographic assumptions

The main area of demographic risk is people living longer than expected. We have shown below the high level impact of people living longer than currently expected by using a more prudent assumption for future longevity improvements. The more prudent assumption assumes that the rate of future improvements continues to increase ('non-peaked'). The valuation assumption assumes that the rate of future improvements have peaked.

	Peaked improvements	Non-peaked improvements
(Deficit) Funding Level	(235) 83%	(267) 81%

Other risks to consider

There are other risk factors which would have an impact on the funding position. Examples of these include the level of ill health retirements, withdrawals from the scheme and take up of the 50:50 option. These are probably unlikely to change in such a way that would rank them as amongst the highest risks facing the Fund and therefore we have not sought to provide further quantification of their risk.

Other events

Since carrying out the valuation, the United Kingdom held a referendum on its participation as a full member of the European Union. The result was a mandate to leave the European Union. At this time, it is difficult to predict the long term effect of this possible course of action. We have made no allowance for the referendum result in preparing this report

7. Next Steps

The purpose of this report is to present the initial whole fund solvency results and summarise the experience over the intervaluation period. This report is useful to identify any areas of potential risk that the Fund may want to consider and explore possible avenues of risk mitigation during the valuation process.

The next steps in the process are as follows.

- All parties to ***understand the whole fund results*** and the assumptions on which they are based, discuss any questions or issues before moving on to the next stage of the valuation process. This includes the Fund ***identifying any areas of risk*** that it is concerned about and wishes to explore further and understand how the risk can be identified, quantified, mitigated and monitored.
- Once all parties are happy with the whole fund results, we will quantify the ***valuation results for each individual employer*** that participates in the Fund. When we present you with these results, we will set out the contribution rates that each employer should pay for the next three years from 1 April 2017 based on the funding principles previously discussed.
- For some employers, the contribution rate that they should pay in principle may be different to what they will actually pay in practice. Any deviation will be based on their own circumstances and a range of factors including (amongst other things) their perceived security, whether they are going to be pooled with other employers or any budgetary constraints that they may be bound by. We expect there to be a consultation period where you gather together all of these issues and ***come back to us with a set of final agreed contribution rates for each employer.***
- We understand that you may require additional input from us before agreeing the final contribution rates. Some employers may accept their proposed contribution rates quite readily whilst others may want to explore their options. You may want us to look at the viability of ***different contribution strategies*** that are proposed by individual employers.
- Once a set of final contribution rates have been agreed for all employers, we will provide you with a ***final valuation report*** which will clearly set out the final valuation results and will meet all the relevant regulatory requirements. Included in this report will be the Certificate of Rates and Adjustments, which will certify the minimum contribution rates to be paid by each employer for the three year period beginning on 1 April 2017. This final valuation report must be provided to you no later than 31 March 2017.

Appendix – Reliances and limitations

This document has been requested by and is provided to London Borough of Tower Hamlets in its capacity as Administering Authority to the London Borough of Tower Hamlets Pension Fund. It has been prepared by Hymans Robertson LLP to support a discussion on funding strategy with the Fund as part of the 2016 funding valuation.

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

Reliances and limitations

This document has been prepared for the purpose of communicating the initial results of the 2016 valuation at whole fund level. Nothing contained within it affects any member's benefits. Furthermore, none of the figures should be used for accounting purposes (e.g. under FRS102 or IAS19) or for any other purpose (e.g. a termination valuation).

The valuation results are wholly dependent on the data provided to us and the assumptions that we use in our calculations. We are carrying out validations on the data provided to ensure it is fit for the purpose of the valuation. Further details can be found in our paper entitled "Data report for 2016 valuation", which will be issued shortly once fully validated. We believe the membership data will be of a good standard and fit for the purposes of this valuation.

It is possible that as part of our ongoing discussions you may find that there is additional information you should provide us with. In a similar way, you may feel that one or more of the assumptions is no longer not suitable for the Fund and you may wish to explore the use of alternatives. Until both of these

areas are definitively agreed by all relevant parties, the results in this document will remain "initial" and could be subject to change before the final valuation report is signed off.

This document is a "component report" of the eventual final aggregate valuation report due to be completed by 31 March 2017.

The results contained in this document are for the Fund as a whole. It does not set out the valuation results for individual employers, which will be derived at a later date. Employers come in different shapes and sizes and their valuation results are not uniform. We would advise against extrapolating the results contained in this document to predict possible contribution rates for employers at this stage.

The figures in this report are based on our understanding of the benefit structure of the LGPS as at 31 March 2016.

Actuarial Standards

The following Technical Actuarial Standards[1] are applicable in relation to this report and have been complied with where material:

- TAS R – Reporting;
- TAS D – Data;
- TAS M – Modelling; and
- Pensions TAS.

[1] Technical Actuarial Standards (TASs) are issued by the Financial Reporting Council (FRC) and set standards for certain items of actuarial work.

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Government
Actuary's
Department

LGPS ENGLAND AND WALES

Appendices to Section 13 Dry Run Report

Date: July 2016

Author: John Bayliss
Ian Boonin

Contents

Appendix A: Section 13 of the Public Service Pensions Act 2013[1]

13 Employer contributions in funded schemes

(1) This section applies in relation to a scheme under section 1 which is a defined benefits scheme with a pension fund.

(2) Scheme regulations must provide for the rate of employer contributions to be set at an appropriate level to ensure—

(a) the solvency of the pension fund, and

(b) the long-term cost-efficiency of the scheme, so far as relating to the pension fund.

(3) For that purpose, scheme regulations must require actuarial valuations of the pension fund.

(4) Where an actuarial valuation under subsection (3) has taken place, a person appointed by the responsible authority is to report on whether the following aims are achieved—

(a) the valuation is in accordance with the scheme regulations;

(b) the valuation has been carried out in a way which is not inconsistent with other valuations under subsection (3);

(c) the rate of employer contributions is set as specified in subsection (2).

(5) A report under subsection (4) must be published; and a copy must be sent to the scheme manager and (if different) the responsible authority.

(6) If a report under subsection (4) states that, in the view of the person making the report, any of the aims in that subsection has not been achieved—

(a) the report may recommend remedial steps;

(b) the scheme manager must—

(i) take such remedial steps as the scheme manager considers appropriate, and

(ii) publish details of those steps and the reasons for taking them;

(c) the responsible authority may—

(i) require the scheme manager to report on progress in taking remedial steps;

(ii) direct the scheme manager to take such remedial steps as the responsible authority considers appropriate.

(7) The person appointed under subsection (4) must, in the view of the responsible authority, be appropriately qualified.

[1] http://www.legislation.gov.uk/ukpga/2013/25/section/13

Appendix B: Extracts from other relevant regulations

Regulations 35 and 36 from 'The Local Government Pension Scheme (Administration) Regulations 2008[2]'

Funding strategy statement

35.–(1) This regulation applies to the funding strategy statement prepared and published by an administering authority under regulation 76A of the 1997 Regulations[3].

(2) The authority must—

(a) keep the statement under review;

(b) make such revisions as are appropriate following a material change—

(i) in its policy on the matters set out in the statement, or

(ii) to the current version of its statement under regulation 9A of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (statement of investment principles); and

(c) if revisions are made, publish the statement as revised.

(3) In reviewing and making revisions to the statement, the authority must—

(a) have regard to the guidance set out in the document published in March 2004 by CIPFA and called "CIPFA Pensions Panel Guidance on Preparing and Maintaining a Funding Strategy Statement (Guidance note issue No.6)"; and

(b) consult such persons as it considers appropriate.

Actuarial valuations and certificates

36.–(1) Each administering authority must obtain—

(a) an actuarial valuation of the assets and liabilities of each of its pension funds as at 31st March 2010 and in every third year afterwards;

(b) a report by an actuary in respect of the valuation; and

(c) a rates and adjustments certificate prepared by an actuary.

(2) Each of those documents must be obtained before the first anniversary of the date ("the valuation date") as at which the valuation is made or such later date as the Secretary of State may agree.

(3) A report under paragraph (1)(b) must contain a statement of the demographic assumptions used in making the valuation; and the statement must show how the assumptions relate to the events which have actually occurred in relation to members of the Scheme since the last valuation.

[2] http://www.legislation.gov.uk/uksi/2008/239/contents/made
[3] Regulation 76A was inserted by The Local Government Pension Scheme (Amendment) Regulations 2004

(4) A rates and adjustments certificate is a certificate specifying—

(a) the common rate of employer's contribution; and

(b) any individual adjustments,

for each year of the period of three years beginning with 1st April in the year following that in which the valuation date falls.

(5) The common rate of employer's contribution is the amount which, in the actuary's opinion, should be paid to the fund by all bodies whose employees contribute to it so as to secure its solvency, expressed as a percentage of the pay of their employees who are active members.

(6) The actuary must have regard to—

(a) the existing and prospective liabilities of the fund arising from circumstances common to all those bodies;

(b) the desirability of maintaining as nearly constant a common rate as possible; and

(c) the current version of the administering authority's funding strategy statement mentioned in regulation 35.

(7) An individual adjustment is any percentage or amount by which, in the actuary's opinion, contributions at the common rate should, in the case of a particular body, be increased or reduced by reason of any circumstances peculiar to that body.

(8) A rates and adjustments certificate must contain a statement of the assumptions on which the certificate is given as respects—

(a) the number of members who will become entitled to payment of pensions under provisions of the Scheme; and

(b) the amount of the liabilities arising in respect of such members,

during the period covered by the certificate.

(9) The authority must provide the actuary preparing a valuation or a rates and adjustments certificate with the consolidated revenue account of the fund and such other information as he requests.

Regulation 12 of 'The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009[4]'

Statement of investment principles

12.–(1) An administering authority must, after consultation with such persons as it considers appropriate, prepare, maintain (in accordance with paragraph (5)) and publish a written statement of the principles governing its decisions about the investment of fund money.

(2) The statement must cover its 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.

(3) The statement must also state the extent to which the administering authority complies with guidance given by the Secretary of State, and, to the extent the authority does not so comply, the reasons for not complying.

(4) The first such statement must be published no later than 1st July 2010.

(5) The statement must be reviewed, and if necessary, revised, by the administering authority from time to time and, in the case of any material change in the authority's policy on the matters referred to in paragraphs (2) and (3), before the end of a period of six months beginning with the date of that change.

(6) A statement revised under paragraph (5) must be published.

[4] http://www.legislation.gov.uk/uksi/2009/3093/regulation/12/made

Regulations 58 and 62 of 'The Local Government Pension Scheme Regulations 2013[5]'

Funding strategy statement

58.–(1) An administering authority must, after consultation with such persons as it considers appropriate, prepare, maintain and publish a written statement setting out its funding strategy.

(2) The statement must be published no later than 31st March 2015.

(3) The authority must keep the statement under review and, after consultation with such persons as it considers appropriate, make such revisions as are appropriate following a material change in its policy set out in the statement, and if revisions are made, publish the statement as revised.

(4) In preparing, maintaining and reviewing the statement, the administering authority must have regard to—

(a) the guidance set out in the document published in March 2004 by CIPFA, the Chartered Institute of Public Finance and Accountancy and called "CIPFA Pensions Panel Guidance on Preparing and Maintaining a Funding Strategy Statement (Guidance note issue No. 6)[6]"; and

(b) the statement of investment principles published by the administering authority under regulation 12 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009.

Actuarial valuations of pension funds

62.–(1) An administering authority must obtain—

(a) an actuarial valuation of the assets and liabilities of each of its pension funds as at 31st March 2016 and on 31st March in every third year afterwards;

(b) a report by an actuary in respect of the valuation; and

(c) a rates and adjustments certificate prepared by an actuary.

(2) Each of those documents must be obtained before the first anniversary of the date ("the valuation date") as at which the valuation is made or such later date as the Secretary of State may agree.

(3) A report under paragraph (1)(b) must contain a statement of the demographic assumptions used in making the valuation; and the statement must show how the assumptions relate to the events which have actually occurred in relation to members of the Scheme since the last valuation.

(4) A rates and adjustments certificate is a certificate specifying—

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[5] http://www.legislation.gov.uk/uksi/2013/2356/contents/made

[6] ISBN Number 085299 996 8; copies may be obtained from CIPFA at 3 Robert Street, London, WC2N 6RL

(a) the primary rate of the employer's contribution; and

(b) the secondary rate of the employer's contribution,

for each year of the period of three years beginning with 1st April in the year following that in which the valuation date falls.

(5) The primary rate of an employer's contribution is the amount in respect of the cost of future accruals which, in the actuary's opinion, should be paid to a fund by all bodies whose employees contribute to it so as to secure its solvency, expressed as a percentage of the pay of their employees who are active members.

(6) The actuary must have regard to—

(a) the existing and prospective liabilities arising from circumstances common to all those bodies;

(b) the desirability of maintaining as nearly constant a common rate as possible;

(c) the current version of the administering authority's funding strategy mentioned in regulation 58 (funding strategy statements); and

(d) the requirement to secure the solvency of the pension fund and the long term cost efficiency of the Scheme, so far as relating to the pension fund.

(7) The secondary rate of an employer's contributions is any percentage or amount by which, in the actuary's opinion, contributions at the primary rate should, in the case of a Scheme employer, be increased or reduced by reason of any circumstances peculiar to that employer.

(8) A rates and adjustments certificate must contain a statement of the assumptions on which the certificate is given as respects—

(a) the number of members who will become entitled to payment of pensions under the provisions of the Scheme; and

(b) the amount of the liabilities arising in respect of such members,

during the period covered by the certificate.

(9) The administering authority must provide the actuary preparing a valuation or a rates and adjustments certificate with the consolidated revenue account of the fund and such other information as the actuary requests.

Appendix C: Data provided

C.1 At the request of the Department for Communities and Local Government ('DCLG') the Government Actuary's Department ('GAD') has collected data from each fund's 2013 valuation report. These actuarial funding valuations were conducted by four actuarial firms:

> Aon Hewitt

> Barnett Waddingham

> Hymans Robertson

> Mercer

C.2 Data were received from the relevant local actuary or the administering authority for 89 of the 91 pension funds. Information for the Environment Agency Closed Fund and South Yorkshire Passenger Transport Authority Pension Fund have been taken directly from their respective 2013 valuation reports by GAD.

C.3 Limited checks, consisting of spot checks to make sure that data entries appear sensible, have been performed by GAD and the data received appears to be of sufficient quality for the purpose of analysing the 2013 valuation results. These checks do not represent a full, independent audit of the data supplied. The analysis contained in this report relies on the general completeness and accuracy of the information supplied by the administering authority or their actuaries.

C.4 In addition, data has been collated from the '*Local government pension scheme funds local authority data*', which is published annually by DCLG. This published data may be referred to elsewhere as SF3 statistics.

C.5 Unless otherwise stated the data detailed above has been used to inform the analysis contained in the LGPS England and Wales Section 13 Dry Run Report.

C.6 The original data request sent to individual funds for the collection of 2013 valuation data and accompanying explanatory notes now follow.

Data specification

1) MEMBERSHIP DATA
Data split by gender.

a) Active members: number, average age (weighted as appropriate), average period of membership, total rate of annual actual pensionable pay at 31 March 2013, total rate of annual FTE pensionable pay at 31 March 2013,
b) Deferred members: number, average age (weighted as appropriate), total annual preserved pension revalued to 31 March 2013. Note this should exclude undecided members.
c) Pensioners (former members): number, average age (weighted as appropriate), total annual pensions in payment at 31 March
d) Pensioners (dependants including partners and children): number, average age (weighted as appropriate), total annual pensions in payment at 31 March
e) Pensionable pay definition, has the 2008 or 2014 definition been used to assess pensionable pay

2) FINANCIAL ASSUMPTIONS
Provide separately for past service liabilities and future contributions, if different assumptions adopted. If different assumptions are adopted for Scheduled bodies and Admitted bodies the assumptions adopted for Scheduled bodies should be entered.

a) Nominal discount rate (pre & post retirement separately if applicable)
b) RPI inflation
c) CPI inflation rate
d) Earnings inflation

3) DEMOGRAPHIC ASSUMPTIONS
Rates to be provided at sample ages split by gender

a) Age Retirement Assumptions (split between members with and without Rule of 85 protection)
b) Rates of Ill-health Retirement from Active service
c) Distribution of ill health retirements between tiers 1, 2 and 3
d) Rates of Withdrawal from Active service
e) Death in Service Rates
f) Promotional Salary Scale (if not included in earnings inflation assumption)
g) Proportions Partnered
h) Age disparity between Member & Partner
i) Commutation Assumptions
j) Assumed life expectancy for pensioner members aged 65 and active / deferred members at age 65 if they are currently aged 45 (for members retiring on normal health, members retiring on ill health and dependents)
k) Description of post retirement mortality assumption (baseline and future improvements)

4) ASSETS
a) Value of Assets (market value)
b) Actual Asset Distribution (split by UK equities, overseas equities, corporate bonds, gilts, property, cash and other investments).

5) LIABILITIES AND FUTURE CONTRIBUTION RATE
a) Common contribution rate
b) Standard Contribution Rate
c) Contribution rate in respect of surplus or deficit
d) Assumed member contribution yield
e) Expenses, split by administration and (if not included implicitly in discount rate) investment

f) Past Service Liability – split between Actives, Deferred and Pensioners
g) Funding Level
h) Surplus / Deficit at valuation date
i) Deficit Recovery Period
j) Past Service Liability (on a low risk / gilts basis) – split between Actives, Deferred and Pensioners

6) REVENUE ACCOUNTS
a) Value of assets at last valuation (after any smoothing or other adjustments)
b) Value of assets at this valuation (after any smoothing or other adjustments)
c) Total Income: Employee contributions, normal employer contributions, special employer contributions, transfers in, investment income, other income
d) Total Expenditure: Pensions paid, retirement lump sums paid, other lump sums paid, transfers out, investment expenses, administration expenses, other outgoings

7) ANALYSIS OF SURPLUS (PAST SERVICE LIABILITY)
a) Surplus / Deficit at last valuation
b) Interest on Surplus/Deficit
c) Difference between contribution paid and cost of benefits accrued
d) Experience gains and losses (including amounts in the following categories where analysed: Investment Return experience, Salary Increase experience, Pension Increase experience, Pensioner Mortality experience, Other Demographic experience)
e) Change in assumptions (including amounts in the following categories where analysed: financial assumptions, mortality assumptions, other demographic assumptions)
f) Other
g) Surplus / Deficit at this valuation

8) ANALYSIS OF CHANGE IN FUTURE SERVICE CONTRIBUTION RATE
a) Future service rate at last valuation
b) Effect of change in assumptions (including amounts in the following categories where analysed: financial assumptions, mortality assumptions, other demographic assumptions)
c) Change due to introduction new benefit design from April 2014
d) Other
e) Future service rate at this valuation (common contribution rate)

9) AVERAGE EMPLOYER CONTRIBUTION RATE
a) Average employer contribution rate 2014/15, allowing for both contributions paid as a percentage of salary and fixed monetary contributions (where deficit contributions are fixed)

10) EXPERIENCE OVER THE INTERVALUATION PERIOD
Please only provide data that is readily available

a) Actual and expected numbers of deaths in service
b) Actual and expected numbers of withdrawals
c) Actual and expected numbers of age retirements
d) Actual and expected numbers of ill-health retirements
e) Actual and expected pensioner deaths (by lives and amount of pension).
f) Actual and expected numbers of severance / redundancy
g) Actual and assumed amount of commuted lump sum

11) POST 2014 SCHEME

a) Proportion of members assumed to be in 50/50 scheme
b) State Pension Ages used for assessment

Explanatory notes

Common contribution rate: All data requested relates to the common contribution rate, unless otherwise noted.

1 **Membership data:** Average ages should be unweighted, weighted by salary/pension and weighted liability as available. Accrued pensions should include the 2013 Pension Increase Order.

3 **Demographic Assumptions:** We expect this to be shown at sample ages only which will be specified in our template. For example for in service decrement we intend to use five-year intervals from 20 to 65.

3j **Life expectancies:** The life expectancies requested in section 3 j) should be the average life expectancy across the whole fund.

5d **Assumed member contribution yield:** This is the contribution yield that members are assumed to pay over the valuation period. It will vary by authority due to the tiered member contribution rates.

9 **Average employer contribution rate:** This should be calculated as projected employer contributions in 2014/15 divided by projected pensionable pay in 2014/15. Since projected pensionable pay acts only as the weightings in this weighted average, it is acceptable to use a simple projection of pensionable pay (e.g. based on actual pensionable pay at 31 Mar 2013).

10 **Experience over the intervaluation period:** We would only expect experience that has been analysed and is readily available to be included in this section.

11b **State Pension Age used for assessment:** This item refers to the assumed State Pension Ages that have been used in the funding valuation, for example whether allowance has been made for the State Pension Age to increase from age 66 to 67 between 2026 and 2028 (which is Government Policy but has not yet been approved by Parliament).

Adjustment to results for City of Westminster Pension Fund and London Borough of Waltham Forest Pension Fund

C.7 As noted in paragraph 2.9, the purpose of the flags is to identify authorities with whom we might engage and potentially seek additional information from. The importance of clear disclosure in the valuation reports and accurate provision of data from the local authorities and the actuarial firms is highlighted by two examples from our analysis.

C.8 For the City of Westminster Pension Fund, we sought more information from the fund's actuary, clarifying the different actuarial basis that had been applied to some admission bodies, whereas our standard assessment methodology had relied on the same actuarial assumptions being applied for all participating employers in the fund except where this was clear from the valuation report. Based on this additional information, we recalculated our measures and have reported on this revised basis. The result was that Westminster raised only two amber flags.

C.9 For the Borough of Waltham Forest Pension Fund, following engagement with the fund's actuary, we were advised that a material proportion of members had seemingly been incorrectly classified in SF3 data returns. Upon receipt of data reflecting a revised classification of those members, we were able to conclude that Waltham Forest raised only one amber flag.

C.10 Following the 2016 valuation we will request more explicit information and our expectation is that this, together with having highlighted the need for clear and full disclosure and the production of liabilities on the SAB standard basis, will help to improve the overall quality of information provided.

Appendix D: Assumptions

D.1 Each section of analysis contained in the main report is based on one of three sets of assumptions:

> The local fund assumptions, as used in the fund's 2013 actuarial valuation

> The SAB standardised set of assumptions, or SAB standard basis

> A market consistent set of assumptions

D.2 Details of local fund assumptions can be found in each fund's actuarial valuation report as at 31 March 2013. An analysis of the differences in assumptions between funds is contained in the 'Consistency' chapter of the main report.

D.3 Details of the SAB standard basis and the market consistent basis can be found in the tables below. Differences between the bases are highlighted in orange.

Table D.1: SAB standard basis[7]

ASSUMPTION	DETAILS
METHODOLOGY	Projected Unit Methodology with 1 year control period
RATE OF PENSION INCREASES	2% per annum
PUBLIC SECTOR EARNINGS GROWTH	3.5% per annum
DISCOUNT RATE	5.06% per annum
POST RETIREMENT MORTALITY RATES	Long term reduction in mortality rates of 1.5% per annum
CHANGES TO STATE PENSION AGE	As legislated
PENSIONER BASELINE MORTALITY	Set locally based on Fund experience
AGE RETIREMENT	Set locally based on Fund experience
ILL HEALTH RETIREMENT RATES	Set locally based on Fund experience
WITHDRAWAL RATES	Set locally based on Fund experience
DEATH BEFORE RETIREMENT RATES	Set locally based on Fund experience
PROMOTIONAL SALARY SCALES	None
COMMUTATION	We have used the SAB future service cost assumption of 65% of the maximum allowable amount. This is equivalent to 23.2% of post 2008 pension and 12.8% of pre 2008 pension
FAMILY STATISTICS	Set locally based on Fund experience

[7] This is the 5 February 2015 iteration, details of which can be found in the minutes of the Scheme Advisory Board's meeting of 5 February 2015 at: http://www.lgpsboard.org/images/PDF/CMCMar2015/Item4-StandardisedFundingAssumptions.pdf

Table D.2: Market consistent basis

ASSUMPTION	DETAILS
METHODOLOGY	Projected Unit Methodology with 1 year control period
RATE OF PENSION INCREASES	2.25% per annum
PUBLIC SECTOR EARNINGS GROWTH	4.5% per annum
DISCOUNT RATE	5.92% per annum
POST RETIREMENT MORTALITY RATES	As set out in GAD's 2013 scheme wide actuarial valuation
CHANGES TO STATE PENSION AGE	As legislated
PENSIONER BASELINE MORTALITY	As set out in GAD's 2013 scheme wide actuarial valuation
AGE RETIREMENT	Set locally based on Fund experience
ILL HEALTH RETIREMENT RATES	Set locally based on Fund experience
WITHDRAWAL RATES	Set locally based on Fund experience
DEATH BEFORE RETIREMENT RATES	Set locally based on Fund experience
PROMOTIONAL SALARY SCALES	Set locally based on Fund experience
COMMUTATION	Set locally based on Fund experience
FAMILY STATISTICS	Set locally based on Fund experience

D.4 The financial assumptions under the market consistent basis were set with reference to GAD's best estimate view of future market movements as at 31 March 2013.

D.5 The post-retirement mortality assumptions are as set out in GAD's 2013 scheme wide actuarial valuation and were derived after analysing scheme wide mortality experience. The market consistent basis uses these assumptions rather than those set locally as analysis showed local rates, when taken as a whole, were materially higher (i.e. life expectancies were materially lower) than GAD's 2013 scheme wide rates.

D.6 Promotional salary scales and rates of commutation are likely to vary between funds. The market consistent basis allows for this variation by using the rates set in the local 2013 actuarial valuations.

Appendix E: Solvency measures – methodology

E.1 This Appendix details the methodology behind the measures used to assess a fund's solvency position. Some of the measures listed below were calculated using a market consistent set of assumptions. For more information on this market consistent basis please see Appendix D.

***SAB funding level:** A fund's funding level using the SAB standard basis*

E.2 This measure highlights possible risks to a fund as a result of assets being significantly lower than liabilities, where liabilities are those estimated on the SAB standard basis detailed in Appendix D.

E.3 A lower funding level may lead to greater default risk amongst employers without tax raising powers or statutory backing and can leave a fund at greater risk of adverse market movements.

E.4 This measure assesses the relative funding levels of individual funds. All funds have been ordered by this measure (highest funding level first) and the ten funds ranked 82 to 91, out of 91 are assigned an amber colour code. All other funds are assigned a green colour code.

***Open fund:** Whether the fund is open to new members*

E.5 A scheme that is closed to new members will be closer to maturity than a scheme which is still open. This creates a possible risk to sponsoring employees as there is less scope to make regular contributions and receive investment returns on those contributions. Additionally, if problems do occur with the scheme funding level, the reduced time maturity of the scheme means that additional contributions must be spread over a shorter timeframe, and could be more volatile as a result. Employer interest in the scheme may also start to wane and could lead to a failure to make required contributions in the future.

E.6 This measure is a *'Yes'* when a fund is still open to new members and a *'No'* otherwise. A *'Yes'* results in a green colour code, while a *'No'* results in an amber colour code.

***Non-statutory employees:** The proportion of employees within the fund who are employed by an employer without tax raising powers or statutory backing*

E.7 LGPS regulations require employers to pay contributions set in the valuation. DCLG has confirmed that:

> there is a guarantee of LGPS pension liabilities by a public body;

- that public bodies are incapable of becoming insolvent; and
- governing legislation is designed to ensure the solvency and long term economic efficiency of the Scheme.

E.8 It is important, in this context, that administering authorities and other employers understand the potential cost that may fall on taxpayers in the future if employers without statutory backing or tax raising powers are unable to meet their required contributions and those with such powers become responsible for the accrued costs.

E.9 Data for this measure has been taken from the publically available *'Local government pension scheme funds local authority data: 2014 to 2015'* published by DCLG[8]. The data contains the number of employees within each fund by employer group, where:

- Group 1 refers to local authorities and connected bodies;
- Group 2 refers to centrally funded public sector bodies;
- Group 3 refers to other public sector bodies; and
- Group 4 refers to private sector, voluntary sector and other bodies.

E.10 For the purposes of this measure, and unless information has been provided to the contrary, it has been assumed that employers listed under groups 1 and 2 are those ***with*** tax raising powers or statutory backing and that employers listed under groups 3 and 4 are those ***without*** tax raising powers or statutory backing.

E.11 The measure therefore gives the proportion of employees within the fund that are employed by group 1 and 2 employers as a proportion of all employees within the fund.

E.12 The proportions quoted in this report are based on number of employees as at March 2015 as the required data were not available for March 2013. However, it is assumed that this proportion will not have varied much over the two years from the date of the last triennial actuarial valuations, 31 March 2013. The 2016 Section 13 report will use proportions as at March 2016 which we plan to base on liabilities rather than number of employees.

E.13 The required data were not available for:

- Environment Agency Active Fund;
- London Borough of Haringey Pension Fund; and
- London Borough of Newham Pension Fund.

E.14 Under this measure a fund has been allocated a red colour code if their proportion of employees who are employed by an employer without tax raising powers or statutory backing is greater than 50%.

[8] https://www.gov.uk/government/collections/local-government-pension-scheme

E.15 A fund has been allocated an amber colour code if their proportion of employees who are employed by an employer without tax raising powers or statutory is between 25% and 50%, and a green colour code in all other cases.

Contribution cover: *Actual contributions paid by the fund as a proportion of local authority income*

E.16 This measure does not form part of this 2013 dry run report as the required data were unavailable. However, it is expected to be used as a measure of solvency in the 2016 Section 13 report.

E.17 Continued solvency of a fund depends on the ongoing ability of employers to pay contributions into the fund, which may be higher or lower than at present. If contributions are a low proportion of income (or outgo) employers are likely to find it easier to cope with any increase in contributions that is required.

E.18 This measure should give the actual contributions paid by the fund in the 2012/13 financial year as a proportion of local authority income over the same year. It is important to note that this measure is based on actual contributions. These may not be the same as the contribution rates derived in a fund's actuarial valuation as contribution rates are sometimes smoothed to reduce volatility. There may also have been additional lump sum contributions made.

E.19 Under this measure, a fund where the actual contributions paid as a proportion of local authority income are higher than x%[9] will be assigned a red colour code.

E.20 A fund where the actual contributions paid as a proportion of local authority income is between x% and y% will be assigned an amber colour code, while funds with a lower proportion will be assigned a green colour code.

Liability Shock: *The change in average employer contribution rates as a percentage of payroll after a 10% increase in liabilities*

E.21 Contribution rates are normally specified as a percentage of payroll. They are likely to vary at each triennial actuarial valuation in response to economic conditions, both at the time of the valuation and assumed future economic conditions, and fund experience over the inter-valuation period. These factors could cause either an increase or decrease in required contributions.

[9] Where a measure does not form part of the 2013 dry run report trigger points are listed as x% or y%. The actual level of these trigger point will be determined when completing the section 13 review following the 2016 local valuations.

E.22 The continued solvency of a fund depends on the ongoing ability of employers to pay the required contributions into the fund, whether they are higher or lower than at present. If contributions are a low proportion of a fund's payroll employers are likely to find it easier to meet increased required contributions.

E.23 Total employer contribution rates are often split into contributions required to cover the expected cost of future accrual of benefits and contributions required to eliminate any existing deficit. Contributions in respect of deficit will increase if a fund's deficit increases, i.e. if a fund's asset value falls or liabilities increase, assuming the assumptions underlying the deficit remain unchanged.

E.24 This measure investigates the effect of an increase in a fund's liabilities on total employer contribution rates, as a proportion of payroll. The necessary calculations have been undertaken by simulating a one-off increase to liabilities of 10% of their 31 March 2013 value. For the purposes of this measure, liabilities have been set out on the standardised market consistent basis and deficit recovery periods have been standardised using a period of 20 years to ensure that results are comparable. Where a fund is in surplus under the standardised market consistent basis, the surplus is assumed to be paid back to the employer over a period of 20 years through reduced contribution rates.

E.25 The measure is the change in total employer contribution rate from the resulting from the increase to liabilities. A high figure indicates that contributions rates as a proportion of payroll are highly sensitive to a change in liabilities. This could be a result of a low payroll.

E.26 A fund is allocated a red colour code if its result is greater than 7.5%, an amber colour code if its result is between 5.0% and 7.5% and a green colour code otherwise.

E.27 Note that no results are available for the Environment Agency Closed Fund as there are no remaining active members within the fund with which to calculate contribution rates.

Liability shock cover: *The change in average employer contribution rates as a percentage of local authority income after a 10% increase in liabilities*

E.28 This measure does not form part of this 2013 Section 13 report as the required data were unavailable. However, it is expected to be used as a measure of solvency in the 2016 Section 13 report.

E.29 The results under this measure are expected to be similar to those under the liability shock measure. This measure may therefore be used instead of, rather than in addition to, liability shock in the 2016 Section 13 Report.

E.30 It is likely that a fund where the required employer contributions are a low proportion of total income (or outgo) will be more able to meet any increase in contributions required at future valuations

E.31 Under both measures a fund will be allocated a red colour code if its result is greater than x%, an amber colour code if its result is between x% and y%, and a green colour code otherwise.

Asset shock: *The change in average employer contribution rates as a percentage of payroll after a 15% fall in value of return-seeking assets*

E.32 This measure shows the effect on total employer contribution rates (as a percentage of payroll) of a one off decrease in the value of a fund's return seeking assets equal to 15% of the value of those assets. Defensive assets are assumed to be unaffected.

E.33 For the purposes of this measure liabilities have restated on the standardised market consistent basis and deficit recovery periods have been standardised using a period of 20 years to ensure that results are comparable. Where a fund is in surplus under the standardised market consistent basis, the surplus is assumed to be paid back to the employer over a period of 20 years.

E.34 Return-seeking asset classes are assumed to be:

> Overseas Equities;
> UK Equities;
> Other Investments; and
> Property.

Defensive asset classes are assumed to be:

> Cash;
> Gilts; and
> Corporate Bonds.

E.35 We investigated the 'Other Investments' category in respect of the two funds flagged up red under this measure and it was found that only West Midland ITA had a significant amount, of which just over 80% related to a buy-in policy. This buy-in policy has been allowed for as a defensive asset in our calculations.

E.36 Under this measure, a fund invested entirely in return-seeking assets will experience a decrease in total asset value of 15%. A fund with no exposure to return-seeking assets will experience no decrease in total asset value. In practice, the majority of funds will experience decreases between these two extremes, dependant on their investment strategy.

E.37 In general we have treated 'other investments' in the same manner as equities. However, we have investigated the actual nature of 'other investments' where a flag has been raised. We intend to investigate in more depth for our 2016 Section 13 valuation report.

E.38 The one-off decrease in asset values results in an increase in fund deficits (or reduction in surpluses). As deficit recovery periods are constant, employer contributions in respect of deficits will increase. If contributions are a small proportion of payrolls employers are likely to be able to better cope with this increase.

E.39 The measure gives the change in contribution rate from the pre-decrease value. A high number indicates that contribution rates as a proportion of payroll are highly sensitive to a change in the value of return seeking assets.

E.40 A fund is allocated a red colour code if its result is greater than 7.5%, an amber colour code if its result is between 5.0% and 7.5% and a green colour code otherwise.

E.41 Note that no results are available for the Environment Agency Closed Fund as there are no remaining active members within the fund with which to calculate contribution rates.

Asset shock cover: *The change in average employer contribution rates as a percentage of local authority income after a 15% fall in value of return-seeking assets*

E.42 This measure does not form part of this 2013 Section 13 report as the required data were not available. However, it is expected to be used as a measure of solvency in the 2016 Section 13 report.

E.43 The results under this measure are expected to be similar to those under the asset shock measure. This measure may therefore be used instead of, rather than in addition to, the asset shock measure in the 2016 Section 13 Report.

E.44 It is likely that a fund where the required employer contributions are a low proportion of total income (or outgo) will be more able to meet any increase in contributions required at future valuations

E.45 The measure will be calculated in the same way as the asset shock measure, detailed above, except that total contribution rates and the increases resulting from a 15% fall in the value of return-seeking assets will be measured as a percentage of local authority income, rather than a percentage of payroll.

E.46 Under this measure a fund will be allocated a red colour code if its result is greater than x%, an amber colour code if its result is between x% and y% and a green colour code otherwise.

Employer default: *The change in average employer contribution rates as a percentage of payroll if all employer's without tax raising powers or statutory backing default on their existing deficits*

E.47 LGPS regulations require employers to pay contributions set in the valuation. DCLG has confirmed that:

> there is a guarantee of LGPS pension liabilities by a public body;

> that public body is incapable of becoming insolvent; and

> the governing legislation is designed to ensure the solvency and long term economic efficiency of the Scheme.

E.48 It is important, in this context, that administering authorities and other employers understand the potential cost that may fall on taxpayers in the future if employers without statutory backing or tax raising powers are unable to meet their required contributions and those with such powers become responsible for the accrued costs.

E.49 For the purposes of this measure liabilities have been restated on the standardised market consistent basis and deficit recovery periods have been standardised using a period of 20 years to ensure that results are comparable. Where a fund is in surplus under the standardised market consistent basis, the surplus is assumed to be paid back to the employer over a period of 20 years.

E.50 A fund's deficit will not change as a result of the default, but as the deficit is spread over a smaller number of employers each the contribution rate for each remaining employer will increase.

E.51 If a fund is in surplus it is assumed that those employers without tax raising powers or statutory backing default on their proportion of the surplus. This will have the effect of reducing contributions for those funds in surplus on the standardised market consistent basis who have a non-zero number of employees employed by employers without tax raising powers or statutory backing.

E.52 The measure shows the increase in total contribution rates that has resulted from the default of employers without tax raising powers or statutory backing.

E.53 Data were not available for:

> Environment Agency Active Fund;

> London Borough of Haringey Pension Fund; and

> London Borough of Newham Pension Fund.

E.54 A fund is allocated a red colour code if its result is greater than 3%, an amber colour code if its result is between 2% and 3% and a green colour code otherwise.

Employer default cover: *Average employer contribution rates as a percentage of local authority income if all employer's without tax raising powers or statutory backing default on their existing deficits*

E.55 This measure does not form part of this 2013 Section 13 report as the required data were not available. However, it is expected to be used as a measure of solvency in the 2016 Section 13 report.

E.56 The results under this measure are expected to be similar to those under the employer default measure. This measure may therefore be used instead of, rather than in addition to, the employer default measure in the 2016 Section 13 Report.

E.57 It is likely that a fund where the required employer contributions resulting from a default of employer's without tax raising powers or statutory backing are a low proportion of total income (or outgo) will be more able to meet any increase in contributions required.

E.58 The measure will be calculated as the increases resulting from the default measured as a percentage of local authority income.

E.59 A fund will be allocated a red colour code if its result is greater than x%, an amber colour code if its result is between x% and y% and a green colour code otherwise.

Appendix F: Solvency measures – by fund

Table F1: Solvency measures by fund

PENSION FUND	MATURITY (RANK)	SOLVENCY MEASURES					
		RISKS ALREADY PRESENT			EMERGING RISKS		
		SAB FUNDING LEVEL	OPEN FUND	NON-STATUTORY EMPLOYEES	LIABILITY SHOCK	ASSET SHOCK	EMPLOYER DEFAULT
AVON	5.9 (82)	92%	YES	6%	+3%	+4%	+0%
BARKING AND DAGENHAM	6.5 (45)	83%	YES	21%	+4%	+3%	+1%
BARNET	6.8 (31)	79%	YES	0%	+4%	+3%	+0%
BEDFORDSHIRE	5.9 (76)	78%	YES	4%	+3%	+3%	+0%
BERKSHIRE	5.9 (78)	73%	YES	6%	+3%	+3%	+1%
BEXLEY	7.4 (14)	99%	YES	7%	+4%	+6%	-0%
BRENT	6.9 (28)	67%	YES	0%	+4%	+3%	+0%
BROMLEY	6.8 (33)	93%	YES	2%	+4%	+5%	+0%
BUCKINGHAMSHIRE	5.6 (87)	81%	YES	5%	+3%	+3%	+0%
CAMBRIDGESHIRE	5.8 (83)	89%	YES	5%	+3%	+4%	+0%
CAMDEN	8.6 (7)	91%	YES	9%	+5%	+6%	+0%
CARDIFF AND GLAMORGAN	6.8 (32)	79%	YES	6%	+4%	+4%	+0%
CHESHIRE	6.5 (41)	95%	YES	8%	+4%	+4%	+0%
CITY OF LONDON	7.3 (18)	83%	YES	9%	+4%	+4%	+1%
CLWYD	6 (73)	83%	YES	1%	+3%	+4%	+0%
CORNWALL	5.8 (84)	93%	YES	7%	+3%	+4%	+0%
CROYDON	6.7 (37)	72%	YES	5%	+4%	+3%	+1%
CUMBRIA	6.7 (38)	96%	YES	0%	+4%	+4%	+0%
DERBYSHIRE	5.9 (77)	96%	YES	5%	+3%	+4%	+0%
DEVON	6.4 (48)	82%	YES	11%	+4%	+4%	+1%
DORSET	6 (74)	82%	YES	9%	+3%	+4%	+1%
DURHAM	6.9 (27)	86%	YES	3%	+4%	+4%	+0%
DYFED	5.6 (88)	105%	YES	4%	+3%	+4%	-0%
EALING	6.3 (53)	88%	YES	11%	+4%	+4%	+0%
EAST RIDING	6.3 (55)	93%	YES	4%	+4%	+4%	+0%

PENSION FUND	MATURITY (RANK)	SOLVENCY MEASURES					
		RISKS ALREADY PRESENT			EMERGING RISKS		
		SAB FUNDING LEVEL	OPEN FUND	NON-STATUTORY EMPLOYEES	LIABILITY SHOCK	ASSET SHOCK	EMPLOYER DEFAULT
EAST SUSSEX	6.3 (52)	98%	YES	2%	+4%	+5%	-0%
ENFIELD	6.1 (66)	85%	YES	3%	+4%	+3%	+0%
ENVIRONMENT AGENCY ACTIVE	5.8 (85)	103%	YES	N/A	+3%	+4%	N/A
ESSEX	6.2 (65)	83%	YES	16%	+4%	+4%	+1%
GLOUCESTERSHIRE	6.7 (36)	83%	YES	9%	+4%	+4%	+1%
GREATER MANCHESTER	7.2 (22)	103%	YES	22%	+4%	+5%	-1%
GREENWICH	7.2 (21)	85%	YES	6%	+4%	+5%	+0%
GWENT	5.9 (79)	84%	YES	6%	+3%	+4%	+0%
GWYNEDD	5.2 (90)	102%	YES	5%	+3%	+4%	-0%
HACKNEY	7.4 (15)	86%	YES	0%	+4%	+5%	+0%
HAMMERSMITH	8.9 (6)	83%	YES	6%	+5%	+6%	+0%
HAMPSHIRE	6.4 (50)	80%	YES	3%	+4%	+3%	+0%
HARINGEY	7.8 (11)	84%	YES	N/A	+4%	+5%	N/A
HARROW	6.6 (39)	83%	YES	2%	+4%	+4%	+0%
HAVERING	6.8 (34)	68%	YES	1%	+4%	+3%	+0%
HERTFORDSHIRE	6.4 (49)	94%	YES	6%	+4%	+4%	+0%
HILLINGDON	6.2 (64)	83%	YES	25%	+4%	+3%	+1%
HOUNSLOW	6.3 (58)	84%	YES	14%	+4%	+3%	+1%
ISLE OF WIGHT	7.4 (16)	94%	YES	3%	+4%	+5%	+0%
ISLINGTON	6.8 (30)	86%	YES	7%	+4%	+4%	+0%
KENSINGTON AND CHELSEA	7.7 (13)	96%	YES	5%	+4%	+6%	-0%
KENT	6.2 (63)	83%	YES	10%	+4%	+4%	+1%
KINGSTON-UPON-THAMES	6.1 (71)	85%	YES	6%	+3%	+4%	+0%
LAMBETH	8.9 (5)	87%	YES	5%	+5%	+5%	+0%
LANCASHIRE	6.1 (70)	93%	YES	7%	+3%	+4%	+0%
LEICESTERSHIRE	5.7 (86)	85%	YES	5%	+3%	+3%	+0%
LEWISHAM	7.8 (10)	86%	YES	16%	+4%	+5%	+1%
LINCOLNSHIRE	6.3 (56)	85%	YES	8%	+4%	+4%	+0%

PENSION FUND	MATURITY (RANK)	SOLVENCY MEASURES					
		RISKS ALREADY PRESENT			EMERGING RISKS		
		SAB FUNDING LEVEL	OPEN FUND	NON-STATUTORY EMPLOYEES	LIABILITY SHOCK	ASSET SHOCK	EMPLOYER DEFAULT
LONDON PENSIONS FUND	9.6 (4)	92%	YES	0%	+6%	+4%	+0%
MERSEYSIDE	7.3 (17)	92%	YES	13%	+4%	+5%	+0%
MERTON	7.1 (25)	91%	YES	3%	+4%	+4%	+0%
NEWHAM	7.3 (19)	75%	YES	N/A	+4%	+4%	N/A
NORFOLK	6.6 (40)	91%	YES	9%	+4%	+4%	+0%
NORTH YORKSHIRE	5.3 (89)	87%	YES	3%	+3%	+3%	+0%
NORTHAMPTONSHIRE	6.2 (60)	85%	YES	4%	+4%	+4%	+0%
NORTHUMBERLAND	8.2 (8)	84%	YES	6%	+5%	+5%	+0%
NOTTINGHAMSHIRE	6.3 (54)	85%	YES	6%	+4%	+4%	+0%
OXFORDSHIRE	5.9 (75)	85%	YES	36%	+3%	+4%	+2%
POWYS	6.4 (46)	82%	YES	3%	+4%	+3%	+0%
REDBRIDGE	6.3 (51)	83%	YES	9%	+4%	+3%	+0%
RHONDDA CYNON TAF	6.1 (68)	77%	YES	5%	+3%	+3%	+0%
RICHMOND	7.1 (24)	97%	YES	3%	+4%	+5%	-0%
SHROPSHIRE	6.5 (43)	88%	YES	10%	+4%	+4%	+0%
SOMERSET	5.9 (80)	74%	YES	13%	+3%	+3%	+1%
SOUTH YORKSHIRE	6.4 (47)	94%	YES	10%	+4%	+4%	+0%
SOUTH YORKSHIRE PTA	25.2 (1)	114%	NO	100%	+5%	+3%	N/A
SOUTHWARK	7.3 (20)	84%	YES	2%	+4%	+4%	+0%
STAFFORDSHIRE	6.2 (59)	87%	YES	6%	+4%	+4%	+0%
SUFFOLK	6.2 (62)	93%	YES	19%	+4%	+3%	+0%
SURREY	5.9 (81)	86%	YES	5%	+3%	+4%	+0%
SUTTON	6.5 (42)	81%	YES	3%	+4%	+3%	+0%
SWANSEA	6.2 (61)	80%	YES	4%	+4%	+4%	+0%
TEESSIDE	6.8 (29)	103%	YES	13%	+4%	+5%	-0%
TOWER HAMLETS	8.1 (9)	85%	YES	0%	+5%	+5%	+0%
TYNE AND WEAR	7.1 (23)	87%	YES	11%	+4%	+4%	+0%
WALTHAM FOREST	7 (26)	73%	YES	5%	+4%	+4%	+1%

PENSION FUND	MATURITY (RANK)	SOLVENCY MEASURES					
		RISKS ALREADY PRESENT			EMERGING RISKS		
		SAB FUNDING LEVEL	OPEN FUND	NON-STATUTORY EMPLOYEES	LIABILITY SHOCK	ASSET SHOCK	EMPLOYER DEFAULT
WANDSWORTH	7.7 (12)	104%	YES	1%	+4%	+6%	-0%
WARWICKSHIRE	6.1 (67)	92%	YES	6%	+3%	+4%	+0%
WEST MIDLANDS	6.8 (35)	87%	YES	5%	+4%	+4%	+0%
WEST MIDLANDS ITA	25.1 (2)	100%	NO	100%	+5%	+7%	N/A
WEST SUSSEX	6 (72)	102%	YES	6%	+3%	+5%	-0%
WEST YORKSHIRE	6.5 (44)	94%	YES	13%	+4%	+4%	+0%
WESTMINSTER	10.1 (3)	81%	YES	11%	+6%	+6%	+1%
WILTSHIRE	6.1 (69)	85%	YES	20%	+3%	+4%	+1%
WORCESTERSHIRE	6.3 (57)	83%	YES	8%	+4%	+4%	+0%

Notes:

Funding levels are on the SAB standard basis.

The liability value and salary roll figures in the maturity indicator are as at 31 March 2013. The liability value was calculated on the standardised market consistent basis.

The following charts provide a graphical representation of the total contribution rates payable after the liability shock and asset shock tests above.

*Chart F1: **Liability shock** by fund: Average employer contribution rate as a percentage of payroll after a 10% increase in liabilities, market consistent basis.*

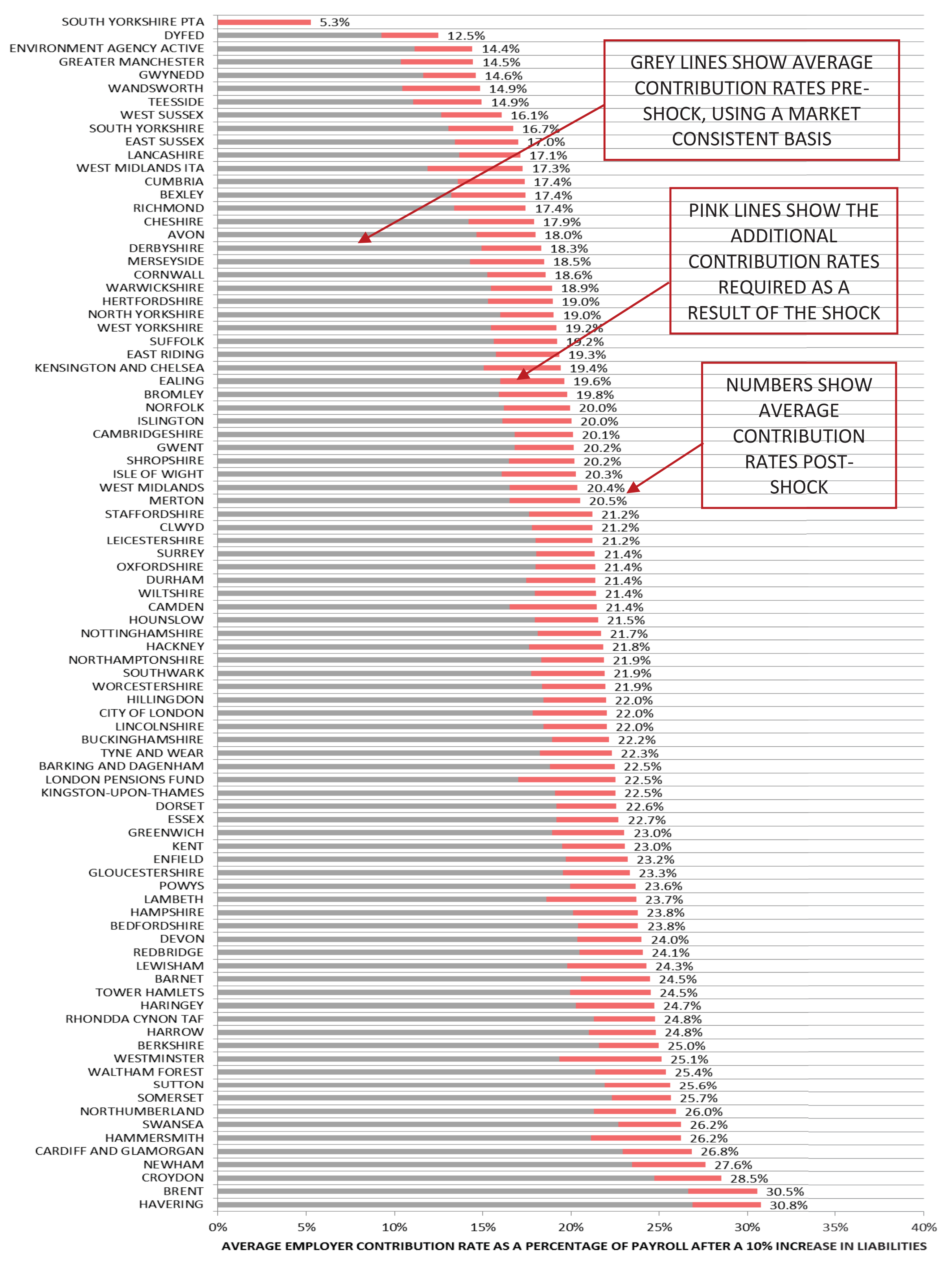
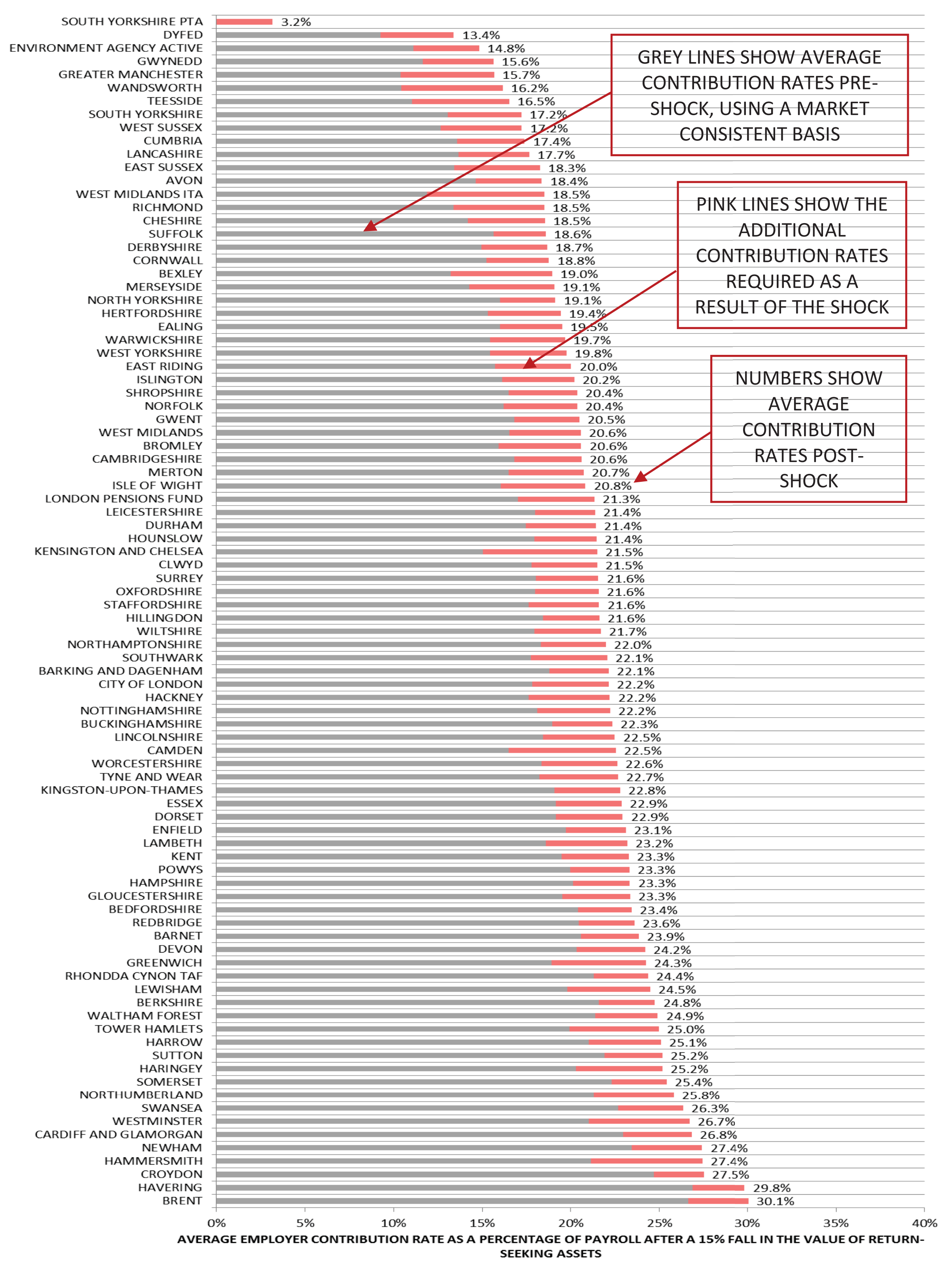


*Chart F2: **Asset shock** by fund: Average employer contribution rate as a percentage of payroll after a 15% fall in value of return seeking assets, market consistent basis.*



Appendix G: Long term cost efficiency measures – methodology

G.1 This Appendix details the methodology behind the measures used to assess a fund's long-term cost efficiency position. Some of the measures listed below were calculated using a market consistent set of assumptions. For more information on this market consistent basis please see Appendix D.

***Deficit repaid:** The proportion of deficit paid off annually, where the deficit is calculated on a standardised market consistent basis*

G.2 This measure is based on SAB key indicator 2(i). However, as the discount rate used in the SAB standard basis is not market-related, each fund's deficit and standard contribution rate on the local fund basis have been restated on a standardised market consistent (MC) basis.

G.3 The proportion of deficit paid off annually was calculated as:

$$\frac{(Avg\ ER\ cont\ rate\ paid - ER\ SCR\ on\ MC\ basis) \times Pensionable\ Salary\ roll}{Deficit\ on\ MC\ basis}$$

Where:

> The average employer contribution rate is for the year 2014/15 allowing for both contributions paid as a percentage of salary and fixed monetary contributions into the fund, where deficit contributions are fixed (i.e. the fixed monetary contributions, if any, have been converted so that they are quoted as a percentage of salary roll).

> The employer standard contribution rate on the standardised market consistent basis, is for the year 2014/15. It is assumed that the standard contribution rate is equal to the future cost of accrual of that particular fund.

> The salary roll is as at 31 March 2013 and has not been adjusted.

> The deficit on the standardised market consistent basis is as at 31 March 2013.

G.4 The data required for each of the funds to carry out the above calculation was provided by their respective fund actuaries.

G.5 Where appropriate this data has been restated on the standardised market consistent basis.

G.6 Funds that were in surplus or were paying off more than 5% of their deficit annually were flagged as green. Those funds paying off between 0% - 5% of their deficit were flagged as amber and if there were any funds that were actually paying contributions that would result in an increase in deficit, they would have been flagged as red.

***Deficit period:** The implied deficit recovery period calculated on a standardised market consistent basis*

G.7 This measure is based on SAB key indicator 3. However, as the SCAPE discount rate used in the SAB standard basis is not market-related, the calculations are done on a standardised market consistent basis.

G.8 The implied deficit recovery period on the standardised market consistent basis was found by solving the following equation for x:

$$\bar{a}_x = \frac{Deficit\ on\ standardised\ MC\ basis}{Annual\ deficit\ recovery\ payment\ on\ standardised\ MC\ basis}$$

G.9 Where:

- x is the implied deficit recovery period.
- $\bar{a}_x$ is a continuous annuity over x years at the rate of interest equal to $\frac{1+i}{1+e} - 1$.
- i is the nominal discount rate assumption on the standardised market consistent basis.
- e is the general earnings inflation assumption on the standardised market consistent basis.
- The deficit on the standardised market consistent basis is as at 31 March 2013.
- The annual deficit recovery payment on the standardised market consistent basis is calculated as the difference between the average employer contribution rate for the year 2014/15, allowing for both contributions paid as a percentage of salary and fixed monetary contributions into the fund, where deficit contributions are fixed (i.e. the fixed monetary contributions, if any, have been converted so that they are quoted as a percentage of salary roll), and the employer standard contribution rate on the standardised market consistent basis for the year 2014/15 (which is assumed to be equal to the future cost of accrual of that particular fund).

G.10 Funds that were in surplus or where the implied deficit recovery period was less than 20 years were flagged as green. Those with recovery periods greater than 20 years were flagged as amber. If there were any funds that were paying contributions as a level that would result in an increase in deficit, they would have been flagged as red.

***Required return:** The required investment return rates to achieve full funding in 20 years' time on the standardised market consistent basis*

G.11 This measure is based on SAB key indicator 4(i). However, as the SCAPE discount rate used in the SAB standard basis is not market-related, the calculations are done on a standardised market consistent basis.

G.12 The following assumptions were made for the purposes of this calculations:

> Time 0 is 31 March 2013.

> Time 20 is 31 March 2033.

> A_0 is the value of the fund's assets at time 0, and was obtained from the data provided by the local fund actuaries.

> A_{20} is the value of the fund's assets at time 20.

> L_0 is the value of the fund's liabilities at time 0, and was obtained from the data provided by the local fund actuaries.

> L_{20} is the value of the fund's liabilities at time 20.

> C_0 is one year's employer contributions paid from time 0. (DCLG's SF3 statistics for the year 2014/15 were used for this purpose).

> $C_{0\text{-}20}$ is the total employer contributions payable over the period time 0 – 20, assumed to occur mid-way between time 0 and time 20 (i.e. at time 10).

> B_0 is the value of one year's benefits paid (excluding transfers) from time 0. (DCLG's SF3 statistics for the year 2014/15 were used for this purpose).

> $B_{0\text{-}20}$ is the total value of benefits payable (excluding transfers) over the period time 0 – 20, assumed to occur mid-way between time 0 and time 20 (i.e. at time 10).

> SCR_0 is the standard contribution rate payable from time 0 to time 1 and was calculated by restating the standard contribution rates on the local fund bases using the market consistent basis.

> $SCR_{0\text{-}20}$ is the standard contribution rate payable from time 0 – 20, assumed to occur mid-way between time 0 and time 20 (i.e. at time 10).

> Sal_0 is the salary roll at time 0 and was obtained from the data provided by the local fund actuaries.

> i is the nominal discount rate assumption on the standardised market consistent basis.

> e is the general earnings assumption on the standardised market consistent basis.

> x is the required investment return that is to be calculated.

G.13 The membership profile is assumed to be constant.

G.14 The assets and liabilities at time 20 were then equated and the resulting quadratic equation solved to find the required rate of investment return to achieve full funding, i.e.:

$$A_{20} - L_{20} = 0$$

Where:

> $A_{20} = [A_0 \times (1+x)^{20}] + [(C_{0-20} - B_{0-20}) \times (1+x)^{10}]$

> $L_{20} = [L_0 \times (1+i)^{20}] + [(SCR_{0-20} - B_{0-20}) \times (1+i)^{10}]$

> $C_{0-20} = C_0 \times 20 \times (1+e)^{10}$

> $B_{0-20} = B_0 \times 20 \times (1+e)^{10}$

> $SCR_{0-20} = Sal_0 \times SCR_0 \times 20 \times (1+e)^{10}$

G.15 Given the assumptions and simplifications made in the above calculations, the use of the contribution income and benefit payments from the 2014/15 SF3 data is not likely to have a material impact on the results.

G.16 Funds where the required investment return was higher than the nominal discount rate on the standardised market consistent basis (i.e. i where i = 5.92%) were classified as amber, whereas funds were classified as green if the required return was less than i.

Repayment shortfall: *The difference between the actual deficit recovery contribution rate and the annual deficit recovery contributions required as a percentage of payroll to pay off deficit in 20 years, where the deficit is calculated on a standardised market consistent basis*

G.17 This measure extends the deficit period measure. We calculate the required annual deficit recovery contribution rate on a standardised market consistent basis to pay off the deficit in 20 years' time, and then work out the difference between the actual deficit recovery contribution rate and this rate.

G.18 The 20 year deficit recovery period is based on the SAB key indicator 4(i).

G.19 The required annual deficit recovery contribution rate to be paid on a standardised market consistent basis is equal to:

$$\frac{Deficit\ on\ standardised\ market\ consistent\ basis}{\bar{a}_{20}\ \times Salary\ roll}$$

Where:

> The deficit on the standardised market consistent basis is as at 31 March 2013.

> $\bar{a}_{20}$ is a continuous annuity over the 20 year deficit recovery period at the rate of interest equal to $\frac{1+i}{1+e} - 1$.

> i is the nominal discount rate assumption on the standardised market consistent basis.

> e is the general earnings inflation assumption on the standardised market consistent basis.

> The salary roll is as at 31 March 2013 and has not been adjusted.

G.20 The difference in deficit recovery contribution rates is then defined as:

$$(Avg\ ER\ cont\ rate\ paid - ER\ SCR\ on\ MC\ basis) - \frac{Deficit\ on\ MC\ basis}{\bar{a}_{20}\ \times Salary\ roll}$$

Where:

> The average employer contribution rate is for the year 2014/15, allowing for both contributions paid as a percentage of salary and fixed monetary contributions into the fund where deficit contributions are fixed ((i.e. the fixed monetary contributions, if any, have been converted so that they are quoted as a percentage of salary roll).

> The employer standard contribution rate on the standardised market consistent basis is for the year 2014/15. It is assumed that the standard contribution rate is equal to the future cost of accrual of that particular fund.

G.21 The data required for each of the funds to carry out the above calculation was provided by their respective fund actuaries.

G.22 Where appropriate these data has been restated on the standardised market consistent basis.

G.23 Funds where the difference in deficit recovery contribution rates is greater than 0% are flagged as green. Where the difference between contribution rates is between 0% and -3%, the funds are flagged as amber. If the difference in deficit recovery contribution rates is less than -3%, then the fund is flagged as red.

Repayment pace: *The amount of deficit paid off over each future valuation period, as a proportion of the deficit disclosed at the last valuation, and the number of years required to pay off 50% of the value of the original deficit, where the deficit calculations are carried out on a standardised market consistent basis*

G.24 The data required to calculate this measure was not available during this dry run. However, we expect this calculations to be included as part of the Section 13 report following the 2016 valuations.

G.25 This first part of this measure is similar to deficit repaid, whilst the second part of this measure is similar to deficit period. Both calculations will need to be carried out on the standardised market consistent basis.

G.26 Part one requires funds to set out what proportion of the deficit they intend to pay off in each of the future valuation periods. Part two requires funds to set out the point in time when they would pay off 50% of the value of the original deficit.

***Return scope:** The required investment return rates as calculated in required return, compared with the fund's expected best estimate future returns assuming current asset mix maintained*

G.27 This measure is based on SAB key indicator 4(ii).

G.28 The required investment return (x) calculated in the required return measure was compared against the best estimate investment return expected from the fund's assets held on 31 March 2013.

G.29 The asset data used in this calculation was provided by each fund's respective fund actuary.

G.30 Funds where the best estimate future returns were higher than the required investment return by 0.5% or more were flagged as green. Those funds where this difference was between 0% and 0.5% were flagged as amber, whilst those where the best estimate returns were lower than the required investment returns were flagged as red.

***Deficit extension:** The change in each fund's reported deficit recovery period from the 2010 valuation to the 2013 valuation*

G.31 This measure compares the deficit recovery periods as at 31 March 2010 and 31 March 2013, using the data provided by each fund's actuary.

G.32 Funds where the deficit recovery period had increased by more than 6 years were flagged as red, where the deficit recovery period had increased by less than 6 years were flagged as amber and where there was no change or the deficit recovery period was shorter in 2013 were flagged as green.

***Interest cover:** A check on whether the annual deficit recovery contributions paid by the fund are sufficient to cover the annual interest payable on that deficit, where the deficit is calculated on a standardised market consistent basis*

G.33 This measure was triggered if the following inequality did not hold true:

$$(Avg\ ER\ cont\ rate\ paid - ER\ SCR\ on\ MC\ basis) \times Sal\ roll > Deficit\ on\ MC\ basis\ \times i$$

Where:

> The average employer contribution rate is for the year 2014/15, allowing for both contributions paid as a percentage of salary and fixed monetary contributions into the fund where deficit contributions are fixed (i.e. the fixed monetary contributions, if any, have been converted so that they are quoted as a percentage of salary roll).

> The employer standard contribution rate on the standardised market consistent basis is for the year 2014/15. It is assumed that the standard contribution rate is equal to the future cost of accrual of that particular fund.

> The salary roll is as at 31 March 2013 and has not been adjusted.

> The deficit on the standardised market consistent basis is as at 31 March 2013.

> i is the nominal interest rate assumption on the standardised market consistent basis.

G.34 The data required for each of the funds to carry out the above calculation was provided by their respective fund actuaries.

G.35 Where appropriate these data have been restated on the standardised market consistent basis.

G.36 Funds that paid sufficient annual deficit recovery contributions to cover the annual interest payable on the deficit were flagged as green, whilst those that did not were flagged as red.

Deficit reconciliation: *Confirmation that the deficit period can be demonstrated to be a continuation of the previous deficit recovery plan, after allowing for actual fund experience*

G.37 The data required to calculate this measure were not available during this dry run. However, we expect this calculations to be included as part of the Section 13 report following the 2016 valuations.

G.38 This measure will be used to monitor the change in the length of the deficit recovery period set locally by the fund at each valuation and what the underlying reasons are for any adverse changes in this period.

G.39 For example, if a fund's deficit recovery period has increased from the value calculated in the previous valuation, was this due to the fund not paying sufficient deficit recovery contributions over the inter-valuation period, or was this due unfavourable demographic experience, such as increasing longevity.

Surplus retention: *Confirmation that contributions from funds not in deficit are not likely to lead to a deficit arising in the future.*

G.40 Note that all the funds that were in surplus on the market consistent basis were paying sufficient contributions to cover ongoing accrual of benefits on that basis.

G.41 This measure has therefore been excluded from our tables of long term cost efficiency measures for the purposes of the LGPS England and Wales Section 13 Dry Run Report as no funds triggered an amber or red flag.

G.42 This measure looks at the funding level of the funds that were in surplus on the standardised market consistent basis.

G.43 The fund would be need to pay sufficient contributions after allowing for future costs of accrual, such that:

$$Avg\ ER\ cont\ rate\ paid - ER\ SCR\ on\ MC\ basis > 0$$

Where:

> The average employer contribution rate is for the year 2014/15, allowing for both contributions paid as a percentage of salary and fixed monetary contributions into the fund where deficit contributions are fixed (i.e. the fixed monetary contributions, if any, have been converted so that they are quoted as a percentage of salary roll).

> The employer standard contribution rate on the standardised market consistent basis is for the year 2014/15. It is assumed that the standard contribution rate is equal to the future cost of accrual of that particular fund.

G.44 The data required for each of the funds to carry out the above calculation were provided by their respective fund actuaries.

G.45 Where appropriate these data have been restated on the standardised market consistent basis.

Appendix H: Long term cost efficiency measures – by fund

Table H1: Long term cost efficiency measures by fund

PENSION FUND	MATURITY (RANK)	LONG TERM COST EFFICIENCY MEASURES						
		RELATIVE CONSIDERATIONS				ABSOLUTE CONSIDERATIONS		
		DEFICIT REPAID	DEFICIT PERIOD	REQUIRED RETURN	REPAYMENT SHORTFALL	RETURN SCOPE	DEFICIT EXTENSION	INTEREST COVER
AVON	5.9 (82)	>50%	1	2%	16%	4.3%	-3	Yes
BARKING AND DAGENHAM	6.5 (45)	18%	6	3%	9%	2.5%	0	Yes
BARNET	6.8 (31)	15%	7	3%	9%	2.2%	0	Yes
BEDFORDSHIRE	5.9 (76)	11%	9	4%	6%	1.8%	0	Yes
BERKSHIRE	5.9 (78)	4%	34	6%	-2%	-0.5%	-3	No
BEXLEY	7.4 (14)	IN SURPLUS	IN SURPLUS	4%	7%	2.5%	0	Yes
BRENT	6.9 (28)	9%	12	4%	6%	2.3%	-3	Yes
BROMLEY	6.8 (33)	>50%	2	3%	13%	3.1%	3	Yes
BUCKINGHAMSHIRE	5.6 (87)	8%	13	5%	2%	1.2%	-3	Yes
CAMBRIDGESHIRE	5.8 (83)	18%	6	4%	5%	2.1%	0	Yes
CAMDEN	8.6 (7)	43%	2	3%	14%	3.2%	0	Yes
CARDIFF AND GLAMORGAN	6.8 (32)	9%	13	5%	3%	0.9%	-2	Yes
CHESHIRE	6.5 (41)	>50%	0	2%	14%	3.9%	0	Yes
CITY OF LONDON	7.3 (18)	7%	15	5%	1%	0.8%	0	Yes
CLWYD	6 (73)	17%	6	3%	8%	2.7%	-2	Yes
CORNWALL	5.8 (84)	>50%	2	3%	9%	2.4%	0	Yes
CROYDON	6.7 (37)	8%	14	5%	3%	1.2%	-2	Yes
CUMBRIA	6.7 (38)	>50%	0	2%	19%	3.7%	-3	Yes
DERBYSHIRE	5.9 (77)	>50%	0	4%	7%	1.7%	0	Yes
DEVON	6.4 (48)	7%	15	5%	2%	0.6%	-5	Yes
DORSET	6 (74)	8%	15	5%	1%	0.8%	0	Yes
DURHAM	6.9 (27)	16%	6	4%	7%	1.5%	-1	Yes
DYFED	5.6 (88)	IN SURPLUS	IN SURPLUS	3%	7%	3.0%	0	Yes
EALING	6.3 (53)	20%	5	4%	8%	2.0%	-3	Yes
EAST RIDING	6.3 (55)	>50%	2	3%	10%	2.6%	0	Yes

PENSION FUND	MATURITY (RANK)	LONG TERM COST EFFICIENCY MEASURES						
		RELATIVE CONSIDERATIONS				ABSOLUTE CONSIDERATIONS		
		DEFICIT REPAID	DEFICIT PERIOD	REQUIRED RETURN	REPAYMENT SHORTFALL	RETURN SCOPE	DEFICIT EXTENSION	INTEREST COVER
EAST SUSSEX	6.3 (52)	IN SURPLUS	IN SURPLUS	3%	9%	3.2%	0	Yes
ENFIELD	6.1 (66)	12%	9	5%	4%	0.7%	0	Yes
ENVIRONMENT AGENCY ACTIVE	5.8 (85)	IN SURPLUS	IN SURPLUS	N/A	N/A	N/A	3	N/A
ESSEX	6.2 (65)	14%	8	4%	6%	2.1%	0	Yes
GLOUCESTERSHIRE	6.7 (36)	19%	6	3%	10%	2.9%	0	Yes
GREATER MANCHESTER	7.2 (22)	IN SURPLUS	IN SURPLUS	2%	8%	3.7%	0	Yes
GREENWICH	7.2 (21)	8%	13	5%	2%	1.2%	0	Yes
GWENT	5.9 (79)	13%	8	5%	5%	1.5%	5	Yes
GWYNEDD	5.2 (90)	IN SURPLUS	IN SURPLUS	2%	10%	3.8%	0	Yes
HACKNEY	7.4 (15)	40%	3	1%	19%	5.4%	-2	Yes
HAMMERSMITH	8.9 (6)	9%	12	5%	4%	1.0%	-3	Yes
HAMPSHIRE	6.4 (50)	9%	12	5%	3%	0.6%	-3	Yes
HARINGEY	7.8 (11)	14%	7	4%	7%	1.8%	0	Yes
HARROW	6.6 (39)	9%	12	5%	3%	1.0%	0	Yes
HAVERING	6.8 (34)	8%	14	4%	3%	1.4%	0	Yes
HERTFORDSHIRE	6.4 (49)	>50%	1	3%	11%	2.9%	0	Yes
HILLINGDON	6.2 (64)	12%	9	4%	4%	1.3%	0	Yes
HOUNSLOW	6.3 (58)	12%	9	5%	5%	1.1%	0	Yes
ISLE OF WIGHT	7.4 (16)	>50%	2	4%	9%	2.4%	0	Yes
ISLINGTON	6.8 (30)	18%	6	4%	8%	1.8%	-3	Yes
KENSINGTON AND CHELSEA	7.7 (13)	IN SURPLUS	IN SURPLUS	4%	7%	2.1%	-3	Yes
KENT	6.2 (63)	11%	10	5%	5%	1.5%	0	Yes
KINGSTON-UPON-THAMES	6.1 (71)	19%	5	3%	8%	3.0%	0	Yes
LAMBETH	8.9 (5)	30%	3	2%	17%	3.6%	0	Yes
LANCASHIRE	6.1 (70)	>50%	2	4%	10%	1.9%	0	Yes
LEICESTERSHIRE	5.7 (86)	13%	8	5%	4%	1.5%	0	Yes
LEWISHAM	7.8 (10)	11%	9	5%	4%	1.3%	0	Yes
LINCOLNSHIRE	6.3 (56)	14%	8	4%	5%	1.9%	0	Yes

PENSION FUND	MATURITY (RANK)	LONG TERM COST EFFICIENCY MEASURES						
		RELATIVE CONSIDERATIONS				ABSOLUTE CONSIDERATIONS		
		DEFICIT REPAID	DEFICIT PERIOD	REQUIRED RETURN	REPAYMENT SHORTFALL	RETURN SCOPE	DEFICIT EXTENSION	INTEREST COVER
LONDON PENSIONS FUND	9.6 (4)	48%	2	2%	20%	4.0%	-3	Yes
MERSEYSIDE	7.3 (17)	>50%	1	1%	24%	4.9%	-3	Yes
MERTON	7.1 (25)	>50%	1	1%	20%	5.2%	-3	Yes
NEWHAM	7.3 (19)	10%	11	4%	6%	2.1%	0	Yes
NORFOLK	6.6 (40)	33%	3	4%	9%	2.4%	0	Yes
NORTH YORKSHIRE	5.3 (89)	27%	4	3%	10%	2.6%	-3	Yes
NORTHAMPTONSHIRE	6.2 (60)	20%	5	4%	9%	2.4%	0	Yes
NORTHUMBERLAND	8.2 (8)	14%	8	4%	7%	1.4%	-3	Yes
NOTTINGHAMSHIRE	6.3 (54)	10%	10	5%	3%	1.2%	0	Yes
OXFORDSHIRE	5.9 (75)	12%	9	4%	4%	1.5%	0	Yes
POWYS	6.4 (46)	12%	9	4%	6%	1.3%	0	Yes
REDBRIDGE	6.3 (51)	13%	8	4%	5%	1.5%	0	Yes
RHONDDA CYNON TAF	6.1 (68)	11%	10	5%	6%	1.3%	0	Yes
RICHMOND	7.1 (24)	IN SURPLUS	IN SURPLUS	3%	13%	3.1%	0	Yes
SHROPSHIRE	6.5 (43)	17%	6	4%	6%	1.6%	0	Yes
SOMERSET	5.9 (80)	5%	24	6%	-1%	0.0%	0	No
SOUTH YORKSHIRE	6.4 (47)	>50%	1	2%	17%	3.7%	-3	Yes
SOUTH YORKSHIRE PTA	25.2 (1)	IN SURPLUS	IN SURPLUS	N/A	11%	N/A	N/A	Yes
SOUTHWARK	7.3 (20)	17%	6	4%	7%	2.0%	-3	Yes
STAFFORDSHIRE	6.2 (59)	23%	5	4%	9%	2.4%	5	Yes
SUFFOLK	6.2 (62)	>50%	1	2%	13%	2.9%	0	Yes
SURREY	5.9 (81)	22%	5	3%	9%	3.0%	0	Yes
SUTTON	6.5 (42)	11%	10	4%	5%	1.4%	0	Yes
SWANSEA	6.2 (61)	10%	10	4%	4%	1.6%	0	Yes
TEESSIDE	6.8 (29)	IN SURPLUS	IN SURPLUS	5%	3%	1.3%	-3	Yes
TOWER HAMLETS	8.1 (9)	22%	5	3%	11%	3.4%	0	Yes
TYNE AND WEAR	7.1 (23)	22%	5	4%	10%	2.2%	0	Yes
WALTHAM FOREST	7 (26)	11%	9	3%	10%	2.4%	0	Yes

PENSION FUND	MATURITY (RANK)	LONG TERM COST EFFICIENCY MEASURES						
		RELATIVE CONSIDERATIONS				ABSOLUTE CONSIDERATIONS		
		DEFICIT REPAID	DEFICIT PERIOD	REQUIRED RETURN	REPAYMENT SHORTFALL	RETURN SCOPE	DEFICIT EXTENSION	INTEREST COVER
WANDSWORTH	7.7 (12)	IN SURPLUS	IN SURPLUS	4%	9%	2.3%	-3	Yes
WARWICKSHIRE	6.1 (67)	40%	3	4%	7%	2.4%	0	Yes
WEST MIDLANDS	6.8 (35)	19%	6	4%	8%	2.0%	-3	Yes
WEST MIDLANDS ITA	25.1 (2)	IN SURPLUS	IN SURPLUS	N/A	45%	N/A	N/A	Yes
WEST SUSSEX	6 (72)	IN SURPLUS	IN SURPLUS	3%	9%	2.9%	0	Yes
WEST YORKSHIRE	6.5 (44)	44%	2	5%	2%	0.7%	0	Yes
WESTMINSTER	10.1 (3)	8%	15	5%	3%	0.9%	-5	Yes
WILTSHIRE	6.1 (69)	17%	6	4%	6%	2.1%	0	Yes
WORCESTERSHIRE	6.3 (57)	14%	7	4%	7%	2.0%	2	Yes

Notes:

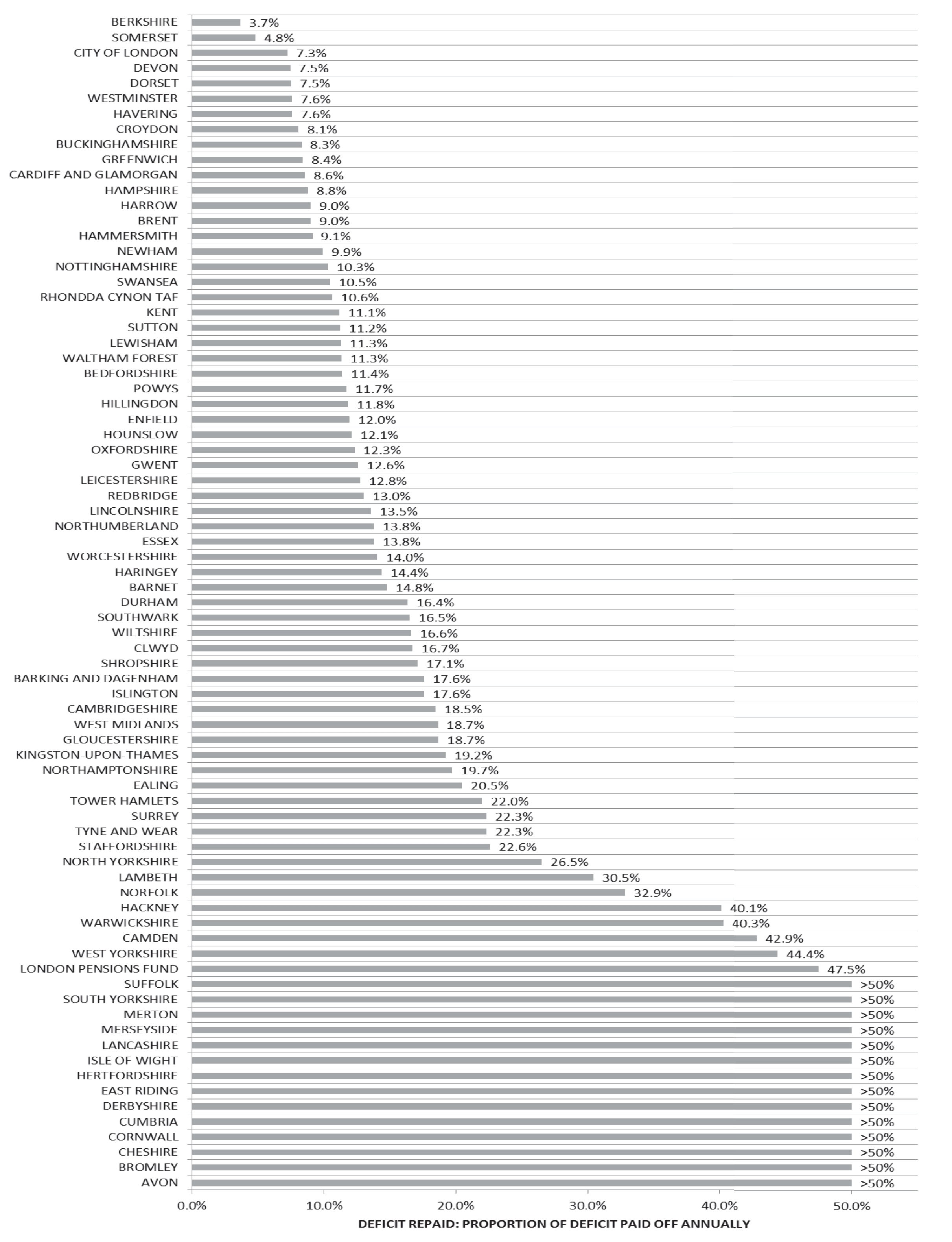
The liability value and salary roll figures in the maturity indicator are as at 31 March 2013. The liability value was calculated on the standardised market consistent basis.

The ‘Required Return’ and ‘Return Scope’ measures were not calculated for South Yorkshire PTA and West Midlands ITA as these are closed funds. They were also not calculated for the Environment Agency Open fund as the DCLG SF3 statistics did not contain data for the fund.

The ‘Deficit Extension’ measure was not calculated for South Yorkshire PTA and West Midlands ITA as information on deficit recovery periods was not available.

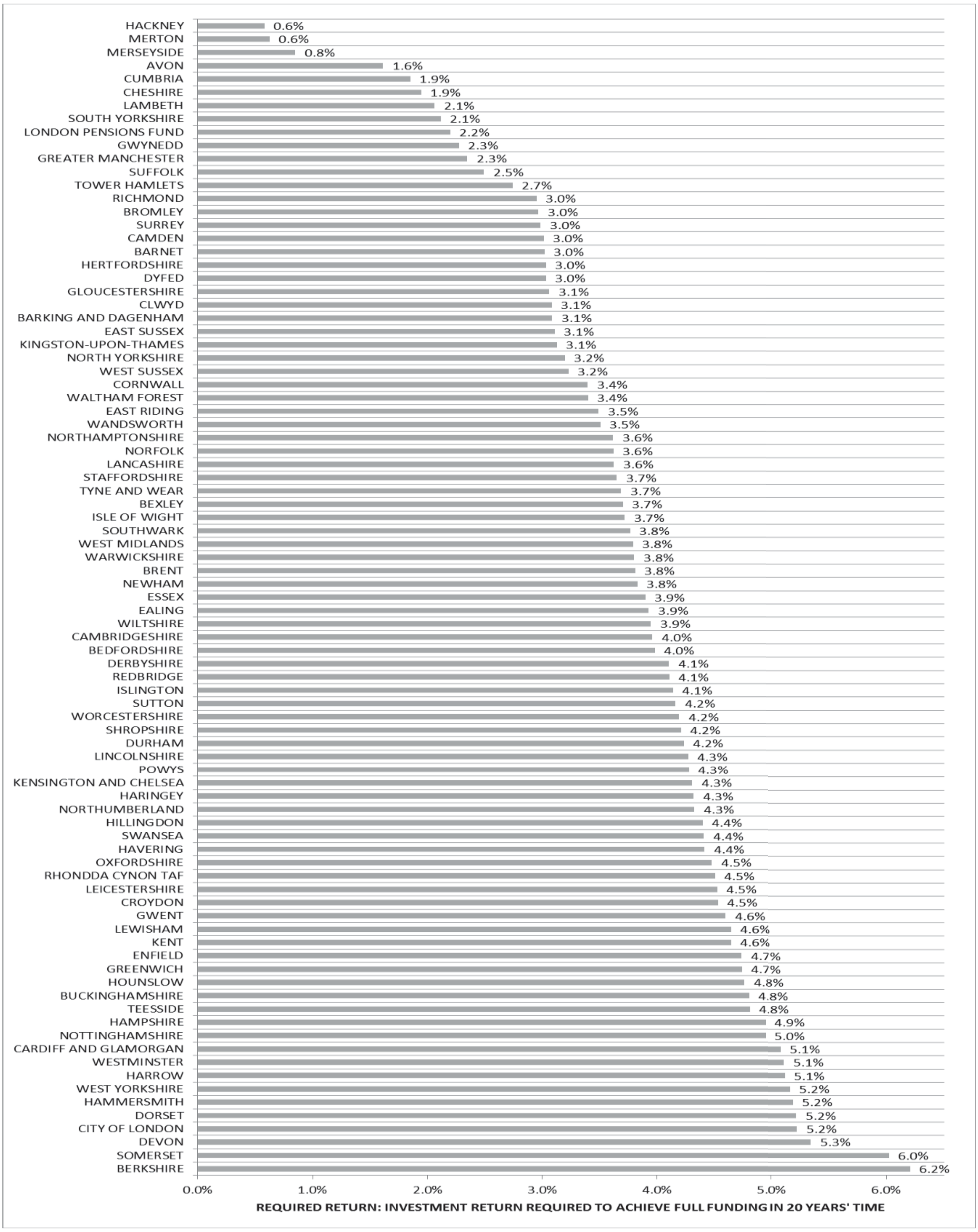
The following charts provide a graphical representation of the ‘Deficit Repaid’ and ‘Required Return’ measures.

*Chart H1: **Deficit Repaid** by fund: The proportion of deficit paid off annually.*



Note: Funds in surplus have been excluded.

*Chart H2: **Required Return** by fund: The investment return required to achieve full funding in 20 years' time.*



Note: Neither closed funds nor the Environment Agency Active fund were assessed under this measure.

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Non-Executive Report of the: **Pensions Committee** 7th December 2016	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
Investment Performance Review for Quarter End 30th September 2016	

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 30th September 2016.

For the quarter, the Fund outperformed the benchmark by 1.5%, delivering a positive absolute return of 6.9% against benchmark return of 5.4%.

The Fund is ahead of its benchmark for the last twelve months to end of September 2016. The Fund returned 18.1% which was ahead of the benchmark return of 17.6% by 0.5%.

For longer term performance, the Fund matched the benchmark return of 9.2% for three year returns and outperformed the benchmark marginally by posting five year returns of 10.5%; this is 0.1% above the benchmark return of 10.4%.

For this quarter end, all the eight mandates matched or achieved returns above the benchmark.

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:

1) note the contents of this report and
2) approve the current Fund strategic asset allocation as set out at table 4 of section 3.22.

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 ending 30th September 2016.

3.4 London Common Investment Vehicle (LCIV)

3.4.1 The London CIV was formed as a voluntary collaborative venture by the London Local Authorities in 2014 and has led the way in pooling of investments in the Local Government Pension Scheme (LGPS). London CIV aims to be the investment vehicle of choice for Local Authority Pension Funds through successful collaboration and delivery of compelling performance. LCIV was launched in December 2015, as a fully authorised and regulated investment management company. The founding members are London boroughs and the City of London Corporation and LCIV has been established as a collective investment vehicle for their Local Government Pension Scheme funds. The current regulatory permission allows the London CIV to operate an Authorised Contractual Scheme Fund (the UK's version of a Tax Transparent Fund).

3.4.2 London CIV currently manages three investment portfolios of LBTH fund listed below:

a) **The Baillie Gifford diversified growth fund (DGF)** mandate was opened in February 2011 with contract value of £40m. £6.409m was added to this portfolio in the month of June 2015. 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%. This mandate was transferred to LCIV, 15th February 2016 at a market value of £54.177m. The market value of assets as at 30th September 2016 was £59.269m. The fund is now named LCIV (BG) DGF.

b) **The Baillie Gifford global equity fund** had a value of £118.9m at the start of the mandate in July 2007. 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 period. This mandate was transferred to LCIV 22nd April 2016 at market value of £214.1m. The market value of the assets as of 30thSeptember 2016 was £251.52m. Now named LCIV (BG) GA.

c) **Ruffer LLP** 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 2nd June 2015. 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. The management of this portfolio was transferred to LCIV, 20th June 2016 at market value of £54m. The value of assets under management as of 30th September 2016 was £60.614m. The fund is now named LCIV Ruffer.

3.5 GMO

3.5.1 GMO manages a Global Equity Mandate, the initial value of assets taken on at the commencement (29th April 2005) of the contract was £201.8m. 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 portfolio had a market value of £289.654m at 30th September 2016.

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 Goldman Sachs Asset Management

3.6.1 On 4th April 2016, the fund invested £75m in Goldman Sachs Strategic Absolute Return Bond II (STRAT II). The portfolio had a market value of £76.477m at 30th September 2016.

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 Insight Investment Management

3.7.1 On 1st July 2016, the fund invested £70m with Insight Investment Management in BNY Mellon Global Funds. The portfolio had a market value of £70.187m at 30th September 2016.

3.7.2 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. It is too early to comment on the fund's initial performance.

3.8 Legal & General Investment Management

3.8.1 Legal & General was appointed (2ndAugust 2010) to manage passive UK Equity and UK Index-Linked Mandates. At 30th September 2016, the UK Equity portfolio had a market value of £245.639m, and the UK Index linked portfolio was £74.810m.

3.8.2 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.

3.9 Schroder Investment Management

3.9.1 Schroder manages a property mandate. The value of this mandate on 20nd September 2004 was £90m. The market value of assets at 30th September 2016 was £135.876m.

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.

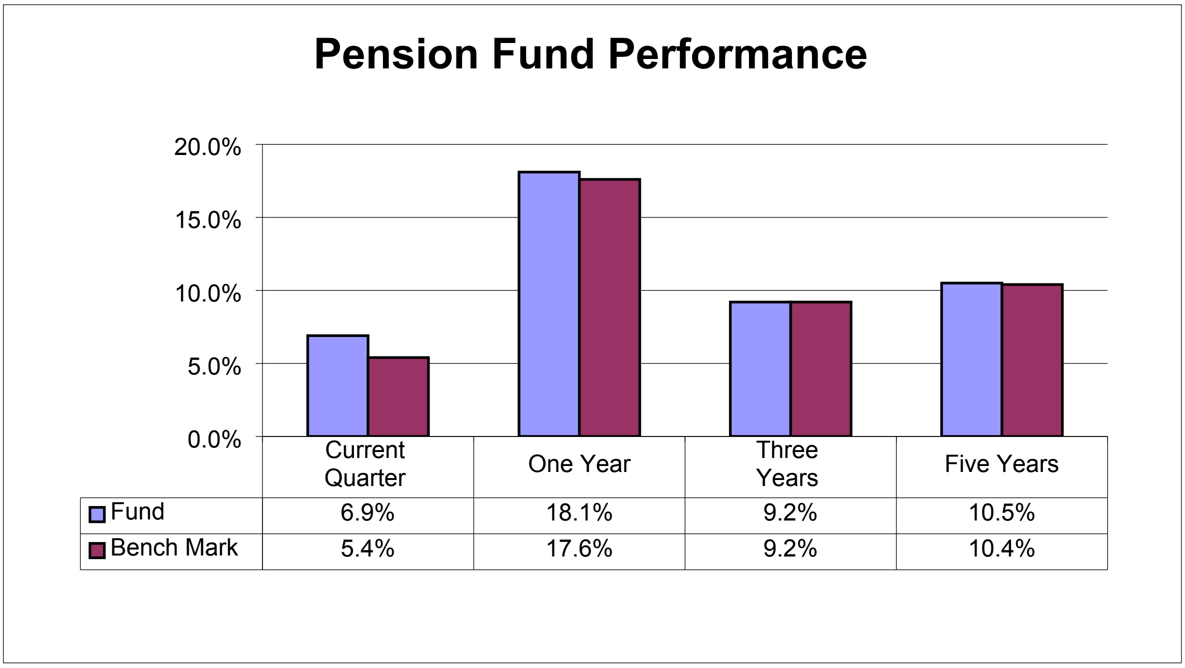
3.10 INVESTMENT PERFORMANCE

I. The Fund's overall value appreciated by £84.994m from £1,185.57m as of 30th June 2016 to £1,270.564m as of 30th September 2016.

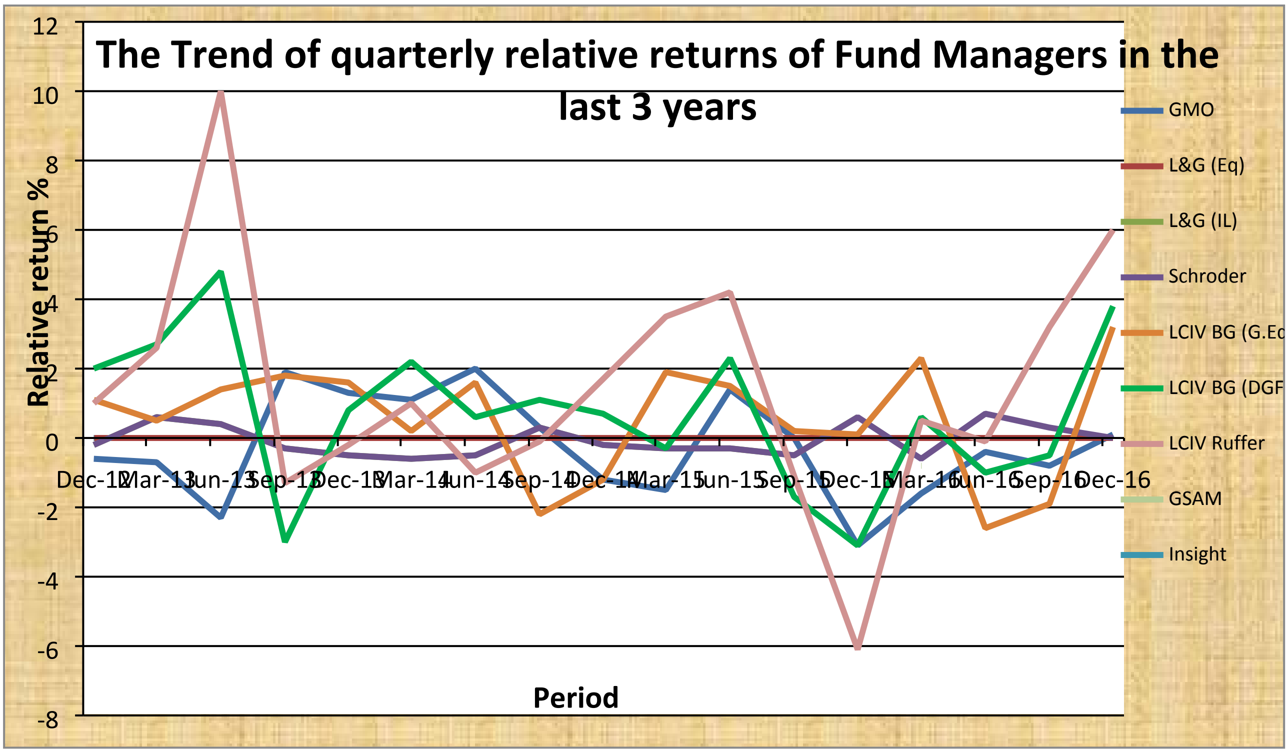
II. The fund outperformed the benchmark this quarter with a return of 6.9% compared to the benchmark return of 5.4%. The twelve month period sees the fund ahead of its benchmark by 1.5%.

III. The performance of the fund over the longer term is as set out in the chart below.

Table 1 – Pension Fund Performance



IV. 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.

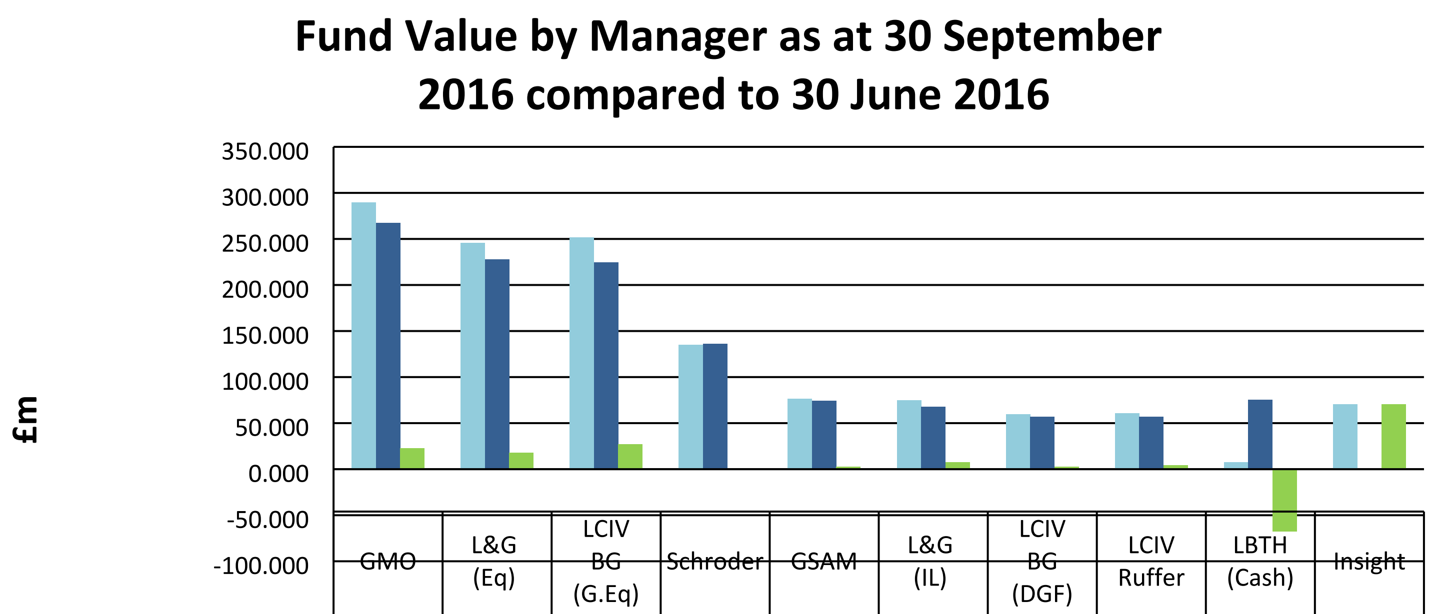


3.11 MANAGERS

I. The Fund is managed on a specialist basis with GMO and LCIV (BG GE) managing the Global Equities on an active basis. UK Equities and UK Index-Linked are passively managed by LGIM. GSAM and Insight managing absolute return pooled bond funds and Schroder is the property manager. The managers, mandate and funds held under management are set out below: The Fund was valued at £1,270.56million as at 30th September 2016.This includes cash held and being managed internally (by LBTH Treasury Management); this stands at 0.59% of the total assets value. This is working capital.

Table 2: Management Structure

Manager	Mandate	Value £M	Weight Target of FM AUM %	Actual Weight of FM AUM %	Over/(Under) Weight Target %	Date Appointed
GMO	Global Equity	289.654	22.00%	22.80%	0.80%	29-Apr-05
LCIV BG	Global Equity	251.520	18.00%	19.80%	1.80%	22-Apr-16
LCIV BG (Diversified Growth Fund)	Absolute Return	59.269	5.00%	4.66%	(0.34)%	15-Feb-16
LCIV Ruffer (Total Return Fund)	Absolute Return	60.614	5.00%	4.77%	(0.23)%	20-Jun-16
L & G UK Equity	UK Equity	245.639	20.00%	19.33%	(0.67)%	02-Aug-10
L & G Index Linked-Gilts	UK Index Linked	74.810	6.00%	5.89%	(0.11)%	02-Aug-10
GSAM	Bonds	76.477	6.00%	6.02%	0.02%	04-Apr-16
Insight	Bonds	70.187	6.00%	5.52%	(0.48)%	01-Jul-16
Schroder	Property	134.876	12.00%	10.62%	(1.38)%	30-Sep-04
Cash (Awaiting Investment)	Internal cash management	7.518	0.00%	0.59%	0.59%	
Total		**1,270.56**	**100.00%**	**100.00%**	**0.00%**	



	GMO	L&G (Eq)	LCIV BG (G.Eq)	Schroder	GSAM	L&G (IL)	LCIV BG (DGF)	LCIV Ruffer	LBTH (Cash)	Insight
Value at 30/09/2016	289.654	245.639	251.520	134.876	76.477	74.810	59.269	60.614	7.518	70.187
Value at 30/06/2016	267.215	227.850	224.429	135.900	74.152	67.423	56.615	56.676	75.311	0.000
Gain/(Loss) of Value	22.439	17.789	27.091	1.024	2.325	7.387	2.654	3.938	67.793	70.187

II. The above graph illustrated portfolio value movement of each mandate for this reporting quarter compared to the last quarter.

III. 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	0.00%	-2.60%	-1.40%	-1.30%
L & G UK Equity	0.00%	0.10%	0.10%	0.10%
LCIV (BG) Global Equities	3.20%	1.50%	1.40%	2.30%
LBTH (Cash Management)	0.50%	1.00%	0.60%	0.6
Schroder	0.00%	0.30%	-0.40%	-0.50%
L & G Index Linked-Gilts	0.00%	0.00%	0.00%	0.00%
LCIV (BG) Diversified Growth	3.80%	3.20%	1.40%	2.20%
LCIV (Ruffer) Total Return Fund	6.00%	9.00%	2.50%	2.80%
GSAM (STAR II)	2.50%	N/A	N/A	N/A
Total Variance (Relative)	**1.50%**	**0.50%**	**0.00%**	**0.10%**

3.12 **GMO** - The portfolio posted benchmark return of 8.4% over the reporting quarter.

I. The portfolio position in emerging markets has been focused on specific, undervalued stocks within sectors, including Russia Energy and China Telecommunication Services. Emerging markets accounted for approximately 22% of the total portfolio weight on average during the quarter. This position resulted in both positive allocation and selection impacts during the quarter as emerging markets surged strongly.

II. The portfolio position in high quality is comparatively multinational and carries less cyclical economic exposure compared to the U.S. market. The manager allocation to high quality accounted for approximately 15% of the total portfolio weight on average during the quarter. This produced a negative allocation but neutral selection impact during the quarter. The U.S. market underperformed MSCI ACWI, but the manager high quality holdings essentially matched the S&P 500's return during the period. Qualcomm was the most significant individual stock contributor in high quality, while Oracle was the biggest detractor.

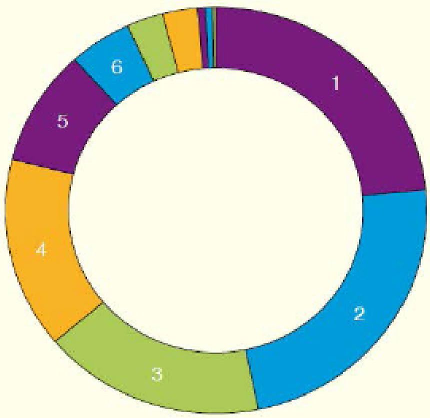
III. The manager allocation in the U.S. includes mainly value stocks selected by the manager quantitative valuation approach. The allocation was approximately 21% of the total portfolio weight on average during the quarter to this group. This position in the U.S. produced both negative allocation and selection impacts during the quarter as the U.S. market underperformed other markets and our holdings underperformed in the U.S. during the quarter. Significant detractors from relative return included the underweight positions in Apple and Amazon.com.

IV. The manager position in Europe carries a fair amount of exposure to some of the more cyclically-exposed segments of the market. Positioning in Europe accounted for approximately 24% of the total portfolio weight on average during the quarter. The position in Europe produced a neutral allocation impact during the quarter as European stocks essentially matched the MSCI ACWI index. Stock selection was a positive, as the manager's stocks in Europe did better than the region overall, particularly in Germany. The portfolio overweight position in Daimler (Germany) and underweight position in Novo Nordisk (Denmark) were significant individual stock contributors to relative returns.

V. In the year to 30th September 2016 the portfolio posted a return of 27.7%, compared to the benchmark return of 31.1%. The portfolio performance returns over the longer periods are also not encouraging. The portfolio lagged behind the benchmark return by -1.4% for over three years and lagged behind the benchmark by -1.3% for over five years.

3.13 **LCIV (Baillie Gifford) Global Equities** – the portfolio outperformed the benchmark by delivering a return of 11.8% compared to benchmark return of 8.4% over the quarter, resulting in relative outperformance of 3.2%. 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 outperformed the benchmark for one year to reporting period by 1.5%, and also ahead of the benchmark return over 3 years by 1.4% and by 2.3% for 5 years.

The sector breakdown of the portfolio is set out below:



Sector Weights		(%)
1	Financials	23.4
2	Information Technology	23.4
3	Consumer Discretionary	17.1
4	Industrials	15.2
5	Health Care	9.2
6	Materials	4.8
7	Energy	2.8
8	Consumer Staples	2.7
9	Cash	0.6
10	Real Estate	0.6
11	Telecommunication Services	0.2
	Total	100.0

Source: Baillie Gifford as at 30/09/16

I. The portfolio was impacted by a significant underweight exposure (approx. 1/3rd index weighting) to the energy sector in the quarter to 30th June, which had seen a significant bounce over the quarter as oil prices recovered from the depths of the selloff seen towards the end of 2015 and into 2016. Lack of holdings in the utility sector which similarly bounced back after a period of underperformance also impacted on the returns seen by the fund since April. However, strong performances from the IT and Financial sectors over the second quarter, where the portfolio was overweight meant that the fund recovered significantly over the quarter to September.

II. The financial sector added value during the quarter, with the exposure focused away from banks and on financial service companies including insurance companies, this is an area that could be impacted by a sharp reversal in bond yields and is an area which we are closely monitoring with the manager. The manager has previously commented that they regard the financial exposure as being well diversified and away from the key stocks, such as mainstream banks which might be affected by a sharp reversal in bond yields.

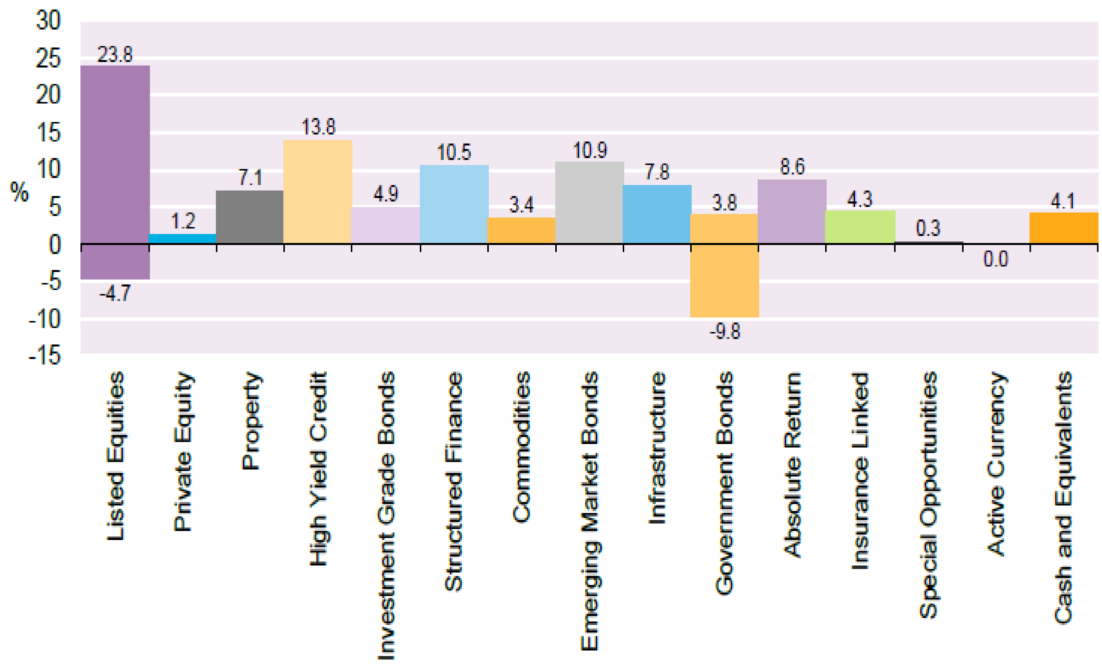
III. The portfolio maintained an overweight exposure to Japan. Whilst Japan has often looked to be on the verge of offering value, it has on a number of occasions disappointed and there remain concerns as to whether Abenomics will deliver growth in Japan. However, Japanese exposure is due to the fact that the weighting is made up of positions in individual companies that offer attractive growth opportunities rather than them being a reflection of optimism on the economy. The manager also believes that recent improvements in corporate governance amongst Japanese companies should deliver value over time we seeing some merit in this argument which seems to be developing some traction. We remain to be convinced that the overall level of exposure will add significant value to the fund and will continue to monitor and challenge the manager on the overweight position.

IV. The fund is focused on a bottom up stock-picking approach with a diversified portfolio (typically 90-110 stocks). The top 10 stocks in the portfolio at the end of the quarter were:

Top Ten Holdings

Company Name	Description of Business	% of Portfolio
Amazon.com	Online retailer	4.6
Naspers	Media and e-commerce company	3.3
Prudential	International financial services group	3.1
TSMC	Semiconductor manufacturer	2.8
Royal Caribbean Cruises	Global cruise company	2.8
SAP	Enterprise software provider	2.7
Alphabet	Online search engine	2.4
Moody's	Credit rating agency	2.1
CRH	Diversified building materials company	2.1
First Republic Bank	US retail bank	2.1
Total		28.1

3.14 **LCIV (Baillie Gifford) Diversified Growth Fund** for this reporting quarter, the return of the portfolio was 4.7%. The fund invests in a diversified range of asset classes and the breakdown is shown below with the negative exposures being delivered through short futures positions:



Source: Baillie Gifford as at 30/09/16.
Total may not sum due to rounding
Any difference between asset class exposure and asset class weight relates to futures positions.
Active currency exposure reflects the net unrealised profit or loss of open positions in the Fund as at 30 September 2016.
In other asset classes, any negative exposures relate to futures positions.

I. The asset classes with the strongest positive returns were listed equities and high yield credit which recovered strongly, along with a number of other asset classes, following their initial shock after the vote to leave the European Union. Active currency was a small detractor from performance over the quarter.

II. In the year to 30th September 2016 the portfolio delivered a return of 6.9%. Over the longer-term, and with relevance to the portfolio's return objective, the three year return was 5% and the five year return was 5.9% per annum. Delivered volatility for the past five years was 4.3% per annum.

III. Over the 12 month period, the profile of returns was broadly similar with listed equities and emerging market bonds the largest positive contributors. Both asset classes continue to benefit from the rise in asset valuations. Active currency and government bonds detracted from performance.

IV. The manager cautious approach to emerging market currencies suffered following a rally in a number of these currencies at the end of March 2016 quarter which continues into the September 2016 quarter.

3.15 **Ruffer Total Return Fund (Absolute Return)** – The portfolio posted a return of 6.9% compared with benchmark return of 0.9% over the quarter.

I. With a strong outperformance for 12 months to September 2016 with return of - 13% compared with benchmark return of 3.6%. The portfolio outperformed the benchmark by posting a return of 6.2 % per annum over three years, which is over benchmark return by 2.5% per annum and ahead of benchmark return by 2.8% per annum for over five years period.

II. The Fund benefited from having defensive positions with significant exposure to index linked bonds which added positively to performance being pushed higher by Brexit, further quantitative easing and ongoing low rates. The manager also took advantage of weakness in UK domestic stocks following the Brexit vote, such as house builders which subsequently bounced quite strongly.

III. The fund also has an above average exposure to Japan, having taken the view that Abenomics would help to deliver stronger growth, but this has been an area of concern to us and LCIV officers questioned the manager over the size and conviction of this exposure, the portfolio manager confirmed that their level of conviction in Japanese holdings is perhaps less strong than it was and they are currently reviewing their allocations to equities (including financials) and the yen, this is subject to the findings of the fund manager chief economist who is currently visiting the country.

3.16 **Legal & General - L & G (UK Equity)** – The portfolio returned 7.8% matching the index return over the quarter.

I. Among blue chip UK equities, mining and energy stocks performed well, lifted by firmer oil prices. The FTSE 100 also continued to benefit from the boost to international earnings provided by the weakness in sterling. Despite having fallen sharply in the immediate aftermath of the referendum result in late June, the FTSE 250 outperformed the FTSE 100 as mid cap stocks rose sharply following the Bank of England's latest announcement of support for the domestic economy.

3.17 **L & G Index Linked Gilts** – The portfolio returned 10.9% matching the index return over the quarter.

I. Having fallen to record lows in June following the result of the UK referendum on European Union membership, global government bond yields generally inched higher over the quarter, with overall bond prices treading water as investors remained vigilant of any potential moves from leading central banks. In particular, the US Federal Reserve's (Fed) overall direction of travel continued towards tightening policy.

II. Gilts proved to be an exception, however, with UK yields moving lower and bond prices higher following the Bank of England's decision in August to cut interest rates by 0.25%. In an effort to shore up post-referendum confidence, UK policymakers also announced an extension to their programme of quantitative easing via a combination of gilt and corporate bond purchases. Continuing the trend from earlier in the year, index-linked gilts produced very strong returns, outperforming conventional gilts as sterling

3.18 **Goldman Sachs Asset Management (GSAM) -** The portfolio outperformed the benchmark of 3 month LIBOR plus 2% in the reporting period by posting returns of 3.1% against a benchmark return of 0.6%.

I. **GSAM** remain cautious on corporate credit exposure at current spread levels. They believe that deteriorating US corporate fundamentals and the potential for late-cycle volatility makes the current environment less favourable for corporate bond exposure, even though the global hunt for yield provides a potential tailwind. In contrast, the manager sees supportive developments for the US housing market, which they believe remains in expansionary phase. As a result, they have a more favourable view on the securitised credit space.

II. Within macro strategies, GSAM country strategy contributed to performance, mainly from their long US vs short UK rates positions in the long end of the curve. Within sector strategies, the securitised strategy contributed, primarily from their exposure to Collateral Loans Obligations (CLOs) and Asset Backed Securities.

III. The manager corporate strategy was a detractor due to their short beta exposure to corporate credit.

3.19 **Insight Investment** - The portfolio underperformed the benchmark of 3 month LIBOR plus 2% in the reporting period by posting returns of 0.25% against a benchmark return of 0.6%.

I. Market allocation and yield-curve positioning detracted from performance but strong contributions from the investment-grade credit, asset-backed securities and duration segments generated strong gains. Emerging-market debt was neutral on balance, while currency and high-yield debt detracted marginally.

3.20 **Schroder (Property)** – The portfolio matched the benchmark return for this reporting quarter and also the performance was marginally above the benchmark for twelve months to 30th September 2016, with 0.3%, whilst over the longer term; performance is below the benchmark by -0.4% per annum over three years and -

0.5% for over five years periods. The UK portfolio has outperformed the benchmark over all time periods.

I. The surprise outcome of the EU referendum vote caused a run on a number of real estate funds towards the end of Q2 and resulted in an immediate fall in values over the following months. Transaction volumes have been relatively low, but it is estimated that values have fallen by between 2% and 4% on average over the quarter. The largest falls in value occurred in July and by the end of the quarter there were signs that yields on good quality institutional grade property had broadly stabilised in most market sectors.

II. Although property funds aimed at retail investors generated a number of headlines in the immediate aftermath of the EU referendum, the institutional funds which are in the portfolio have been relatively unmarked other than short term performance volatility and small volumes of redemptions to satisfy.

3.21 **Internal Cash Management**

I. 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 flow requirements, although transfers can be made to Fund managers to top up or rebalance the Fund.

II. The Pension Fund cash balance is invested in accordance with the Council's Treasury Management strategy agreed by Full Council in February 2016, which is delegated to the Corporate Director of Resources to manage on a day to day basis within set parameters.

III. The cash balance as at 30th September 2016, was £7.5m and this is essentially the Fund working cash flows. 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.

3.22 **ASSET ALLOCATION**

I. 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 Pensions Committee – the latest review was carried out in January 2014. The asset allocation will be reviewed once the results of the 2016 valuation is known.

Asset allocation is determined by a number of factors including:-

a) 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.

b) 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.

c) The deficit recovery term. Most LGPS 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. At recent valuations, the actuary set a twenty year deficit recovery term for this Council which enables a longer term investment perspective to be taken.

II. Although due to major markets price appreciation, the allocations have moved away from the original benchmark. For example UK Gilts & Indexed Linked had a benchmark weight of 3% and at the end of September 2016, the weight of this asset class represent 5.94%, this asset are currently very expensive, moreover the Committee were considering increasing the benchmark weight of this asset class at previous meetings. It is now deemed necessary to revise the strategic benchmark to accommodate the current weight of this asset class rather than selling down the position as having more of this assets in the Fund strengthens the liability hedging ratio of the Fund.

III. 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.

IV. The revised benchmark of asset distribution and the fund position at 30th September 2016 are set out below:

Table 4: Asset Allocation

Asset Class	Benchmark	Revised Benchmark	Fund Position as at 30 September 2016	Variance as at 30 September 2016
UK Equities	20.0%	20.0%	19.3%	(0.7)%
Global Equities	40.0%	40.0%	42.6%	2.6%
Total Equities	**60.0%**	**60.0%**	**61.9%**	**1.9%**
Property	12.0%	12.0%	10.6%	(1.4)%
Bonds	15.0%	12.0%	11.6%	(0.4)%
UK Index Linked	3.0%	6.0%	5.9%	(0.1)%
Alternatives	10.0%	10.0%	9.4%	(0.6)%
Cash	0.0%	0.0%	0.6%	0.6%
Total Equities	**100.0%**	**100.0%**	**100.0%**	

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 7(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 requires the Council, as an administering authority, after taking proper advice, to formulate an investment strategy which must be in accordance with guidance issued from time to time by the Secretary of State. Regulation 7(2) states that the investment strategy must include the following:

(a) a requirement to invest fund money in a wide variety of investments;

(b) the authority's assessment of the suitability of particular investments and types of investments;

(c) the authority's approach to risk, including the ways in which risks are to be assessed and managed;

(d) the authority's approach to pooling investments, including the use of collective investment vehicles and shared services;

(e) the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and

(f) the authority's policy on the exercise of the rights (including voting rights) attaching to investments.

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. The Council may only appoint an investment manager if it (a) reasonably believes that the investment manager's ability in and practical experience of financial matters make that investment manager suitably qualified to make investment decisions for it. The Council must take proper advice in relation to the appointment and the terms on which the appointment is made. Regulation 8 gives the Secretary of State the power to issue a direction to an authority in relation to its investment functions, if the Secretary of State is satisfied that the authority is failing to act in accordance with guidance issued under regulation 7(1).

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

- Appendix 1 – SSGS Quarterly Performance Review

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 SSGS Quarterly Performance Review. (To be email if required)

Officer contact details for documents:

- Bola Tobun Investment &Treasury Manager x4733

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Non-Executive Report of the: **Pensions Board & Pensions Committee** 05 & 07 December 2016	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** Unrestricted
2015/16 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 2015/16 and 2015/16 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 was presented for consideration at the last meeting of the Pensions Committee. For completeness, this report is included on the December 2016 Pension Committee agenda for noting.

Recommendations:

The Pensions Board is recommended to note the contents of this report and the following listed reports as already approved by Pensions Committee:

- The draft ISA 260 (Appendix A);
- The Pension Fund Statement of Accounts 2015/16;
- The Pension Fund Annual Report (Appendix B) and
- The draft Audit Opinion for Pension Fund Account 2015/16.

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). The annual report has been prepared in accordance with the Local Government Pension Scheme Regulations 2013 and includes all the items required.

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 KPMG is required to issue an ISA 260 Annual Governance Report is attached as Appendix A, reporting their 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.

3.5 The Chair and the Chief Financial Officer were required to sign a letter of representation to acknowledge the Council's responsibility for the fair presentation of the information in the financial statements and the Pension Fund Annual Report. A proposed draft of this letter is shown at Appendix C of this report for the Committee's information. The auditor expected to issue an unqualified audit opinion on the Pension Fund in late November and their comments are included within the attached draft ISA 260. Comments on their findings are included under Section 3.

3.6 THE ANNUAL REPORT AND STATEMENT OF ACCOUNTS

3.6.1 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.

3.6.2 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.

3.6.3 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 £4.37m in 2015/16 compared £5.2m in 2014/15 and 8.2m in 2013/14.

3.6.4 The Fund net cash flow position in 2015/16 is 16% less than the previous year. Investment income decreased over the year by £2.3m (13.5%) largely due to a reduction in dividend income. Transfer Values received (amounts paid over when a fund member transfers their benefits from one fund to another) increased by £447k (26%). 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 decrease slightly by £80k. Employer contributions went up by roughly £3m and this mainly due to an increase in the employer's deficit funding payment of £2m.

3.6.5 In 2015/16 the overall Fund expenditure reduced by £2.8m (34%). The major contributor to the reduction was the fall in transfers out of £3.2m (43.7%). There investment management costs increased by £626k (25.6%) over the year and did administration costs by £235k (29.3%). Benefits payable rose by £6.94m (15.32%), this is largely due to lump sum benefit paid in the year (an increase of £5.1m).

3.6.6 Overall, fund membership has increased slightly. The active members increased marginally by 116 (2%) and deferred and retired membership numbers by 336 (5.2%) and 221 (5.3%) respectively.

3.6.7 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 negative return on its investment portfolio of -1.3% in 2015/16 which underperformed the benchmark return of 1.1% by -2.4%. The Fund posted a 3 year return of 6.2%

which is marginally worse than the benchmark return of 6.3% but delivered a 10 year return of 4.7% underperforming a benchmark return of 5.3% by 0.6%.

3.6.8 Overall, fund assets reduced by £12m. The reduction was due to the performance of the financial markets in which the Fund held its investments and a net loss between fund income and expenditure.

3.6.9 The net asset statement represents the net worth (£1,126m) of the Fund as at the 31st March 2016. The statement reflects how the transactions outlined in the other statement have impacted on the value of the Fund's assets.

3.6.10 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.

3.6.11 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. The 2016 triennial valuation initial results has been discussed at the September meeting, as we are still waiting for the final valuation and contribution results, the contribution rate approval for the next three years will be sought at the next Committee meeting.

3.6.12 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.

3.6.13 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.

3.6.14 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

- Appendix A – LBTH ISA260 201516 DRAFT AC VERSION
- Appendix B – 2015/16 LBTH Pension Fund Annual Report
- Appendix C - LBTH PF Audit Opinion 1516

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

London Borough of Tower Hamlets Pension Fund Draft Annual Report and Accounts 2015/16

WWW.TOWERHAMLETS.GOV.UK

Contents

Foreword by Cllr Andrew Cregan

The Pensions Committee, which I have the privilege to Chair has the responsibility for all aspects of the Pension Fund including managing the investments, ensuring governance arrangements are appropriate and scheme members and employers are kept informed of key information.
The Committee carries with it a considerable responsibility to ensure that the Pension Fund, which was valued at £1,126m at 31 March 2016 and has over 19,000 scheme members, is managed in an efficient and effective way.

Key areas of focus for the Committee during the year revolved around ensuring that the Fund is able to meet the challenges posed by Central Government around investment reform. To this end the Committee has been very supportive of the establishment of the London Collective Investment Vehicle (CIV). The Committee fully support the development of the CIV but believe its future success will depend on the extent of flexibility, rather than compulsion, if national government allows. The Fund has transferred some 31% of the fund assets onto the LCIV platform with the fund's three existing fund managers under what LCIV named CQC, that is **Commonality** of mandate, **Quantum** of assets under manager, **Conviction,** how committed to the manager and mandate boroughs are.

The Fund has also supported collaborative working more generally, playing a key role in the development the National LGPS Procurement Framework.

Compliance with The Pension Regulator's new Code of Practice featured strongly on the Committee's agenda during 2015/16. Although following the Code itself is not a legal requirement, it sets out how the Regulator expects the requirements of the Public Sector Pensions Act 2013 should be met. The Regulator has the power to take action where the provisions of the Act are not being met, and will use the Code as a core reference document in deciding on the appropriate action to take. The Committee has considered whether the management of the LB Tower Hamlets Pension Fund meets the standards set out in the Code through use of a compliance checklist, and ensured that appropriate policies and processes are being developed for the few areas in which the Fund has not yet achieved full compliance.

In accordance with the new regulatory requirement to have additional governance arrangement in place by creating a Pension Board to assist the Administering Authority, London Borough of Tower Hamlets, in ensuring compliance with regulations. This board has been established and in operation, the board annual report is enclosed in this report.

The Fund net cash flow position remains positive with contributions and transfers in outstripping benefits paid and transfers out by £4.3m plus a further net inflow from investment income of £14.3m. 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.

A funding update has been received from the Fund Actuary, advising a that the fund funding level has risen by 11% from 72% with corresponding estimated deficit £365m as at 31 March 2013 triennial valuation to 83% with corresponding deficit of £235m. This was largely as a result of asset performance being better than expected. And the liability of the Fund shrunk from £1,293m as at 31 March 2013 triennial valuation to £1,361m as at 31 March 2016. Although equities have rebounded; bond yields are low 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 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.

All asset classes except equity delivered a positive performance over the year resulting in an overall marginal decrease in the assets under management. 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.

2015/16 was a difficult year for the Fund in terms of investment performance, resulting in a slight fall in the overall value of the Fund. Much of the poor performance was driven by the Fund's exposure to global equity markets which saw considerable volatility over the year, with particular concerns over stalling growth in China. The rout during August and September and further slide over the New Year both detracted from performance, although both were followed by periods of recovery.
Performance across other asset classes was also mixed, with market sentiment dominated by worries over global growth and central bank policy.

The Committee continued to monitor the investment portfolios and the performance of the Fund Managers it employs on a quarterly basis, as well as reviewing the rolling annual, 3yr and 5yr performance. By the end of the financial year the Pension Fund had seen a slight fall in value of around 1.07% to £1,126m decreasing from £1,138m at the end of March 2015.

Cllr. Andrew Cregan
Chair of Pensions Committee

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 2016

The Pensions Committee during 2015/16 was made up of eight Councillor Members, an Employer Representative and a Scheme Member representative.

Pensions Committee:

Councillors:	Councillor Andrew Cregan (Chair) Councillor Clare Harrisson (Vice Chair) Councillor Suluk Ahmed Councillor Harun Miah Councillor Mohammed Mufti Miah Councillor Abdul Mukit MBE Councillor Candida Ronald
Trade Union Representative (non-voting):	Kehinde Akintunde (GMB)
Admitted Bodies Representative (non-voting):	Tony Childs (Tower Hamlets Homes)

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:

Zena Cooke – Corporate Director, 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.

London LGPS CIV Ltd
70 Great Bridgewater Street, Manchester, M1 5ES.

Governance and Oversight Review

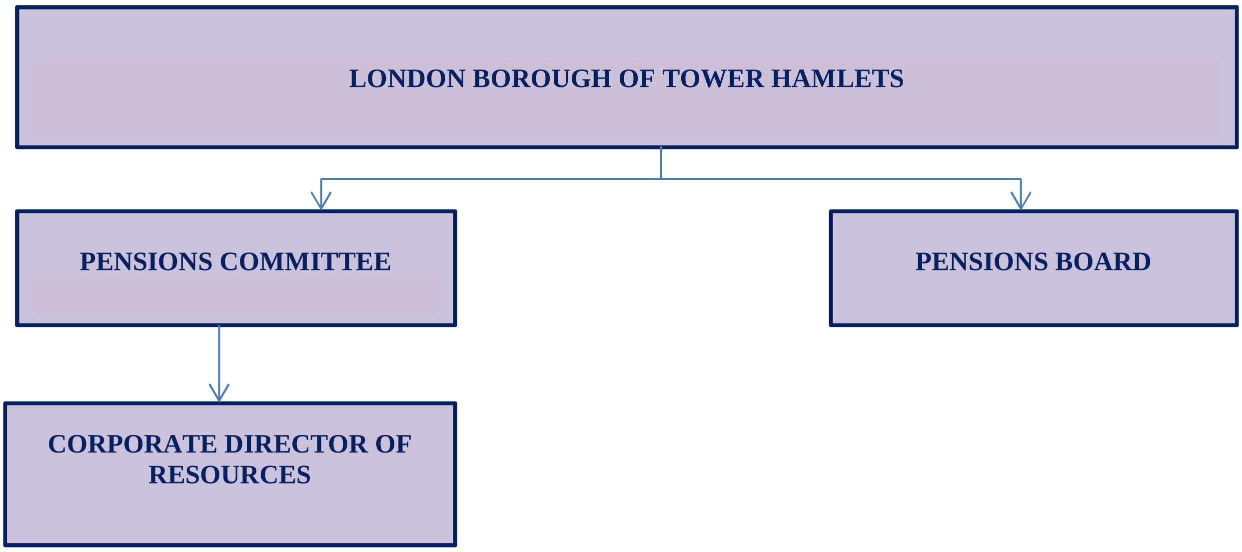
The Pension Fund Regulations require a new additional governance arrangement (Pensions Board) to be in place from 1 April 2015.

London Borough of Tower Hamlets is the Administering Authority of the pension Fund, 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.

Please see below chart illustrating the new governance arrangement.

<u>From Financial Year 2015/16</u>



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 2015/16

Attendee	Voting Rights	23-Jul	17-Sep	25-Nov	09-Mar
Member					
Cllr Andrew Cregan	√	Present	Present	Present	Present
Cllr Clare Harrisson	√	Present	Present	Present	Present
Cllr Suluk Ahmed	√		Present		
Cllr Harun Miah	√				
Cllr Mohammed Mufti Miah	√	Present			
Cllr Abdul Mukit MBE	√			Present	
Cllr Candida Ronald	√	Present		Present	Present
John Gray (Non-voting)	x		Present		
Tony Childs (Non-voting)	x				
Kehinde Akintunde (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
Zena Cooke	x	Present	Present	Present	Present
Ngozi Adedeji	x	Present	Present	Present	Present
Charles Yankiah	x				Present
Antonella Burgio	x	Present		Present	
David Knight	x		Present		
Public					
Raymond Haines (Adviser)	x	Present	Present	Present	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 2015/16 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

The second half of 2015 proved to be a difficult one for investors, and 2016 started in a similar fashion, with equity market volatility returning to levels not seen so consistently since the peak of the euro zone crisis in 2011. Global growth expectations have continued to be downgraded, repeating a pattern established over the last five years. Although much of the stress is being experienced in commodity related sectors, fears have grown of this spreading into the banking sector in the form of bad debts, which in turn raised concerns of a repeat of the financial crisis of 2008. Although we believe that to be too pessimistic a view, it betrays an underlying nervousness that permeates the investment community, leaving markets vulnerable to further negative developments.

Equity and Corporate Bond markets responded badly to three separate factors in the first six weeks of 2016. Initially there were concerns about China, concerns that have been magnified since the country initiated a devaluation of its currency in August 2015. A weaker renminbi is viewed as negative on two fronts: either it is a deliberate devaluation engineered by the Chinese government to boost an economy that is much weaker than they are owning up to in public data, or it is an expression of a lack of confidence by its citizens who would prefer to protect their capital by taking it out of the country. Neither option supports the already dull global growth outlook.
Once China stabilised, the oil price took centre stage, plumbing new depths for this cycle. A more negative interpretation of the lower oil price was a lack of global demand, playing to existing concerns about low growth, but our view remains that the current oil cycle is more about resurgent supply, which will eventually rebalance. However this will in all probability not happen until several oil companies, especially in the US shale sector, have gone bankrupt, and this is where concern about banks emerges. This concern was exacerbated by the negative interest rate policies of the European Central Bank (ECB) and the Bank of Japan (BoJ), policies which potentially make it much harder for banks to make a decent return on their equity.

Baillie Gifford Diversified Growth Fund - In the year to 31 March 2016 the Fund delivered a return (net of fees) of -1.5%. The return on the Fund (net of fees) over the past five years has been 4.3% on an annualised basis. Delivered volatility over the same period was 4.5% per annum.
Over the 12 months, active currency, infrastructure and insurance linked securities all contributed positively to performance. Within active currency a long position in the Japanese yen was a key driver of positive returns. The Fund's overall negative return was driven by weak performance of economically-sensitive asset classes, including listed equities, emerging market bonds and high yield credit.

Ruffer portfolio - Over the last year, the portfolio was down 4.2%. It is clearly disappointing that over the last twelve months the manager has not succeeded in their primary objective of preserving capital, an outcome largely rooted in the portfolio's fall in Q3 2015. With this in mind it was encouraging to see a much more robust performance from the portfolio in the first quarter of 2016 under not dissimilar circumstances.

GMO - The benchmark return for the 12 month period to 31 March 2016 was -1.2% and the assets invested with GMO lagged this with a return of -6.0% (net of fees). There was a significant amount of volatility during the period. The second quarter of 2015 was relatively calm for equity markets, but the strong pound sterling translated this to disappointing returns for GBP investors, then equity markets fell heavily in quarter three with much of the focus being on weak economic signs from China. There was a strong bounce back in the fourth quarter, with a much anticipated interest rate increase in the US proving to be a non-event from a market perspective, whilst the first quarter of 2016 proved to be the most volatile of all, with MSCI ACWI falling almost double digits in the first six weeks before recovering to finish positive in GBP terms at quarter end.

Baillie Gifford Global Alpha - In the 12 months to 31st March 2016, your portfolio returned -0.1%, marginally outperforming the benchmark by around 0.5%. Among the largest contributors to performance were Amazon (ecommerce), Ryanair (air travel) and Alphabet (internet search).
Amazon’s core ecommerce offering continues to grow strongly while its cloud computing platform, Amazon Web Services (AWS), now accounts for around 40% of earnings and has supported significant share price appreciation over the period. Looking further ahead, we believe Amazon’s focus on the long-term and ongoing investment bodes well for future earnings growth. Expansion to new airports and growing passenger numbers were behind Ryanair’s strong share price performance. Management maintained an admirable grip on the firm’s ex-fuel unit cost and improved its website, which should be positive for Ryanair in the long run as it looks to generate revenues via tailored ancillary offers and upselling. Within Alphabet, Google achieved revenue growth of over 20%+ year-on-year, driven mainly by strength in mobile search. Google now has several platforms with over 1 billion users each – the fastest growing of which is YouTube, which is benefitting from a growing trend towards watching content online and generated $9bn of revenue in FY’15.
Stocks which detracted from performance included Ultra Petroleum (oil and gas), Prudential (insurance) and Carmax (used car retail).

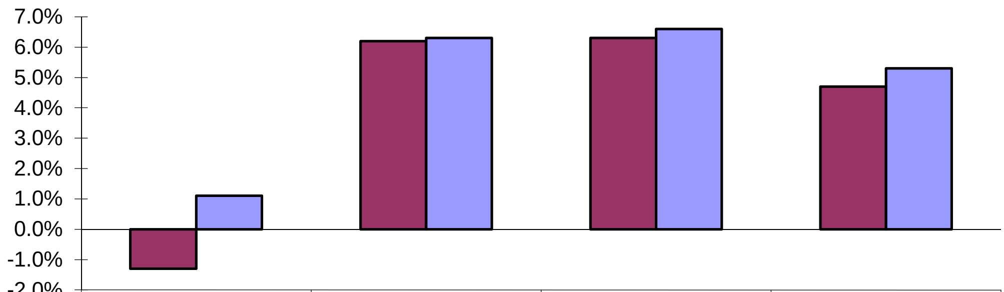
Schroder (Property) – The twelve months to March 2016 represented another strong year for UK commercial real estate, with the market delivering unleveraged total returns of 11%. Most of this performance was driven by rental growth, as a buoyant economy and low levels of development pushed rental levels up in most sectors. Performance was front end loaded, with investors more cautious at the end of 2015 and in the first few months of 2016. Accordingly, the IPD all property initial yield stabilised at 5.0% last October and secondary units in many unlisted funds switched from trading at premiums to discounts.
Central London offices delivered the strongest returns in the year to end March 2016 (16%), although after a long period of rental growth and falling yields, this is the part of the market that looks most vulnerable to a correction in pricing. Regional office markets (13%) and industrials (14%) also delivered strong return returns, the latter recording unprecedented levels of rental growth in some markets. The retail sector remains the laggard (8%), with very little rental growth outside of central London. Secondary high streets and shopping centres in particular, are still suffering from the growth in e-tailing and an oversupply of retail space from the previous cycle. Alternative property sectors, including student accommodation and healthcare, delivered returns of 10%, derived largely from a higher than average income return. These sectors are expected to be more defensive in the next stage in the cycle, with demand often driven by structural changes such as demographics and less linked to the economic cycle.

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".

The fund performance was disappointing over the latest year, with the fund recording an absolute return of -1.3%, 2.4% behind the benchmark and 1.6% below the local authority average return. The three year return also marginally lagged behind the benchmark with the fund returning 6.2% against a benchmark of 6.3%. The return for 5 year and 10 year continued to lag the benchmark by 0.3% and 0.6% respectively.

<u>Fund Performance (One, Three, Five and 10 Years)</u>



	One Year	3 Years	5 Years	10 Years
Fund	-1.3%	6.2%	6.3%	4.7%
Benchmark	1.1%	6.3%	6.6%	5.3%
Relative Return	(2.4%)	(0.1%)	(0.3%)	(0.6%)
Rank	77	57	80	81

Fund Management Activity

The London Borough of Tower Hamlets Pension Fund has been actively managed on a specialist basis by: Baillie Gifford and GMO (Global Equities), Investec Asset Management (Corporate Bonds), Schroders Property Capital Partners (Property), Baillie Gifford and Ruffer LLP (DGF) and passive management of UK Equities and UK Gilt & Index Linked by Legal & General Investment Management (LGIM).

Towards the end of the year, February 2016, the Baillie Gifford DGF mandate was transferred to the London CIV platform with the same target benchmark and the Investec mandate was redeemed 22nd March 2016.

The volatility 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.
The underperformance from GMO, Ruffer and Baillie Gifford Diversified Growth was unfavourable.
.
The main driver of GMO underperformance over the period stems from being underweight the U.S. and overweight Emerging Markets, although individual stock selection was also a detractor over the period, with Amazon's outperformance being outweighed by

underperformance from Valeant Pharmaceuticals. The manager advised that they retain conviction in their U.S. vs Emerging view but have reduced the concentration of single stock positions, so would not expect single names to dominate performance attribution in future periods.

The fund continues to participate in the Collective Investment Vehicle (CIV) and at the time of writing this report, Baillie Gifford (Global Equity) mandate and Ruffer LLP mandate have been transferred to LCIV platform.

The fund received a positive cash flow from dealings with members of £4.37m 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 2016 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%	19%	-5%
Global Equities	37.0%	41%	4%
UK Index Linked	3.0%	5%	2%
Pooled Bonds	14.0%	0%	-14%
Property	12.0%	12%	0%
Alternatives	10.0%	10%	0%
Cash	0.0%	13%	13%

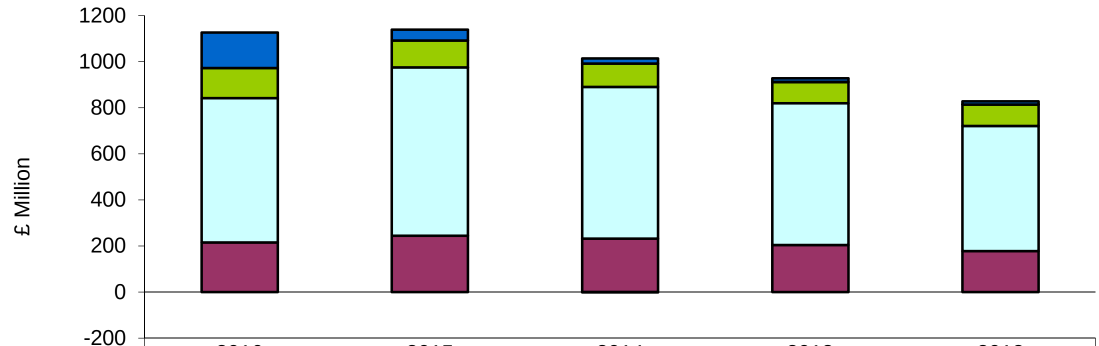
The Fund remains close to its strategic allocation although the bond mandate was redeemed at 22nd March 2016, hence there is an overweight cash position at year end. This cash was used to fund the two new bond pooled investment funds with Goldman Sachs Assets Management and Insights Investments Management.

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 2015/16 the value of the Fund decline slightly by £12m from £1,138.2m to £1126m, a decrease of 1.05%. This is mainly attributable to the underperformance of the Fund global equity managers.

ANALYSIS OF ASSET CLASS

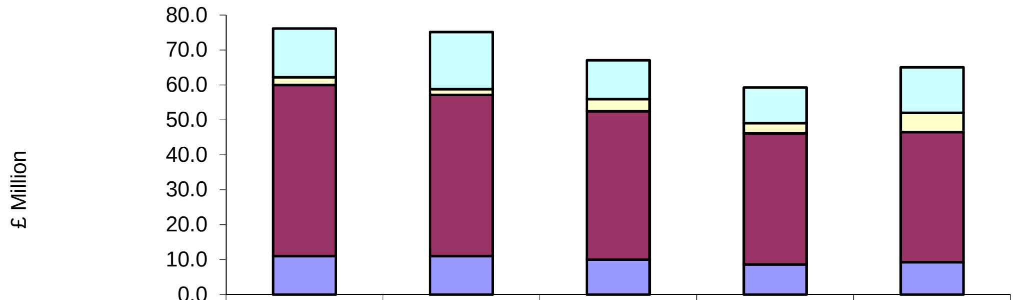


	2016	2015	2014	2013	2012
Cash	154.6	47.2	21.6	15.1	14.2
Derivatives	0	0	-0.4	0.5	0.2
Property Units	129.9	116.9	102.1	92.1	92
Unit Trusts	626.9	730	658.7	615.2	542.9
Equities	214.6	244.3	231.0	203.9	177.9

Fund Income

There was a reduction in the amount of income received by the Fund in 2015/16 compared to 2014/15.

Fund Income Analysis



	2016	2015	2014	2013	2012
Investment Income	13.9	16.3	11.1	10.2	13
Transfer Values	2.2	1.7	3.5	2.9	5.5
Council Related Contributions	49.0	46.1	42.4	37.5	37.3
Employees Contributions	11.0	11.0	10.0	8.6	9.2

Investment income decreased over the year by £2.4m, mainly due to a reduction in dividend income. Transfer Values received (amounts paid over when a fund member transfers their benefits from one fund to another) increased by £500k. It is not possible to predict the value of transfer value payments as they are dependent on individual's length of service and salary and as such may vary significantly. Employee contributions remain the same. Employer contributions went up by £2.9m (6.3%) mainly due to an increase in the employer's deficit funding payment of £2m.

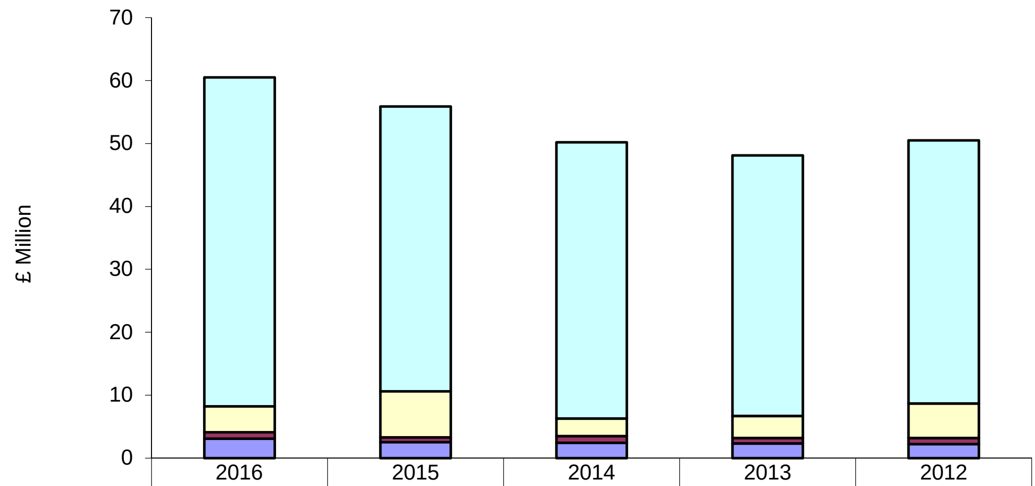
Fund Income Variance Analysis

Type of Income	2016 £m	2015 £m	Variance %
Employees Contributions	11.0	11.0	0.0%
Council Related Contributions	49.0	46.1	6.3%
Transfer Values	2.2	1.7	29.4%
Investment Income	13.9	16.3	-14.7%
Total Fund Income	**76.1**	**75.1**	**1.3%**

Fund Expenditure

In 2015/16 the overall Fund expenditure increased by £4.6m (8..4%). The major contributor to the increase was the rise in Benefits payable by £7m (15.5%). (160.7%). There was also a significant in investment management costs of £0.6m (24%) while transfers out fell by £3.2m (43.8%) and a modest rise in administration costs by £0.2m (25%), this increase is mainly due to capital regulatory contribution to LCIV.

Fund Expenditure Analysis



	2016	2015	2014	2013	2012
Benefits Payable	52.3	45.3	43.9	41.4	41.8
Transfer Values	4.1	7.3	2.8	3.5	5.5
Administration	1.0	0.8	1.1	0.9	1.0
Investment Management	3.1	2.5	2.4	2.3	2.2

The reduction in transfers out was a reflection of the value of transfer out payments being made, it could be combination of different things the number of staff leaving had reduced significantly and or lower salary paid leavers. The investment management fees which are performance based have risen in line with the increase in the market value of the funds held during the year.

Fund Expenditure Variance Analysis

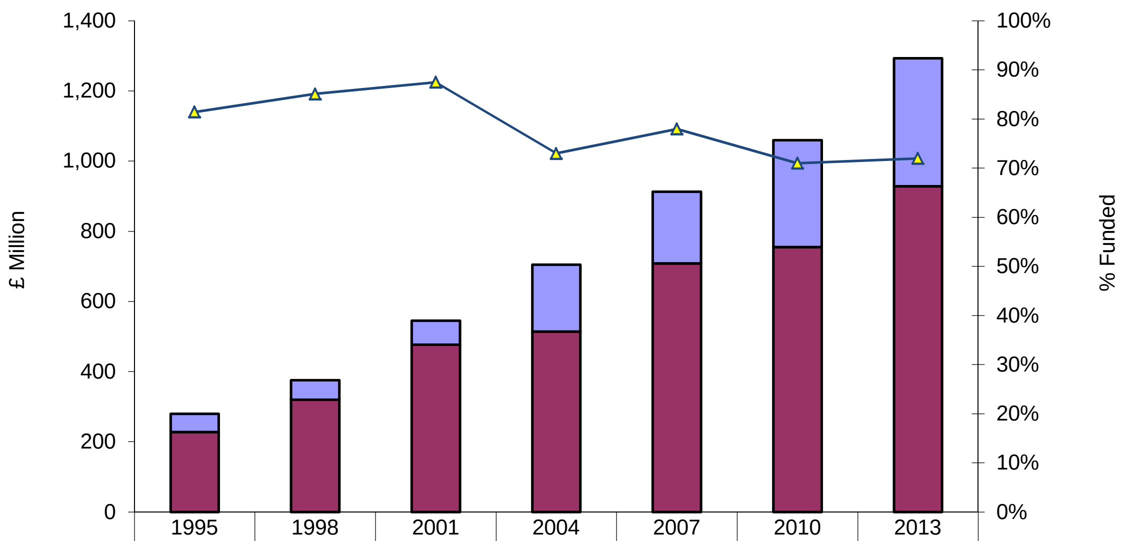
Type of Expenditure	2016	2015	Variance £m	Variance %
Investment Management	3.1	2.5	0.6	24.0%
Administration	1.0	0.8	0.2	25.0%
Transfer Values	4.1	7.3	-3.2	-43.8%
Benefits Payable	52.3	45.3	7.0	15.5%
Total Fund Expenditure	60.5	55.9	4.6	8.2%

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.

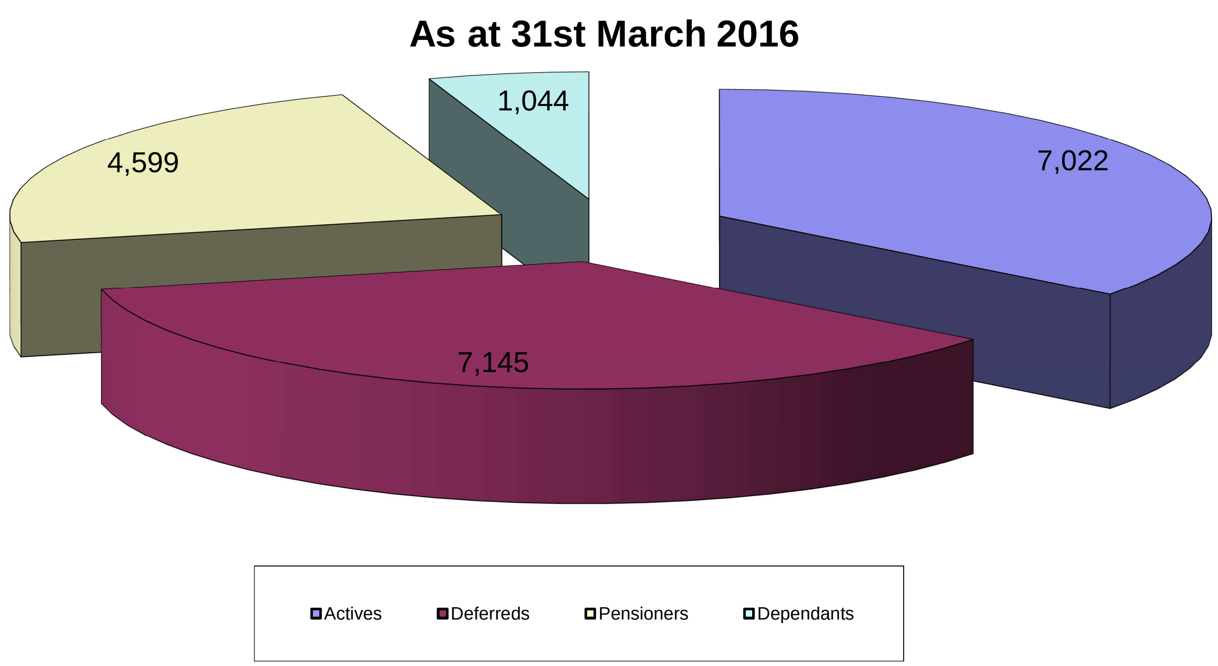
It should be noted that the foregoing is not an exhaustive list and that certain conditions have to be met for an individual to be entitled to the benefits outlined.

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 19,810 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 4.2% between 2014/15 and 2015/16. The number of actives members (those currently contributing to the fund) has increased by 162 (2.4%). The deferred membership category (members who have contributed in the past but who have not yet become entitled to their benefits) has increased by 359 (5.3%) and pensioner members by 247 (5.7%). The dependants' category saw an increase of 33 (3.3%).

The table below sets out the movement in membership number between the different categories in 2014/15 and 2015/16.

Movement in Fund Membership

Membership Type	31-Mar-16	31-Mar-15	Variance No.	Variance %
Actives	7,022	6,860	162	2.4%
Deferreds	7,145	6,786	359	5.3%
Pensioners	4,599	4,352	247	5.7%
Dependants	1,044	1,011	33	3.3%
Total	19,810	19,009	801	4.2%

The membership of the fund over the last five years is as set out below.

Membership Type	31-Mar-16	01-Apr-15	31-Mar-14	31-Mar-13	31-Mar-12
Actives	7,022	6,860	6,792	5,298	5,252
Deferreds	7,145	6,786	6,664	6,292	6,060
Pensioners	4,599	4,352	4,246	4,148	4,064
Dependants	1,044	1,011	975	979	940
Total	19,810	19,009	18,677	16,717	16,316

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 admitted bodies and scheduled participating in the fund are set out below.

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

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

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 £22m 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 Corporate Director, 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 Corporate Director, Resources

The Corporate Director, 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 Corporate Director, 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 Corporate Director, 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 31 to 47 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 2016 and the amount and disposition of the Fund's assets and liabilities as at 31 March 2016.

Zena Cooke
Corporate Director, 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 and Accounts

We have audited the financial statements of pension fund financial statements published with the Pension Fund Annual Report and Accounts for the year ended 31 March 2016 on pages 32 to 48. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

This report relates to the pension fund financial statements published with the Pension Fund Annual Report and Accounts and is made solely to the members of the Authority, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014. Our audit work has been undertaken so that we might state to the members of the Authority, as a body, those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the members of the Authority, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Corporate Director of Resources and auditor

As explained more fully in the Statement of the Corporate Director of Resources' Responsibilities, the Corporate Director of Resources is responsible for the preparation of the pension fund financial statements published with the Pension Fund Annual Report and Accounts, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that the financial statements give a true and fair view. Our responsibility is to audit, and express an opinion on, the pension fund financial statements published with the Pension Fund Annual Report and Accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the pension fund financial statements, published with the Pension Fund Annual Report and Accounts, sufficient to give reasonable assurance that the pension fund financial statements, published with the Pension Fund Annual Report and Accounts, are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Pension Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Corporate Director of Resources; and the overall presentation of the pension fund financial statements published with the Pension Fund Annual Report and Accounts.

In addition, we read all the financial and non-financial information in the Pension Fund Annual Report and Accounts to identify material inconsistencies with the audited pension fund financial statements, published with the Pension Fund Annual Report and Accounts, and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the pension fund financial statements published with the Pension Fund Annual Report and Accounts:

- give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2016 and the amount and disposition of the Fund's assets and liabilities as at 31 March 2016 other than liabilities to pay pensions and other benefits after the end of the scheme year; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

Matters on which we are required to report by exception

The Code of Audit Practice requires us to report to you if:

- the information given in the Pension Fund Annual Report for the financial year for which the financial statements are prepared is not consistent with the financial statements; or
- any matters have been reported in the public interest under Section 24 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of, the audit; or
- any recommendations have been made under Section 24 of the Local Audit and Accountability Act 2014; or
- any other special powers of the auditor have been exercised under the Local Audit and Accountability Act 2014.

We have nothing to report in respect of these matters.

Andrew Sayers
For and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square, London, E14 5GL
30 November 2016

The London Borough of Tower Hamlets Pension Fund

Appendix 1

Draft Statement of Accounts 2015/16

PENSION FUND ACCOUNTS

PENSION FUND ACCOUNT	Note	2014/15 £'000	2015/16 £'000
DEALINGS WITH MEMBERS, EMPLOYERS AND OTHERS DIRECTLY INVOLVED IN THE SCHEME			
Contributions			
From employers			
Normal	3	26,855	26,812
Augmentation	3	780	1,697
Deficit funding	3	18,500	20,500
From members	3	11,031	10,951
Transfers in			
Transfers in from other pension funds	4	1,719	2,166
Benefits			
Pensions	4	(37,265)	(39,103)
Lump sum benefits	4	(8,055)	(13,158)
Payments to and on account of leavers			
Refunds of contributions		(125)	(169)
State scheme premiums		(132)	(196)
Transfers out to other pension funds		(7,263)	(4,092)
Administrative expenses	13	(803)	(1,038)
NET ADDITIONS FROM DEALINGS WITH MEMBERS		**5,242**	**4,370**
RETURN ON INVESTMENTS		**2014/15 £'000**	**2015/16 £'000**
Investment income	11	16,581	14,349
Taxes on Income		(329)	(409)
Change in market value of investments			
Realised		23,292	1,321
Unrealised	10	82,933	(28,625)
Investment management expenses	13	(2,450)	(3,076)
NET RETURN ON INVESTMENTS		**120,027**	**(16,440)**
Net increase in the Fund during the year		125,269	(12,070)
Add: Opening net assets of the scheme		1,012,930	1,138,199
CLOSING NET ASSETS OF THE SCHEME		**1,138,199**	**1,126,129**

NET ASSETS STATEMENT AS AT 31ST MARCH	Note	2015 £'000	2016 £'000
Investments Assets			
Equities		244,335	214,617
Pooled Investment Vehicles			
Unit Trusts		628,744	572,275
Property		116,945	129,933
Other		101,303	54,607
		1,091,327	971,432
Cash deposits	6	5,414	5,647
Other investment balances	5	978	1,973
Investments Liabilities			
Other investment balances	5	(223)	(35)
Current Assets	5	42,154	149,054
Current Liabilities	5	(1,451)	(1,942)
TOTAL NET ASSETS		**1,138,199**	**1,126,129**

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 Government Pension Scheme Regulations 2013 (as amended) and the Local Govememnt 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 2016. 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 2016.
(ii) Pooled investment vehicles are valued at bid price, middle market price or single price at close of trading on 31st March 2016.
(iii) Property unit trusts are shown by reference to bid price at close of business on 31st March 2016.
(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 2016. 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) 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.

Administrative Expenses

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.

Oversight & Governance Costs

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.

Investment Management Expenses

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.

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 2016 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 2015/16, the Council's actuaries advised that the net pensions liability had decreased by £123.5 million to £505.0 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 2016 range from 15.9% to 41.4% of pensionable pay. The Council paid an agreed additional monetary contribution of £20.5m to recover the deficit. Contributions shown in the revenue statement may be categorised as follows:-

	2014/15 £'000	2015/16 £'000
Members normal contributions		
Council	9,731	9,673
Admitted bodies	221	184
Scheduled body	1,079	1,094
Total members	**11,031**	**10,951**
Employers		
Normal contributions		
Council	22,356	22,105
Admitted bodies	1,015	887
Scheduled bodies	3,484	3,820
Deficit funding contributions		
Council	18,500	20,500
Other contributions		
Council	780	1,697
Total employers	**46,135**	**49,009**
Total contributions	**57,166**	**59,960**

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 2015/16 employees made contributions of £10,870.28 (£60,530.28 in 2014/15) into the AVC Scheme operated by Aviva (Norwich Union) and £8,434.33 to Equitable Life (£9,455.96 in 2014/15). 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 based on the consumer price 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.

	2014/15				2015/16			
	Council £'000	Admitted Bodies £'000	Scheduled Bodies £'000	Total £'000	Council £'000	Admitted Bodies £'000	Scheduled Bodies £'000	Total £'000
Pensions	(35,259)	(1,126)	(880)	(37,265)	(37,467)	(585)	(1,051)	(39,103)
Lump sum retirement benefits	(6,027)	(307)	(379)	(6,713)	(10,828)	(441)	(425)	(11,694)
Lump sum death benefits	(1,232)	(42)	(68)	(1,342)	(1,080)	(175)	(208)	(1,463)
Total Pensions and Benefits	**(42,518)**	**(1,475)**	**(1,327)**	**(45,320)**	**(49,375)**	**(1,201)**	**(1,684)**	**(52,260)**
Transfer Values Received (Individual)	1,719	0	0	1,719	2,166	0	0	2,166
Transfer Values Paid (Individual)	(7,263)	0	0	(7,263)	(4,092)	0	0	(4,092)
Total	**(48,062)**	**(1,475)**	**(1,327)**	**(50,864)**	**(51,301)**	**(1,201)**	**(1,684)**	**(54,186)**

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.

	2014/15 £'000	2015/16 £'000
Debtors		
Other Investment Balances		
Investment sales	8	805
Dividends receivable	583	649
Tax recoverable	387	519
	978	1,973
Current Assets		
Contributions due from admitted bodies	101	237
London Borough of Tower Hamlets Pension Fund	230	457
	331	694
Total Debtors	**1,309**	**2,667**
Creditors		
Other Investment Balances		
Investment purchases	223	35
Current Liabilities		
Unpaid benefits	1,138	1,271
Administrative expenses	313	671
London Borough of Tower Hamlets Pension Fund	0	0
	1,451	1,942
Total Creditors	1,674	1,977
Net Debtors	**(365)**	**690**

6. CASH

The deposits held by fund managers can be further analysed as follows:

	2014/15 £'000	2015/16 £'000
Aberdeen: Private Equity Portfolio	10	10
GMO	2,930	3,702
Schroders: Multi Asset Portfolio	15	0
Schroders: Property Portfolio	2,458	1,934
London Borough of Tower Hamlets Pension Fund	41,823	148,359
TOTAL CASH	**47,236**	**154,005**

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 25th November 2015.

9. MEMBERSHIP OF THE FUND

The following table sets out the membership of the Fund at 31st March:

	2015	2016
London Borough of Tower Hamlets		
Active Members	6,249	6,365
Pensioners	4,131	4,352
Deferred Pensioners	6,434	6,770
Dependants	993	1,018
	17,807	**18,505**
Admitted & Scheduled Bodies		
Active Members	611	657
Pensioners	221	247
Deferred Pensioners	352	375
Dependants	18	26
	1,202	**1,305**

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 nine 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:

	2015		2016	
	£ million	%	£ million	%
Baillee Gifford Life Ltd - Diversified Growth	50.7	4.6	0.0	-
Baillee Gifford Life Ltd - Equities	217.7	19.8	209.9	21.4
GMO UK Ltd.	274.3	25.0	248.4	25.4
Investec Asset Management	99.6	9.1	0.0	-
Legal & General Investment Management - Equities	225.7	20.1	217.3	22.2
Legal & General Investment Management	59.4	5.9	60.6	6.2
Ruffer LLP	50.6	4.6	54.6	5.6
Schroders Asset Management Property Fund	119.5	10.9	131.9	13.5
London CIV	0.0	0.0	56.3	5.8

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 2015 £'000	Purchases £'000	Sales £'000	Change in Market Value £'000	Market Value as at 31 Mar 2016 £'000
Baillee Gifford Life Ltd - Diversified Growth	50,685	6,490	(46,746)	(10,429)	0
Baillee Gifford Life Ltd - Equities	217,670	481	(3,274)	(4,989)	209,888
GMO UK Ltd.	270,637	244,815	(256,368)	(16,288)	242,796
Investec Asset Management	99,631	0	(98,701)	(930)	0
Legal & General Investment Management	285,141	0	0	(7,277)	277,864
Ruffer LLP	50,618	6,474	0	(2,486)	54,606
Schroders Asset Management Property	116,945	10,360	(8,978)	11,607	129,934
London CIV	0	54,177	0	2,167	56,344
	1,091,327	322,797	(414,067)	(28,625)	971,432
Other Investment Balances					
Cash Deposits	5,414	0	0	0	5,647
Investment income due	978	0	0	0	1,973
Amounts payable for purchases of investments	(223)	0	0	0	(35)
Net Investment Assets	6,169				7,585

	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
Derivative Contracts					
Forward Currency Contracts	(409)	0	0	409	0
	(409)	0	0	409	0
Other Investment Balances					
Cash Deposits	5,292	0	0	0	5,414
Investment income due	817	0	0	0	978
Amounts payable for purchases of investments	0	0	0	0	(223)
Net Investment Assets	6,109				6,169

10. INVESTMENTS (continued)

A further analysis of investments assets is as follows.

	Market Value as at 1 Apr 2015 £'000	Market Value as at 31 Mar 2016 £'000
Equities		
UK		
Quoted	27,874	16,023
Overseas		
Quoted	216,487	198,593
	244,361	214,616
Pooled Funds - Additional Analysis		
UK		
Fixed Income Unit Trust	159,079	60,630
Unit Trusts	544,666	538,072
Overseas		
Unit Trusts	26,276	28,181
	730,021	626,883
Pooled Property Investments	116,945	129,934
	116,945	129,934
Cash Deposits	5,414	5,647
Investment Income Due	978	1,973
	6,392	7,620
Total Investment Assets	1,097,719	979,053
Investment Liabilities		
Amounts Payable for Purchases	(223)	(35)
Total Investment Liabilities	(223)	(35)
Net Investment Assets	**1,097,496**	**979,018**

10. INVESTMENTS (continued)

A further analysis of investments assets is as follows.

	Market Value as at 1 Apr 2015 £'000	Market Value as at 31 Mar 2016 £'000
Equities		
UK		
Quoted	27,874	16,023
Overseas		
Quoted	216,487	198,593
	244,361	214,616
Pooled Funds - Additional Analysis		
UK		
Fixed Income Unit Trust	159,079	60,630
Unit Trusts	544,666	538,072
Overseas		
Unit Trusts	26,276	28,181
	730,021	626,883
Pooled Property Investments	116,945	129,934
	116,945	129,934
Cash Deposits	5,414	5,647
Investment Income Due	978	1,973
	6,392	7,620
Total Investment Assets	1,097,719	979,053
Investment Liabilities		
Amounts Payable for Purchases	(223)	(35)
Total Investment Liabilities	(223)	(35)
Net Investment Assets	**1,097,496**	**979,018**

11. INVESTMENT INCOME

Investment income is broken down as follows.

	2014/15 £'000	2015/16 £'000
Dividends from overseas equities	10,617	8,660
Net rents from properties	5,234	4,733
Interest on cash deposits	170	387
Foreign tax	231	160
TOTAL	16,252	13,940

TAXES ON INVESTMENT INCOME

	2014/15 £'000	2015/16 £'000
Withholding tax - fixed interest securities	0	0
Withholding tax - equities	281	360
Withholding tax - pooled	47	49
TOTAL	328	409

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 2015/16 was 18.5%.

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 £1,659 million (£1,763 million in 2014/15). This includes both vested and non-vested benefits.

Assumptions

To assess the value of the employer's liabilities the actuary rolls forward the values from the liabilities calculated from the funding valuation as at 31 March 2013 using financial assumptions that comply with IAS 19

Demographic assumptions

The demographic assumptions used are consistent with those used for the funding valuation as at March 2013

Average future life expectancies at age 65 years	Males	Females
Current pensioners	22	24
Future pensioners	24	26

Financial assumptions

Year ended	31st March 2015	31st March 2016
Pension increase rate	2.4%	2.2%
Salary increase rate	3.8%	3.7%
Discount rate	3.2%	3.5%

13. MANAGEMENT EXPENSES

	2014/15 £'000	2015/16 £'000
Administration costs	714	910
Investment management expenses	2,450	3,076
Oversight & governance	69	107
Audit Fee	21	21
	3,254	4,114

14. INVESTMENT EXPENSES

	2014/15 £'000	2015/16 £'000
Management fees	2,357	2,901
Custody fees	93	175
	2,450	3,076

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

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 2015 and 31st March 2016 is set out below.

Interest Rate Risk	As At 31st March 2015	As At 31st March 2016
Asset Type	£'000	£'000
Cash and cash equivalents	5,414	5,647
Cash balances	42,154	149,053
Fixed interest securities	159,079	60,630
Total	**206,647**	**215,330**

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 2016	Change in year in net assets available to pay benefits	
		+100 BPS	-100 BPS
Asset Type		£'000	£'000
Cash and cash equivalents	5,647	56	(56)
Cash balances	149,053	1,491	(1,491)
Fixed interest securities	60,630	(606)	606
Total change in net assets available	**215,330**	**941**	**(941)**

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**

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 6.8%. 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 2016 and as at the previous year end.

Currency Exposure - Asset Type Asset Type	As At 31st March 2015 £'000	As At 31st March 2016 £'000
Overseas quoted securities	245,548	230,423
Overseas unit trusts	3,808	3,574
Cash	14	0
Total overseas assets	**249,370**	**233,997**

Currency Exposure - Sensitivity Analysis	Carrying Amount As At 31st March 2016	Change in year in net assets available to pay benefits	
		+6.8%	-6.8%
Asset Type	£'000	£'000	£'000
Overseas quoted securities	230,423	246,092	214,754
Overseas unit trusts	3,574	3,817	3,331
Cash	0	0	0
Total change in net assets available	**233,997**	**249,909**	**218,085**

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
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**

The percentage change in the year of 6.8% 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 2015/16 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 Asset Type	Potential Market Movements (+/-)
UK equities	10.6%
Global equity	11.3%
Total fixed interest	3.8%
Alternatives	4.6%
Cash	0.0%
Pooled Property Investments	2.2%

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 2016 £'000	Percentage change %	Value on increase £'000	Value on decrease £'000
Cash and cash equivalents	154,005	0.0%	154,005	154,005
Investment portfolio assets				
UK equities	217,234	10.6%	240,261	194,207
Global equity	452,685	11.3%	503,838	401,532
Total fixed interest	60,630	3.8%	62,934	58,326
Alternatives	110,950	4.6%	116,054	105,846
Pooled Property Investments	129,934	2.2%	132,793	127,075
Net derivative assets	0	0.0%	0	0
Investment income due	1,973	0.0%	1,973	1,973
Amounts receivable for sales	0	0.0%	0	0
Amounts payable for purchases	(35)	0.0%	(35)	(35)
Total assets available to pay benefits	**1,127,376**	**0%**	**1,211,822**	**1,042,929**

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**

Refinancing risk

The Council does not have any financial instruments that have a refinancing risk as part of its treasury management and investment strategies.

16a. VALUATION OF FINANCIAL INSTRUMENTS CARRIED AT FAIR VALUE

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 2016.

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Equities	214,617	0	0	214,617
Pooled Funds				
Unit Trusts	572,275	0	0	572,275
Property Unit Trust	129,933	0	0	129,933
Other	54,607	0	0	54,607
Derivative Contracts				
Forward Foreign Exchange Contracts	0	0	0	0
Cash and bank Deposits	154,464	0	0	154,464
Current Assets	2,210	0	0	2,210
Current Liabilities	(1,977)	0	0	(1,977)
	1,126,129	**0**	**0**	**1,126,129**

During the year ended 31st March 2016 there were no transfers between the levels of the fair value hierarchy.

The equivalents at 31st March 2015 were as follows:

	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**

16b. FINANCIAL INSTRUMENTS DISCLOSURES

Net gains and losses on financial istruments

	Long-term	
	2014/15 £'000	2015/16 £'000
Financial Assets		
Loans and receivables	180	398
Financial assets at fair value through profit or loss	106,225	(27,304)
Total Financial Assets	**106,405**	**(26,906)**
Financial Liabilities		
Payables		
Financial liabilities at fair value through profit or loss	409	0
Total Financial Liabilities	**409**	**0**

17. CURRENT ASSETS

	2014/15 £'000	2015/16 £'000
Contributions due - employers	101	236
Sundry debtors	230	458
Cash balances	41,823	148,359
	42,154	**149,053**

Analysis of debtors	2014/15 £'000	2015/16 £'000
Other entities and individuals	42,154	149,053
	42,154	**149,053**

18. CURRENT LIABILITIES

	2014/15 £'000	2015/16 £'000
Sundry creditors	313	671
Benefits payable	1,138	1,271
	1,451	**1,942**

Analysis of creditors	2014/15 £'000	2015/16 £'000
Other entities and individuals	1,451	1,942
	1,451	**1,942**

19. 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 (£669k 2014/15) relating to administration of the Fund and has been reimbursed by the Fund for these expenses. The Council contributed £20.5m (£18.5m 2014/15) 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 2016, the Fund held an average investment of £48.1m (£24.8m 31st March 2015), earning interest of £398k (£180k in 2014/15).

The Council has a subsidiary company, Tower Hamlets Homes, who are within the Fund. During the year the Fund received contribution payments totalling £3.4m (£3.5m 2014/15) from this company.

Fund administration expenses payable to the administrating authority are as set out in the table below.

Fund Administration Expenses	2014/15 £'000	2015/16 £'000
Payroll / HR Support	370	494
Corporate Finance	299	175
	669	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

	2014/15 £'000	2015/16 £'000
Short term benefits	20	19
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.

20. 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 2016 was £2.542m (£9.654m 2014/15).

21. 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.

22. IMPAIRMENT LOSSES

During 2015/16 impairment losses were nil (impairment losses in 2014/15 were also nil).

The London Borough of Tower Hamlets Pension Fund

Appendix 2

Statement of Investment Principles

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**	**Benchmark Allocation**	**Investment Ranges**	**Performance Target**
Baillie Gifford (LCIV)	Global Equities Diversified Growth	18% 5%	16-20% 4-6%	Outperform benchmark by 2-3% over a rolling 3 year period 3.5% above UK Base Rate
GMO	Overseas Equities	23%	20-25%	Outperform benchmark by 1.5% over a rolling 3 year period
Investec	Pooled Bonds	17%	15-20%	3 month LIBOR +2% pa
Legal & General	UK Equities UK Index Linked	20% 3%	16-24% 3-5%	FTSE All share FTSE A Gov Index Linked >5yrs
Ruffer (LCIV)	Diversified Growth	5%	4-6%	Greater than the expected return on cash
Schroders	Property	12%	10-14%	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

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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.

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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).

[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.

London Borough of
Tower Hamlets Pension Fund
Appendix 6
Training & Development Policy

Introduction

This is the Training & Development Policy of the London Borough of Tower Hamlets Pension Fund in relation to the Local Government Pension Scheme (LGPS), which is managed and administered by Tower Hamlets Council. The Policy details the training strategy for members of the Pensions Committee and Pension Board, and senior officers responsible for the management of the Fund.

This Training & Development Policy is established to assist Pensions Committee and Pensions Board members and senior officers in developing their knowledge and capabilities in their individual roles, with the ultimate aim of ensuring that the London Borough of Tower Hamlets Pension Fund is managed by individuals who have the appropriate levels of knowledge and skills.
Tower Hamlets Council has delegated responsibility for the implementation of this Training & Development Policy to the Corporate Director, Resources.

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 19,000 current and former members of the Fund, and their dependants
- about 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, the 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

This Policy has been put in place to assist the Fund in achieving these objectives and all Pensions Committee Members, Pension Board members and senior officers to whom this Policy applies are expected to continually demonstrate their own personal commitment to training and to ensuring that these objectives are met.

To assist in achieving these objectives, the London Borough of Tower Hamlets Pension Fund will aim 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.

This Training & Development Policy applies to all Members of the Pensions Committee, Pensions Board, including scheme member and employer representatives. It also applies to all managers in the Tower Hamlets Council Pension Fund Management Team and the Chief Finance Officer (Section 151 Officer) (from here on in collectively referred to as the senior officers of the Fund).

Other officers involved in the daily management of the Pension Fund will also be required to have appropriate knowledge and skills relating to their roles, which will be determined and managed by the Pension Fund Manager and Investment & Treasury Manager and his/her team.
The advisers to the Fund that provides the day to day and strategic advice to the London Borough of Tower Hamlets Pension Fund are also expected to be able to meet the objectives of this Policy, as are all other officers of employers participating in the London Borough of Tower Hamlets Pension Fund who are responsible for pension matters are also encouraged to maintain a high level of knowledge and understanding in relation to LGPS matters, and Tower Hamlets Council will provide appropriate training for them.
This is considered separately in the London Borough of Tower Hamlets Pension Fund Administration Strategy.

CIPFA and TPR Knowledge and Skills Requirements - *(CIPFA Knowledge and Skills Framework and Code of Practice)*

In January 2010 CIPFA launched technical guidance for Representatives on Pensions Committees and non-executives in the public sector within a knowledge and skills framework. The Framework details the knowledge and skills required by those responsible for pension scheme financial management and decision making.

In July 2015 CIPFA launched technical guidance for Local Pension Board members by extending the existing knowledge and skills frameworks in place. This Framework details the knowledge and skills required by Pension Board members to enable them to properly exercise their functions under Section 248a of the Pensions Act 2004, as amended by the Public Service Pensions Act 2013.

The Framework covers eight areas of knowledge and skills identified as the core requirements (which include all those covered in the existing Committee and nonexecutives' framework):

i) Pensions legislation
ii) Public sector pensions governance
iii) Pension accounting and auditing standards
iv) Pensions administration
v) Financial services procurement and relationship management
vi) Investment performance and risk management
vii) Financial markets and products knowledge
viii) Actuarial methods, standards and practice

CIPFA's Code of Practice recommends (amongst other things) that Local Government Pension Scheme administering authorities -

- formally adopt the CIPFA Knowledge and Skills Frameworks (or an alternative training programme)
- ensure that the appropriate policies and procedures are put in place to meet the requirements of the Frameworks (or an alternative training programme);
- publicly report how these arrangements have been put into practice each year.

The Pensions Act 2004 and the Pension Regulator's Code of Practice

Section 248a of the Pensions Act 2004, as amended by The Public Service Pensions Act 2013 (PSPA13) requires Pension Board members to:

- be conversant with the rules of the scheme and any document recording policy about the administration of the scheme, and
- have knowledge and understanding of the law relating to pensions and any other matters which are prescribed in regulations.

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.
These requirements are incorporated and expanded on within the TPR Code of Practice which came into force on 1 April 2015. It is expected that guidance will also be issued by the Local Government Pension Scheme Advisory Board which will explain further how these requirements will relate to LGPS administering authorities.

Application to the London Borough of Tower Hamlets Pension Fund

Tower Hamlets Council recognises that effective financial administration, scheme governance and decision-making can only be achieved where those involved have the requisite knowledge and skills. Accordingly it fully supports the use of the CIPFA Knowledge and Skills Frameworks, and TPR's Code of Practice. Tower Hamlets Council adopts the principles contained in these publications in relation to the London Borough of Tower Hamlets Pension Fund, and this Training and Development Policy highlights how the Council will strive to achieve those principles through use of a Training Plan together with regular monitoring and reporting.

The London Borough of Tower Hamlets Pension Fund Training and Development Plan

Tower Hamlets Council recognises that attaining, and then maintaining, relevant knowledge and skills is a continual process for Pensions Committee members, Pension Board members and senior officers, and that training is a key element of this process. Tower Hamlets Council will develop a rolling Training Plan based on the following key elements:

1) **Individual Training Needs**: A training needs analysis will be developed for the main roles of Pensions Committee members, Pension Board members and senior officers customised appropriately to the key areas in which they should be proficient. Training will be required in relation to each of these areas as part of any induction and on an ongoing refresher basis.

2) **Hot Topic Training**: The Training Plan will be developed to ensure appropriately timed training is provided in relation to hot topic areas, such as a high risk area or a specific area where decisions need to be made. This training may be targeted at specific roles.

3) **General Awareness**: Pensions Committee members, Pension Board members and senior officers are expected to maintain a reasonable knowledge of ongoing developments and current issues, which will allow them to have a good level of general awareness of pension related matters appropriate for their roles and which may not be specific to the London Borough of Tower Hamlets Pension Fund.

Each of these training requirements will be focussed on the role of the individual i.e. a Pensions Committee member, a Pension Board member or the specific role of the officer.
The Pensions Committee agrees a training plan on an annual basis at the first meeting of the Municipal Year. The training plan is developed taking into consideration the needs of the Committee, the Board and officers to both enhance existing knowledge and skills and to develop new areas of understanding. This ensures that training is accessible to all Committee and Board members and key officers involved in the management of the Pension Fund.

Training will be delivered through a variety of methods including:

- In-house training days provided by officers and/or external providers
- Training as part of meetings (e.g. Pensions Committee) provided by officers and/or external advisers
- External training events
- Circulation of reading material
- Attendance at seminars and conferences offered by industry-wide bodies
- Attendance at meetings and events with the London Borough of Tower Hamlets Pension Fund's investment managers and advisors
- Links to on-line training
- Access to the London Borough of Tower Hamlets Pension Fund website where useful London Borough of Tower Hamlets Pension Fund specific material is available.

In addition London Borough of Tower Hamlets Pension Fund officers and advisers are available to answer any queries on an ongoing basis including providing access to materials from previous training events.

Initial Information and Induction Process

On joining the Pensions Committee, the Pension Board or the London Borough of Tower Hamlets Pension Fund Management Team, a new member or officer will be provided with the following documentation to assist in providing them with a basic understanding of London Borough of Tower Hamlets Pension Fund:

- The members' guide to the Local Government Pension Scheme (LGPS)
- The latest Actuarial Valuation report
- The Annual Report and Accounts, which incorporate:
    - The Funding Strategy Statement

  - The Governance Policy and Compliance Statement
  - The Statement of Investment Principles including the London Borough of Tower Hamlets Pension Fund's statement of compliance with the LGPS Myners Principles
  - The Communications Policy
  - The Administration Strategy
- The administering authority's Discretionary Policies
- The Training Policy

In addition, an individual training plan will be developed to assist each Pensions Committee member, Pension Board member or officer to achieve, within six months, their identified individual training requirements.

Monitoring Knowledge and Skills

To identify if Pensions Committee members, Pension Board members and senior officers are meeting the objectives of this policy we will:

1) Compare and report on attendance at training based on the following:

i. Individual Training Needs – ensuring refresher training on the key elements takes place for each individual at least once every three years.
ii. Hot Topic Training – attendance by at least 80% of the required Pensions Committee members, Pension Board members and senior officers at planned hot topic training sessions. This target may be focussed at a particular group of Pensions Committee members, Pension Board members or senior officers depending on the subject matter.
iii. General Awareness – each Pensions Committee member, Pension Board member or officer attending at least one day each year of general awareness training or events.
iv. Induction training – ensuring areas of identified individual training are completed within six months.

2) Consider whether the objectives have been met as part of the annual self-assessment carried out each year which is completed by all Pensions Committee members, Pension Board members and senior officers.

The key risks to the delivery of this Policy are outlined below:

i. Changes in Pensions Committee and/or Pension Board membership and/or senior officers' potentially diminishing knowledge and understanding.
ii. Poor attendance and/or a lack of engagement at training and/or formal meetings by Pensions Committee Members, Pension Board Members and/or other senior officers resulting in a poor standard of decision making and/or monitoring.
iii. Insufficient resources being available to deliver or arrange the required training.
iv. The quality of advice or training provided not being to an acceptable standard.

The Pensions Committee members, with the assistance of London Borough of Tower Hamlets senior officers and Pension Board members will monitor these and other key risks and consider how to respond to them.

Reporting

A report will be presented to the Pensions Committee on an annual basis setting out:

i. The training provided / attended in the previous year at an individual level
ii. Attendance at Pensions Committee and Pension Board meetings
iii. The results of the measurements identified above.

This information will also be included in the London Borough of Tower Hamlets Pension Fund's Annual Report and Accounts.

At each Pensions Committee and Pensions Board meeting, members will be provided with details of forthcoming seminars, conferences and other relevant training events as well as a summary of the events attended since the previous meeting.

Costs

All training costs related to this Training and Development Policy are met directly by the London Borough of Tower Hamlets Pension Fund.

Approval, Review and Consultation

This Training and Development Policy was originally approved at the London Borough of Tower Hamlets Pensions Committee meeting of September 2015 and amendments to incorporate the requirements of the CIPFA Local Pension Boards Framework would be approved on 9th March 2016. This Training and Development Policy was also adopted by the London Borough of Tower Hamlets Pension Board at its first meeting. It will be formally reviewed and updated at least every year or sooner if the training arrangements or other matters included within it worth re-evaluation.

Further Information

If you require further information about anything in or related to this Training and Development Policy, please contact:

Bola Tobun
Investment & Treasury Manager
London Borough of Tower Hamlets Pension Fund
London Borough of Tower Hamlets
Mulberry Place
5 Clove Crescent
London
E14 2BG
E-mail Bola.Tobun@towerhamlets.gov.uk
Telephone 020 7364 4733

LONDON BOROUGH OF TOWER HAMLETS

Administering Authority for
Tower Hamlets Pension Fund

Appendix 7

Procedure for Recording and Reporting Breaches of the Law

1. Introduction

1.1 This document sets out the procedures to be followed by certain persons involved with the Tower Hamlets Pension Fund, the Local Government Pension Scheme managed and administered by Tower Hamlets Council, in relation to reporting breaches of the law to the Pensions Regulator.

1.2 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 making investment or investment-related decisions.

1.3 This Procedure document applies, in the main, to:

- all members of the Tower Hamlets Pensions Committee and Board;
- all officers involved in the management of the Pension Fund ;
- personnel of the shared service pensions administrator providing day to day administration services to the Fund, and any professional advisers including auditors, actuaries, legal advisers and fund managers; and
- officers of employers participating in the Tower Hamlets Pension Fund who are responsible for pension matters.

2. Requirements

2.1 This section clarifies the full extent of the legal requirements and to whom they apply.

2.2 ***Pensions Act 2004***

Section 70 of the Pensions Act 2004 (the Act) imposes a requirement on the following persons:

- a trustee or manager of an occupational or personal pension scheme;
- a member of the pension board of a public service pension scheme;
- a person who is otherwise involved in the administration of such a scheme an occupational or personal pension scheme;
- the employer in relation to an occupational pension scheme;
- a professional adviser in relation to such a scheme; and
- a person who is otherwise involved in advising the trustees or managers of an occupational or personal pension scheme in relation to the scheme, to report a matter to The Pensions Regulator as soon as is reasonably practicable where that person has reasonable cause to believe that:

  (a) a legal duty relating to the administration of the scheme has not been or is not being complied with, and

  (b) the failure to comply is likely to be of material significance to The Pensions Regulator.

The Act states that a person can be subject to a civil penalty if he or she fails to comply with this requirement without a reasonable excuse. The duty to report breaches under the Act overrides any other duties the individuals listed above may have. However the duty to report does not override 'legal privilege'. This means that, generally, communications between a professional legal adviser and their client, or a person representing their client, in connection with legal advice being given to the client, do not have to be disclosed.

2.3 *The Pension Regulator's Code of Practice*

Practical guidance in relation to this legal requirement is included in The Pension Regulator's Code of Practice including in the following areas:

- implementing adequate procedures.
- judging whether a breach must be reported.
- submitting a report to The Pensions Regulator.
- whistleblowing protection and confidentiality.

2.4 *Application to the Tower Hamlets Pension Fund*

This procedure has been developed to reflect the guidance contained in The Pension Regulator's Code of Practice in relation to the Tower Hamlets Pension Fund and this document sets out how the Board will strive to achieve best practice through use of a formal reporting breaches procedure.

3 The Tower Hamlets Pension Fund Reporting Breaches Procedure

The following procedure details how individuals responsible for reporting and whistleblowing can identify, assess and report (or record if not reported) a breach of law relating to the Tower Hamlets Pension Fund. It aims to ensure individuals responsible are able to meet their legal obligations, avoid placing any reliance on others to report. The procedure will also assist in providing an early warning of possible malpractice and reduce risk.

3.1 *Clarification of the law*

Individuals may need to refer to regulations and guidance when considering whether or not to report a possible breach. Some of the key provisions are shown below:

- Section 70(1) and 70(2) of the Pensions Act 2004: www.legislation.gov.uk/ukpga/2004/35/contents
- Employment Rights Act 1996: www.legislation.gov.uk/ukpga/1996/18/contents
- Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 (Disclosure Regulations): www.legislation.gov.uk/uksi/2013/2734/contents/made
- Public Service Pension Schemes Act 2013: www.legislation.gov.uk/ukpga/2013/25/contents
- Local Government Pension Scheme Regulations (various): http://www.lgpsregs.org/timelineregs/Default.html (pre 2014 schemes) http://www.lgpsregs.org/index.php/regs-legislation (2014 scheme)

- The Pensions Regulator's Code of Practice: http://www.thepensionsregulator.gov.uk/codes/code-governance-administration-publicservice-pension-schemes.aspx
  In particular, individuals should refer to the section on 'Reporting breaches of the law', and for information about reporting late payments of employee or employer contributions, the section of the code on 'Maintaining contributions'.

Further guidance and assistance can be provided by the Council Monitoring Officer and the Corporate Director, Resources, provided that requesting this assistance will not result in alerting those responsible for any serious offence (where the breach is in relation to such an offence).

3.2 ***Clarification when a breach is suspected***
Individuals need to have reasonable cause to believe that a breach has occurred, not just a suspicion. Where a breach is suspected the individual should carry out further checks to confirm the breach has occurred. Where the individual does not know the facts or events, it will usually be appropriate to check with the Council Monitoring Officer and the Corporate Director, Resources, a member of the Pensions Committee or Pension Board or others who are able to explain what has happened. However there are some instances where it would not be appropriate to make further checks, for example, if the individual has become aware of theft, suspected fraud or another serious offence and they are also aware that by making further checks there is a risk of either alerting those involved or hampering the actions of the police or a regulatory authority. In these cases The Pensions Regulator should be contacted without delay.

3.3 ***Determining whether the breach is likely to be of material significance***
To decide whether a breach is likely to be of material significance an individual should consider the following, both separately and collectively:

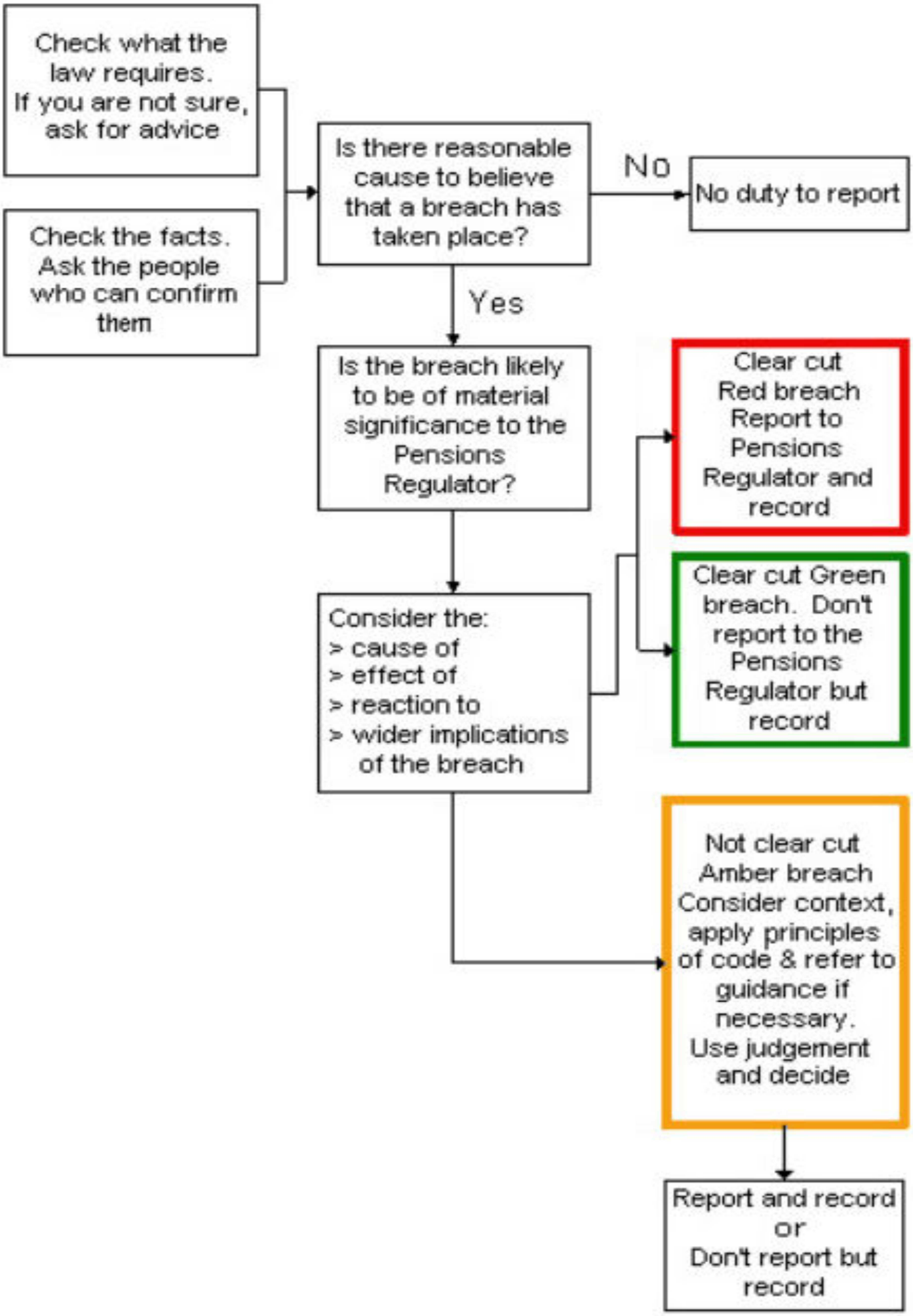
- cause of the breach (what made it happen);
- effect of the breach (the consequence(s) of the breach);
- reaction to the breach; and
- wider implications of the breach.

Further details on the above four considerations are provided in Appendix A to this procedure.

The individual should use the traffic light framework described in Appendix B to help assess the material significance of each breach and to formally support and document their decision.

3.4 A decision tree is provided below to show the process for deciding whether or not a breach has taken place and whether it is materially significant and therefore requires to be reported.

Decision-tree: deciding whether to report



3.5 ***Referral to a level of seniority for a decision to be made on whether to report***

Tower Hamlets Council has a designated Monitoring Officer to ensure the Council acts and operates within the law. They are considered to have appropriate experience to help investigate whether there is reasonable cause to believe a breach has occurred, to check the law and facts of the case, to maintain records of all breaches and to assist in any reporting to The Pensions Regulator, where appropriate. If breaches relate to late or incorrect payment of contributions or pension benefits, the matter should be highlighted to the Council Service Head of Finance & Procurement and the Corporate Director, Resources, at the earliest opportunity to ensure the matter is resolved as a matter of urgency. Individuals must bear in mind, however, that the involvement of the Monitoring Officer is to help clarify the potential reporter's thought process and to ensure this procedure is followed. The reporter remains responsible for the final decision as to whether a matter should be reported to The Pensions Regulator.

The matter should not be referred to any of these officers if doing so will alert any person responsible for a possible serious offence to the investigation (as highlighted in section 2). If that is the case, the individual should report the matter to The Pensions Regulator setting out the reasons for reporting, including any uncertainty – a telephone call to the Regulator before the submission may be appropriate, particularly in more serious breaches.

3.6 ***Dealing with complex cases***

The Council Service Head of Finance & Procurement and the Corporate Director, Resources, may be able to provide guidance on particularly complex cases. Information may also be available from national resources such as the Scheme Advisory Board or the LGPC Secretariat (part of the LG Group - http://www.lgpsregs.org/). If timescales allow, legal advice or other professional advice can be sought and the case can be discussed at the next Board meeting.

3.7. ***Timescales for reporting***

The Pensions Act and Pension Regulators Code require that if an individual decides to report a breach, the report must be made in writing as soon as reasonably practicable. Individuals should not rely on waiting for others to report and nor is it necessary for a reporter to gather all the evidence which The Pensions Regulator may require before taking action. A delay in reporting may exacerbate or increase the risk of the breach. The time taken to reach the judgements on "reasonable cause to believe" and on "material significance" should be consistent with the speed implied by 'as soon as reasonably practicable'. In particular, the time taken should reflect the seriousness of the suspected breach.

3.8 ***Early identification of very serious breaches***

In cases of immediate risk to the scheme, for instance, where there is any indication of dishonesty, The Pensions 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 Pensions Regulator to the breach.

3.9 ***Recording all breaches even if they are not reported***

The record of past breaches may be relevant in deciding whether to report a breach (for example it may reveal a systemic issue). Tower Hamlets Council will maintain a record of all breaches identified by individuals and reporters should therefore provide copies of reports to the Council Monitoring Officer and the Corporate Director, Resources. Records of unreported breaches should also be provided as soon as reasonably practicable and certainly no later than within 20 working days of the decision made not to report. These will be recorded alongside all reported breaches. The record of all breaches (reported or otherwise) will be included in the quarterly Monitoring Report at each Pension Committee, and this will also be shared with the Pension Board.

3.10 ***Reporting a breach***

Reports must be submitted in writing via The Pensions Regulator's online system at www.tpr.gov.uk/exchange, or by post, email or fax, and should be marked urgent if appropriate. If necessary, a written report can be preceded by a telephone call. Reporters should ensure they receive an acknowledgement for any report they send to The Pensions Regulator. The Pensions Regulator will acknowledge receipt of all reports within five working days and may contact reporters to request further information. Reporters will not usually be informed of any actions taken by The Pensions Regulator due to restrictions on the disclosure of information.

As a minimum, individuals reporting should provide:

- full scheme name (Tower Hamlets Pension Fund);
- description of breach(es);
- any relevant dates;
- name, position and contact details;
- role in connection to the scheme; and
- employer name or name of scheme manager (the latter is Tower Hamlets Council).

If possible, reporters should also indicate:

- the reason why the breach is thought to be of material significance to The Pensions Regulator;
- scheme address (provided at the end of this procedures document);
- scheme manager contact details (provided at the end of this procedures document);
- pension scheme registry number (PSR – 00330180RT); and
- whether the breach has been reported before.

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

3.11 ***Confidentiality***

If requested, The Pensions Regulator will do its best to protect a reporter's identity and will not disclose information except where it is lawfully required to do so. If an individual's employer decides not to report and the individual employed by them disagrees with this and decides to report a breach themselves, they may have protection under the Employment Rights Act 1996 if they make an individual report in good faith.

3.12 ***Reporting to Pensions Committee and Pensions Board***

A report will be presented to the Pensions Committee and the Pensions Board on a quarterly basis setting out:

- all breaches, including those reported to The Pensions Regulator and those unreported, with the associated dates;
- in relation to each breach, details of what action was taken and the result of any action (where not confidential);
- any future actions for the prevention of the breach in question being repeated; and
- highlighting new breaches which have arisen in the last year/since the previous meeting.

This information will also be provided upon request by any other individual or organisation (excluding sensitive/confidential cases or ongoing cases where discussion may influence the proceedings). An example of the information to be included in the quarterly reports is provided in Appendix C to this procedure.

3.13 ***Review***

This Reporting Breaches Procedure was originally developed in June 2016. It will be kept under review and updated as considered appropriate by the Corporate Director, Resources. It may be changed as a result of legal or regulatory changes, evolving best practice and ongoing review of the effectiveness of the procedure.

Further Information

If you require further information about reporting breaches or this procedure, please contact:

Bola Tobun - Investment & Treasury Manager
Email: Bola.Tobun@towerhamlets.gov.uk
Telephone: 020 7364 4733
Tower Hamlets Pension Fund
London Borough of Tower Hamlets, London E14 2BG

Designated officer contact details:
1) Service Head of Finance and Procurement – Neville Murton
Email: Neville.Murton@towerhamlets.gov.uk

2) Corporate Director, Resources – Zena Cooke
Email: Zena.Cooke@towerhamlets.gov.uk

3) Monitoring Officer – Melanie Clay
Email: Melanie.Clay@towerhamlets.gov.uk

Appendix A

Determining whether a breach is likely to be of material significance

To decide whether a breach is likely to be of material significance individuals should consider the following elements, both separately and collectively:

- cause of the breach (what made it happen);
- effect of the breach (the consequence(s) of the breach);
- reaction to the breach; and
- wider implications of the breach.

The cause of the breach

Examples of causes which are likely to be of concern to The Pensions Regulator are provided below:

- acting, or failing to act, in deliberate contravention of the law;
- dishonesty;
- incomplete or inaccurate advice;
- poor administration, i.e. failure to implement adequate administration procedures;
- poor governance; or
- slow or inappropriate decision-making practices.

When deciding whether a cause is likely to be of material significance individuals should also consider:

- whether the breach has been caused by an isolated incident such as a power outage, fire, flood or a genuine one-off mistake.
- whether there have been any other breaches (reported to The Pensions Regulator or not) which when taken together may become materially significant.

The effect of the breach

Examples of the possible effects (with possible causes) of breaches which are considered likely to be of material significance to The Pensions Regulator in the context of the LGPS are given below:

- Committee/Board members not having enough knowledge and understanding, resulting in pension boards not fulfilling their roles, the scheme not being properly governed and administered and/or scheme managers breaching other legal requirements.
- Conflicts of interest of Committee or Board members, resulting in them being prejudiced in the way in which they carry out their role and/or the ineffective governance and administration of the scheme and/or scheme managers breaching legal requirements.
- Poor internal controls, leading 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.
- Inaccurate or incomplete information about benefits and scheme information provided to members, resulting in members not being able to effectively plan or make decisions about their retirement.
- Poor member records held, resulting in member benefits being calculated incorrectly and/or not being paid to the right person at the right time.
- Misappropriation of assets, resulting in scheme assets not being safeguarded.
- Other breaches which result in the scheme being poorly governed, managed or administered.

The reaction to the breach

A breach is likely to be of concern and material significance to The Pensions 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.

The wider implications of the breach

Reporters should also consider the wider implications when deciding whether a breach must be reported. The breach is likely to be of material significance to The Pensions Regulator where the fact that a breach has occurred makes it more likely that further breaches will occur within the Fund or, if due to maladministration by a third party, further breaches will occur in other pension schemes.

Appendix B

Traffic light framework for deciding whether or not to report

It is recommended that those responsible for reporting use the traffic light framework when deciding whether to report to The Pensions Regulator. This is illustrated below:

RED

This where the cause, effect, reaction and wider implications of a breach, when considered together, are likely to be of material significance.

These must be reported to The Pensions Regulator.
Example: Several members' benefits have been calculated incorrectly. The errors have not been recognised and no action has been taken to identify and tackle the cause or to correct the errors.

AMBER

This where the cause, effect, reaction and wider implications of a breach, when considered together, may be of material significance. They might consist of several failures of administration that, although not significant in themselves, have a cumulative significance because steps have not been taken to put things right. You will need to exercise your own judgement to determine whether the breach is likely to be of material significance and should be reported.

Example: Several members' benefits have been calculated incorrectly. The errors have been corrected, with no financial detriment to the members. However the breach was caused by a system error which may have wider implications for other public service schemes using the same system.

GREEN

This where the cause, effect, reaction and wider implications of a breach, when considered together, are not likely to be of material significance. These should be recorded but do not need to be reported.

Example: A member's benefits have been calculated incorrectly. This was an isolated incident, which has been promptly identified and corrected, with no financial detriment to the member. Procedures have been put in place to mitigate against this happening again.

All breaches should be recorded even if the decision is not to report.

When using the traffic light framework individuals should consider the content of the red, amber and green sections for each of the cause, effect, reaction and wider implications of the breach, before you consider the four together. Some useful examples of this is framework is provided by The Pensions Regulator at the following link:http://www.thepensionsregulator.gov.uk/codes/code-related-report-reaches.aspx

Appendix C

Example Record of Breaches

Date	Category (e.g. administration, contributions, funding, investment, criminal activity)	Description and cause of breach	Possible effect of breach and wider implications	Reaction of relevant parties to breach	Reported / Not reported (with justification if not reported and dates)	Outcome of report and/or investigations	Outstanding actions

*New breaches since the previous meeting should be highlighted

LONDON BOROUGH OF TOWER HAMLETS

Administering Authority for
Tower Hamlets Pension Fund

Appendix 8
CONFLICTS OF INTEREST POLICY

June 2016

CONFLICTS OF INTEREST POLICY

Introduction

Conflicts of interest have always existed for those with LGPS administering authority responsibilities as well as for advisers to LGPS funds. This simply reflects the fact that many of those managing or advising LGPS funds will have a variety of other roles and responsibilities, for example as a member of the scheme, as an elected member of an employer participating in the LGPS or as an adviser to more than one LGPS administering authority. Further any of those persons may have an individual personal, business or other interest which might conflict, or be perceived to conflict, with their role managing or advising LGPS funds.

It is generally accepted that LGPS administering authorities have both fiduciary and public law duties to act in the best interest of both the scheme beneficiaries and participating employers. This, however, does not preclude those involved in the management of the fund from having other roles or responsibilities which may result in an actual or potential conflict of interest. Accordingly, it is good practice to document within a policy, such as this, how any such conflicts or potential conflicts are to be managed.

This is the Conflicts of Interest Policy of the Tower Hamlets Pension Fund, which is managed by London Borough of Tower Hamlets. The Policy details how actual and potential conflicts of interest are identified and managed by those involved in the management and governance of the Tower Hamlets Pension Fund whether directly or in an advisory capacity.

This Conflicts of Interest Policy is established to guide the Pensions Committee members, Pension Board members, officers and advisers. Along with other constitutional documents, including the various Codes of Conduct, it aims to ensure that those individuals do not act improperly or create a perception that they may have acted improperly. It is an aid to good governance, encouraging transparency and minimising the risk of any matter prejudicing decision making or management of the Fund otherwise.

In relation to the governance of the Fund, the Administering Authority's objectives are to:

- Act in the best interests of the Fund's members and employers
- Have robust governance arrangements in place, to facilitate informed decision making, supported by appropriate advice, policies and strategies
- Ensure the Pension Fund is managed and its services delivered by people who have the appropriate knowledge and expertise
- Act with integrity and be accountable to stakeholders for all decisions, ensuring they are robust and well based
- Understand and monitor risk
- Strive to ensure compliance with the appropriate legislation and statutory guidance, and to act in the spirit of other relevant guidelines and best practice guidance
- Clearly articulate its objectives and how it intends to achieve those objectives through business planning, and continually measure and monitor success

The identification and management of potential and actual conflicts of interest is integral to the Administering Authority achieving its governance objectives.

To whom this Policy Applies

This Conflicts of Interest Policy applies to all members of the Pensions Committee and the Pension Board, including scheme member and employer representatives, whether voting members or not. It applies to all managers in the management of London Borough of Tower Hamlets Pension Fund, the Chief Finance Officer (Section 151 Officer), Corporate Directors, and the Service Heads (from here on in collectively referred to as the senior officers of the Fund).

The Pension Manager/Investment Manager will monitor potential conflicts for less senior officers involved in the daily management of the Pension Fund and highlight this Policy to them as he/she considers appropriate.

This Policy and the issue of conflicts of interest in general must be considered in light of each individual's role, whether this is a management, advisory or assisting role.

The Policy also applies to all advisers and suppliers to the Fund, whether advising the Pension Board, Pensions Committee or Fund officers.

In this Policy, reference to advisers includes all advisers, suppliers and other parties providing advice and services to the Administering Authority in relation to pension fund matters. This includes but is not limited to actuaries, investment consultants, independent advisers, benefits consultants, third party administrators, fund managers, lawyers, custodians and AVC providers. Where an advisory appointment is with a firm rather than an individual, reference to "advisers" is to the lead adviser(s) responsible for the delivery of advice and services to the Administering Authority rather than the firm as a whole.

In accepting any role covered by this Policy, those individuals agree that they must:

- acknowledge any potential conflict of interest they may have;
- be open with the Administering Authority on any conflicts of interest they may have;
- adopt practical solutions to managing those conflicts; and
- plan ahead and agree with the Administering Authority how they will manage any conflicts of interest which arise in future.

The procedures outlined later in this Policy provide a framework for each individual to meet these requirements.

Legislative and related context

The overriding requirements in relation to the management of potential or actual conflicts of interest for those involved in LGPS funds are contained in various elements of legislation and guidance. These are considered further below.

The Public Service Pensions Act 2013
Section 5 of this Act requires that the scheme manager (in the case of the LGPS, this is the administering authority) must be satisfied that a Pension Board member does not have a conflict of interest at the point of appointment and from time to time thereafter. It also requires Pension Board members (or nominated members) to provide reasonable information to the scheme manager for this purpose.

The Act defines a conflict of interest as “a financial or other interest which is likely to prejudice the person’s exercise of functions as a member of the board (but does not include a financial or other interest arising merely by virtue of membership of the scheme or any connected scheme).”

Further, the Act requires that scheme managers must have regard to any such guidance that the national scheme advisory board issue (see below).

The Local Government Pension Scheme Regulations 2013

Regulation 108 of these Regulations applies the requirements of the Public Service Pensions Act (as outlined above) to the LGPS, placing a duty on each Administering Authority to satisfy itself that Pension Board members do not have conflicts of interest on appointment or whilst they are members of the board. It also requires those pension board members to provide reasonable information to the administering authority in this regard.

Regulation 109 states that each Administering Authority must have regard to guidance issued by the Secretary of State in relation to Pension Boards. Further, regulation 110 provides that the national scheme advisory board has a function of providing advice to Administering Authorities and Pension Boards. At the point of writing this Policy, the shadow LGPS national scheme advisory board has issued guidance relating to the creation of Pension Boards including a section on conflicts of interest. It is expected that this guidance will be adopted by the scheme advisory board when it is created by statute and possibly also by the Secretary of State. This Conflicts of Interest Policy has been developed having regard to that guidance.

The Pensions Act 2004

The Public Service Pensions Act 2013 also added a number of provisions to the Pensions Act 2004 related to the governance of public service pension schemes and, in particular, conflicts of interest.

Section 90A requires the Pensions Regulator to issue a code of practice relating to conflicts of interest for pension board members. The Pensions Regulator has issued such a code and this Conflicts of Interest Policy has been developed having regard to that code.

Further, under section 13, the Pensions Regulator can issue an improvement notice (i.e. a notice requiring steps to be taken to rectify a situation) where it is considered that the requirements relating to conflicts of interest for Pension Board members are not being adhered to.

Local Government Act 2000

All members and co-opted members of the Tower Hamlets Pensions Committee are required by the Local Government Act 2000 to abide by Flintshire's Members' Code of Conduct. Part 3 of that Code contains provisions relating to personal interests, personal and prejudicial interests, their disclosure and limitations on members' participation where they have any such interest.

The Public Services Ombudsman for Wales' Ten Guiding Principles

The Local Government Act 2000 empowered the National Assembly to issue principles to which local authority elected members must have regard in undertaking their role as a member. These principles draw on the 7 Principles of Public Life which were set out in the Nolan Report "Standards of Conduct in Local Government in England, Scotland and Wales". Three more were added to these; a duty to uphold the law, proper stewardship of the Council's resources and equality and respect for others.

The current principles were set out in a statutory instrument and are detailed below. Many of the principles are integral to the successful implementation of this Policy.

CODE OF CONDUCT & CONFLICT OF INTEREST POLICY

1. **Code of conduct**

1.1 As members of a publicly funded body with a responsibility to discharge public business, members of the Tower Hamlets Pension Board should have the highest standards of conduct.

1.2 Pension Board members should have regard to the Seven Principles of Public life:
- Selflessness
- Integrity
- Objectivity
- Accountability
- Openness
- Honesty
- Leadership

1.3 All Tower Hamlets Pension Board members must:
- Act solely in the public interest and should never improperly confer an advantage or disadvantage on any person or act to gain financial or other material benefits for yourself, your family, a friend or close associate.

- Not place yourself under a financial or other obligation to outside individuals or organisations that might seek to influence you in the performance of your official duties.

- Make all choices on merit and must be impartial and seen to be impartial, when carrying out your public duties.

- Co-operate fully with whatever scrutiny is appropriate to your role.

- Not, without proper authority, reveal any confidential and sensitive information that is provided to you, such as personal information about someone, or commercially sensitive information which, if disclosed, might harm the commercial interests of the Council or another person or organisation.

- Ensure when using or authorising the use by others of the resources of the authority that such resources are not used improperly for political purposes (including party political purposes) and you must have regard to any applicable Local Authority Code of Publicity made under the Local Government Act 1986.

- Promote and support high standards of conduct when serving in your public post, in particular as characterised by the above requirements, by leadership and example.

- Sign the Conflict of Interest Declaration and declare any further potential conflicts of interest that may arise once appointed as a member.

- Comply with the Tower Hamlets Pension Fund Code in addition to all other existing Codes of Conduct or Protocols (e.g. The Member Code of Conduct).

2. **Conflict of interest**

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

2.2 A conflict of interest exists where a decision on a matter might reasonably be regarded as affecting (to a greater extent than other persons who may be affected by the decision) the well-being or financial position of the Councillor, a relative or a friend or

- the employment or business carried out by those persons, or in which they might be investors (above a certain level)
- any of the bodies with which the decision maker is associated, and which decision maker will have registered in the appropriate register of interests.

It does not need to be shown that a conflict of interest actually exists. It is sufficient if it appears to a fair and informed observer that there was a real possibility of conflict.

..

2.3 Examples of potential conflicts of interest, not only for the Board but also for all those involved in managing the Pension Fund, are listed at appendix 1.

2.4 All prospective Pension Board members are required to complete the Tower Hamlets Pension Fund Conflict of interest declaration before they are appointed to the Pension Board, attached at appendix 2.

2.5 All appointments to the Pension Board should be kept under review by the Corporate Director, Resources.

2.5 It is the duty of any appointed Pension Board member to declare any potential conflict of interest. This declaration should be made to the Chair of the Pension Board in the first instance or to the Scheme Manager, and recorded in a register of interests.

2.7 The Pension Board shall identify and monitor any potential conflict of interests in a register of interests (attached at appendix 3). The register of interests should be circulated to the Tower Hamlets Pension Board and Scheme Manager for review and publication.

2.8 If the Pension Board suspects any conflict of interest it should report its concerns to the Scheme Manager.

2.9 When seeking to prevent a potential conflict of interest becoming detrimental to the conduct and decisions of the Pension Board, the Tower Hamlets Pension Board must consider obtaining legal advice when assessing its course of action and response. The Tower Hamlets Pension Board should consult the Monitoring Officer or the Service Head, Legal Services in the first instance.

2.10 Education on identifying and dealing with conflicts of interest will be included as part of the training requirement in the Knowledge and Understanding policy.

3. Operational procedure for officers, Pensions Committee members and Pension Board members

3.1 The following procedures must be followed by all individuals to whom this policy applies.

What is required	How this will be done
Step 1 - Initial identification of interests which do or could give rise to a conflict	On appointment to their role or on the commencement of this Policy if later, all individuals will be provided with a copy of this Policy and be required to complete a Declaration of Interest the same or similar to that included in Appendix 2. This is in addition to the requirement to register disclosable pecuniary interests and other registerable interests. The information contained in these declarations will be collated into the Pension Fund Register of conflicts of interest in a format the same or similar to that included in Appendix 3.
Step 2 - Ongoing notification and management of potential or actual conflicts of interest	At the commencement of any Pensions Committee, Pension Board or other formal meeting where pension fund matters are to be discussed, the Chairman will ask all those present who are covered by this Policy to declare any new potential conflicts. These will be recorded in the Fund's Register of conflicts of interest. In addition, the latest version of the Register will be made available by the Governance Officer to the Chairman of every meeting prior to that meeting. At Tower Hamlets Pensions Committee meetings there will also, at the start of the meeting, be an agenda item for Members to declare any interests under the Members' Code in relation to any items on that agenda. Any individual, who considers that they or another individual has a potential or actual conflict of interest, as defined by this Policy, which relates to an item of business at a meeting, must advise the Chairman and the Governance Officer prior to the meeting, where possible, or state this clearly at the meeting at the earliest possible opportunity. The Chairman, in consultation with the Officers, should then decide whether the conflicted or potentially conflicted individual needs to leave the meeting during the discussion on the relevant matter or to withdraw from voting on the matter. If such a conflict is identified outside of a meeting the notification must be made to the Governance Officer and where it relates to the business of any meeting, also to the Chairman of that meeting. The Officers, in consultation with the Chairman where relevant, will consider any necessary action to manage the potential or actual conflict. Where information relating to any potential or actual conflict has been provided, the Pensions Manager/Investment & Treasury Manager may seek such professional advice as he or she thinks fit (such as legal advice from the Monitoring Officer) on to how to address any identified conflicts. Any such potential or actual conflicts of interest and the action taken must be recorded on the Fund's Register of conflicts of interest.
Step 3 - Periodic review of potential and actual conflicts	At least once every 12 months, the Officers will provide to all individuals to whom this Policy applies a copy of the Fund's Register of conflicts of interest. All individuals will complete a new Declaration of Interest (see Appendix 2) confirming that their information contained in the Register is correct or highlighting any changes that need to be made to the declaration. Following this exercise, the updated Register will then be circulated by the Officers to all individuals to whom it relates.

4. Operational procedure for advisers

4.1 All of the key advisers are expected to have their own policies on how conflicts of interest will be managed in their relationships with their clients, and these should have been shared with London Borough of Tower Hamlets.

4.2 Although this Policy applies to all advisers, the operational procedures outlined in steps 1 and 3 above relating to completing ongoing declarations are not expected to apply to advisers. Instead all advisers must:

- be provided with a copy of this Policy on appointment and whenever it is updated
- adhere to the principles of this Policy
- provide, on request, information to the Pensions Manager/Investment & Treasury Manager in relation to how they will manage and monitor actual or potential conflicts of interests relating to the provision of advice or services to London Borough of Tower Hamlets
- notify the Pensions Manager/Investment & Treasury Manager immediately should a potential or actual conflict of interest arise.

4.3 All potential or actual conflicts notified by advisers will be recorded in the Fund's Register of conflicts of interest.

4.4 London Borough of Tower Hamlets will encourage a culture of openness and transparency and will encourage individuals to be vigilant, have a clear understanding of their role and the circumstances in which they may have a conflict of interest, and of how potential conflicts should be managed.

4.5 London Borough of Tower Hamlets will evaluate the nature of any dual interests or responsibilities that are highlighted and assess the impact on pension fund operations and good governance were an actual conflict of interest to materialise.

4.6 Ways in which conflicts of interest may be managed include:

- the individual concerned abstaining from discussion, decision-making or providing advice relating to the relevant issue
- the individual being excluded from the meeting(s) and any related correspondence or material in connection with the relevant issue (for example, a report for a Pensions Committee meeting)
- a working group or sub-committee being established, excluding the individual concerned, to consider the matter outside of the formal meeting (where the terms of reference permit this to happen)

4.7 Provided that the Administering Authority, (having taken any professional advice deemed to be required) is satisfied that the method of management is satisfactory, London Borough of Tower Hamlets shall endeavour to avoid the need for an individual to have to resign due to a conflict of interest. However, where the conflict is considered to be so fundamental that it cannot be effectively managed, or where a Pension Board member has an actual conflict of interest as defined in the Public Service Pensions Act 2013, the individual will be required to resign from the Committee, Board or appointment.

4.8 *Minor Gifts*
For the purposes of this Policy, gifts such as t-shirts, pens, trade show bags and other promotional items (subject to a notional maximum value of £10 per item and an overall maximum value of £20 from an individual company per event) obtained at events such as conferences, training events, seminars, and trade shows, that are offered equally to all members of the public attending the event do not need to be declared. Pensions Committee members should, however, be aware that they may be subject to lower limits and a separate notification procedure in the London Borough of Tower Hamlets Members' Code of Conduct.

5. Monitoring and Reporting

5.1 The Fund's Register of conflicts of interest may be viewed by any interested party at any point in time. It will be made available on request by the Governance Officer for the Fund. In addition, it will be published in the annual report and accounts

5.2 In order to identify whether the objectives of this Policy are being met the Administering Authority will:

- Review the Register of conflicts of interest on an annual basis and consider whether there have been any potential or actual conflicts of interest that were not declared at the earliest opportunity
- Provide its findings to the Administering Authority's Independent Adviser and ask him or her to include comment on the management of conflicts of interest in his or her annual report on the governance of the Fund each year.

6. Key Risks

6.1 The key risks to the delivery of this Policy are outlined below. All of these could result in an actual conflict of interest arising and not being properly managed. The Pensions Manager/Investment & Treasury Manager will monitor these and other key risks and consider how to respond to them.

- Insufficient training or poor understanding in relation to individuals' roles on pension fund matters
- Insufficient training or failure to communicate the requirements of this Policy
- Absence of the individual nominated to manage the operational aspects of this Policy and no one deputising, or failure of that individual to carry out the operational aspects in accordance with this Policy
- Failure by a chairperson to take appropriate action when a conflict is highlighted at a meeting.

7. Costs

7.1 All costs related to the operation and implementation of this Policy will be met directly by Tower Hamlets Pension Fund. However, no payments will be made to any individuals in relation to any time spent or expenses incurred in the disclosure or management of any potential or actual conflicts of interest under this Policy.

8. Approval, Review and Consultation

8.1 This Conflicts of Interest Policy is to be approved using delegated responsibilities on 30 June 2016. It will be formally reviewed and updated at least every three years or sooner if the conflict management arrangements or other matters included within it merit reconsideration, including if there are any changes to the LGPS or other relevant Regulations or Guidance which need to be taken into account.

Further Information

If you require further information about anything in or related to this Conflicts of Interest Policy, please contact:

Bola Tobun,
Tower Hamlets Pension Fund Manager,
London Borough of Tower Hamlets
E-mail - Bola.Tobun@towerhamlets.gov.uk
Telephone – 020 7364 4733

Appendix 1

Examples of Potential Conflicts of Interest

a) An elected member on the Pension Committee is asked to provide views on a funding strategy which could result in an increase in the employer contributions required from the employer he or she represents.

b) A member of the Pension Committee is on the board of a Fund Manager that the Committee is considering appointing.

c) An officer of the Fund or member of the Pension Committee accepts a dinner invitation from a Fund Manager who has submitted a bid as part of a tender process.

d) An employer representative on the Pension Board is employed by a company to which the administering authority has outsourced its pension administration services and the Local Pension Board is reviewing the standards of service provided by that company.

e) The person appointed to consider internal disputes is asked to review a case relating to a close friend or relative.

f) An officer of the Fund is asked to provide guidance to the Local Pension Board on the background to an item considered at the Pension Committee. This could be a potential conflict as the officer could consciously or sub-consciously avoid providing full details, resulting in the Board not having full information and not being able to provide a complete view on the appropriateness or otherwise of that Pension Committee item.

g) The administering authority is considering buying its own payroll system for paying pensioners, rather than using the payroll system used for all employees of the Council. The Executive Director of Finance and Public Protection, who has responsibility for the Council budget, is expected to approve the report to go to the Pension Committee, which, if agreed, would result in a material reduction in the recharges to the Council from the Fund.

h) Officers of the Fund are asked to provide a report to the Pension Board or Pension Committee on whether the administration services should be outsourced which, if it were to happen, could result in a change of employer or job insecurity for the officers.

i) An employer representative employed by the administering authority and appointed to the Pension Board to represent employers generally could be conflicted if he or she only acts 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 he or she only acts in the interests of their union and union membership, rather than all scheme members.

j) A Fund adviser is party to the development of a strategy which could result in additional work for their firm, for example, delegated consulting of fund monies or providing assistance with monitoring the covenant of employers.

k) An employer representative has access to information by virtue of his or her employment, which could influence or inform the considerations or decisions of the Pension Committee or Local Pension Board. He or she has to consider whether to share this information 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.

Appendix 2

Declaration of Interests relating to the management of Tower Hamlets Pension Fund administered by London Borough of Tower Hamlets

Tick as appropriate

I, [insert full name], am:

- an officer involved in the management ☐
- Pensions Committee Member ☐
- Pension Board Member ☐

of Tower Hamlets Pension Fund and I set out below under the appropriate headings my interests, which I am required to declare under Tower Hamlets Pension Fund Conflicts of Interest Policy. I have put "none" where I have no such interests under any heading.

Responsibilities or other interests that could result in a conflict of interest (please list and continue overleaf if necessary):

A) Relating to me

B) Relating to family members or close colleagues

Undertaking:

I declare that I understand my responsibilities under the Tower Hamlets Pension Fund Conflicts of Interest Policy. I undertake to notify the Pensions Manager/Investment & Treasury Manager of any changes in the information set out above.

Signed ____ Date ____________________

Name (CAPITAL LETTERS) ____

Appendix 3

Tower Hamlets Pension Fund - Register of Potential and Actual Conflicts of Interest

All reported conflicts of interest will be recorded in the minutes and a register of conflicts will be maintained and reviewed annually by London Borough of Tower Hamlets, the Administering Authority.

Date Identified	Name of Person	Role of Person	Details of conflict	Actual or potential conflict	How notified(1)	Action taken(2)	Follow up required	Date resolved

(1) E.g. verbal declaration at meeting, written conflicts declaration, etc.
(2) E.g. withdrawing from a decision making process, left meeting

LONDON BOROUGH OF TOWER HAMLETS

Administering Authority for
Tower Hamlets Pension Fund

PENSIONS BOARD
ANNUAL REPORT FOR 2015/16

ANNUAL REPORT OF THE PENSIONS BOARD 2015-16

Purpose of the Report
To provide an update on the work undertaken by the Local Pensions Board during 2015-2016 and to meet the legislative requirement to produce an annual report.

Constitution, Representation Meetings and Attendance
The Board was constituted under the Public Service Pensions Act 2013 and held its first meeting on the 28 July 2015 before the recommended Scheme Advisory Board (SAB) deadline of 31 July 2015.
The board consists of three representatives of the scheme employers, three representing of the scheme members and an Independent Chair.

Membership

Tower Hamlets Pension Board Membership 2015 /16

Member Representatives	Designation	Employer Representatives	Designation
David Thompson	Pensioners Representative	Cllr. David Chesterton	Elected Member
John Gray	Admitted Bodies Representative	Minesh Jani	Administering Authority
Stephen Stratton	Active Members Representative	Andrew Crompton	Admitted Bodies

The Independent Chair for the board – John Jones (started March 2016)

The Corporate Director, Resources wishes to thank the Board members for their work over the last year.

The Board met on four occasions during the year ending 31 March 2016.

1) 28 July 2015
2) 01 October 2015
3) 20 November 2015
4) 07 March 2016

Functions and Operation of the Board
The two primary functions of a Local Pension Board are to assist the Administering Authority to:

• Ensure effective and efficient governance and administration of the LGPS
• Ensure compliance with relevant laws and regulation

It therefore has a monitor/assist /review purpose, rather than being a decision making body. It could be seen as being a critical friend. As such, the general approach of the Board is to seek assurances with evidence from the Fund that it is meeting its objectives set out above.
The Board is not a Committee of the Council, but is established under the Public Service Pensions Act 2013. The Board operates under Terms of Reference which were approved at inception.

The establishment and initial meetings of the Board coincided with the period of greatest pressure on officers in the recent history of the LGPS, with the Administering Authority having to respond to the DCLG by 19 February 2016 on the critical consultation documents on both the proposed pooling of LGPS investments, and also on revised Investment and Management of Funds Regulations. These developments placed a relatively higher level of workload on the Fund during the first year of the board's existence.

The Board recognises the need to prioritise and differentiates in its agenda between items for detailed discussion, and those for awareness or noting, and prioritises its time budget accordingly.

Costs

There is a financial budget for the Board of £12.5k. The cost incurred in the creation and implementation of the Board has been minimal, having been incorporated within existing officer workloads. No independent external reviews were commissioned over the course of the year. There was some spend incurred on external training which was contained within the total training budget of £6k.

The costs of running the Board are borne by the Pension Fund as part of its overall budget. The costs have in fact minimal as forming and running the board have been incorporated within existing workloads.

The Board has not commissioned any external consultants for work, however there has been some expenditure on training as follows:

- LGPS Induction Session (Roles & Responsibilities) – Internal
- Half day external training by AXA on Investments, LGPS and the role and purpose of the Board
- Half day triennial valuation – internal training and update provided by the Fund's Actuary.
- Full one day training on custody and performance monitoring by State street
- Full one day external training by Aon on LGPS, valuation and Investments

Detailed Work of the Board:

Scheme documents

Board members were provided with the range of scheme policies which were incorporated in the schemes Annual Report. The Board expects to take forward a detailed review of these policies going forward.

Pensions Committee

The Pensions board has also focused heavily on the attendance of meeting and training of the committee and this has been of great concern to them, therefore there has been monitoring of attendance at their quarterly meetings.
There is an alignment of the Committee and Board agenda's in order to demonstrate the board active oversight of what the Committee is to consider and what the Committee then determined is in operation. The board care so much and spent a lot of time discussing the their input and also trying to determine what contribution a Pension Board should make so that they complement and not duplicate the Committee.
Pensions Board key/action points from their meeting is a standing item on the committee's agenda.

Risk management and register

The board also recognised that there are benefits in reviewing the risk register that is exclusive to the Fund. This is a project in development as officers are preparing risk management policies and parameters for the fund.

Pensions Regulator

Whist it is generally felt that the LGPS is comparatively well governed, nevertheless the Pensions Regulator is examining the Scheme on an ongoing basis and has, for example, highlighted delays by administering authorities in producing Annual Benefit Statements. A TPR compliance checklist has been developed and this will be review by the board semi-annually.

Reporting and Recording Breaches

The Board and its members, as with other players, all have a responsibility to report breaches of law to the Pensions Regulator. A procedure manual and a policy document on reporting and recording breaches have been developed with a quarterly update template.

Scheme Advisory Board (SAB)

The SAB is responsible for providing advice to the responsible authority i.e. the (secretary of state), at the authority's request, on the desirability of changes to the scheme.
The SAB has a two way role: giving advice both upwards to the DCLG and down to individual funds. There is expected to be a two way flow of information between the SAB and individual Funds and it is the aim of the Tower Hamlets Pension Board to be seen as an example of good practice.
The SAB examined the establishment of Local Pension Boards and Tower Hamlets Pension Fund complied with the requirements and timescales.

Training

Each Board member has to be conversant with the details of the Scheme, which translates as having a good working knowledge. The fund has offered a number of training opportunities for Board members where possible. External training was provided for Board members in collaboration with other funds on the role and purpose of the Board, Actuarial valuation.
Assessment of training needs, and how they are met, will be a standing item on the board's agenda going forward. Both formal and informal (cascade) training will be considered.
All members are encouraged to complete self-study and information on the pension regulator's tool-kit has been provided to Board members.

Work plan

The agenda for the first three meetings emerged naturally as the Board scanned the statutory documents, reports to the Pensions Panel, and reports, reviews and compliance requirements of both the Scheme Advisory Board and the Pensions Regulator.
In considering the work of the Board going forward to ensure the continued good governance of the scheme, the following key areas have been highlighted and members will prioritise reviews based on information collected from quarterly compliance updates.

- Triennial Valuation March 2016
- Meeting legislative requirement on pooling
- Improving data quality
- Ensuring strength in employer covenants
- Admission and Termination of other employers to the scheme
- Accounts
- Administration
- Audit and Risk Management
- Governance
- Training

There will be a degree of flexibility to allow for any additional reviews by either the Scheme Advisory Board or the Pensions Regulator.

Attached to this report are:
Appendix 1 is the Pensions Board Members Attendance for 2015/16 and Appendix 2 is the Pensions Committee Members Attendance for 2015/16.

Appendix 1

Pension Board Members Attendance 2015/16

	28th July		1st Oct	14th Sept	20th Nov	10th Dec	7th March	18th March
	Meeting	Training	Meeting	Training	Meeting	Training	Meeting	Training
John Jones (Chair)	N/A	N/A	N/A	N/A	N/A	N/A	P	N/A
David Thompson (Vice Chair)	A	A	P	P	P	P	P	P
Councillor Dave Chesterton	P	P	P	P	P	P	P	P
Minesh Jani	P	P	P	P	P	P	P	P
Andrew Compton	P	P	P	P	P	P	A	P
Steven Stratton	N/A	N/A	N/A	N/A	P	P	A	P
John Gray	P	P	N/A	N/A	A	A	A	P

P=Present
A=Absent
N/A - Attendance not required

Appendix 2

Pension Committee Members Attendance 2015/16

	23rd July		17th September		25th November		9th March	
	Meeting	Training	Meeting	Training	Meeting	Training	Meeting	Training
Councillor Andrew Cregan (Chair)	P	P	P	P	P	P	P	P
Councillor Clare Harrisson (Vice Chair)	P	P	P	P	P	P	P	P
Councillor Suluk Ahmed	A	A	P	P	A	A	A	A
Councillor Harun Miah	A	A	A	A	A	A	A	A
Councillor Mohammed Mufti Miah	P	P	A	A	A	A	A	A
Councillor Abdul Mukit MBE	A	A	A	A	P	P	A	A
Councillor Candida Ronald	P	P	A	A	P	P	P	P
Co-Opted Members								
John Gray	A	A	P	P	N/A	N/A	N/A	N/A
Kehinde Akintunde	N/A	N/A	N/A	N/A	P	P	P	P
Tony Childs	N/A	N/A	N/A	N/A	A	A	A	A

P=Present
A=Absent
N/A - Attendance not required

Training

LGPS Governance
Roles & Responsibilities
Fixed Income
Liability Driven Awareness
Performance Monitoring
TPR code of Practice

KPMG

External Audit Report 2015/16

London Borough of Tower Hamlets

—

DRAFT - 26 September 2016

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. Public Sector Audit Appointments 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 (and the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited), who will try to resolve your complaint. 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 3H.

Section one: Introduction

Introduction

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This document summarises:

- **The key issues identified during our audit of the financial statements for the year ended 31 March 2016 for both the Authority and its pension fund; and**
- **Our assessment of the Authority's arrangements to secure value for money.**

We note that some work is still ongoing and accordingly this draft report will be updated to produce a final version at the point the financial statements are signed.

Scope of this report

This report summarises the key findings arising from:

- Our audit work at the London Borough of Tower Hamlets ('the Authority') in relation to the Authority's 2015/16 financial statements and those of the Local Government Pension Scheme it administers ('the Fund'); and
- The work to support our 2015/16 conclusion on the Authority's arrangements to secure economy, efficiency and effectiveness in its use of resources ('VFM conclusion').

Financial statements

Our *External Audit Plan 2015/16*, presented to you in June 2016 2015, set out the four stages of our financial statements audit process.

Planning → Control Evaluation → Substantive Procedures → Completion

This report focuses on the third stage of the process: substantive procedures. Our on site work for this took place during August and September 2016.

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

VFM Conclusion

Our External Audit Plan 2015/16 explained our risk-based approach to VFM work. We have now completed the work to support our 2015/16 VFM conclusion. This included:

- Assessing the potential VFM risks and identifying the residual audit risks for our VFM conclusion;
- Considering the results of any relevant work by the Authority and other inspectorates and review agencies in relation to these risk areas;
- Continuing our consideration of the Authority's actions to address issues raised by the 'Best Value Inspection of London Borough of Tower Hamlets' report (the BV Inspection report) produced by PricewaterhouseCoopers LLP (PwC);
- consideration of other matters brought to our attention by the Tower Hamlets Commissioners; and the Department for Communities and Local Government (DCLG); and
- following up on relevant issues included in our *ISA 260 Report 2014/15* presented to the Audit Committee in March 2016.

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 2015/16 financial statements of the Authority and the fund.
- Section 4 outlines our key findings from our work on the VFM conclusion.

Acknowledgements

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

Section two: Headlines

Headlines

In relation to the Authority's and Fund's financial statements we anticipate issuing an unqualified audit opinion subject to the satisfactory resolution of our outstanding work.

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This table summarises the headline messages. Sections three and four of this report provide further details on each area.

Proposed audit opinion	We have some further work to be complete relating to the financial statements audit (see 'Completion' later in this Section for details). On the basis the remaining the work and outstanding queries are resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority's financial statements. We will also report that your Annual Governance Statement complies with guidance issued by CIPFA/SOLACE in June 2007. We also anticipate issuing an unqualified audit opinion in relation to the Fund's financial statements, as contained both in the Authority's Statement of Accounts and the Pension Fund Annual Report, subject to completing journals testing and our review and completion procedures being concluded satisfactorily. We note that we have not yet issued our opinion on the 2014/15 financial statements yet. This is due to the objection relating to the Authority's Lender Option Borrower Option loans which raises questions about whether the loans were taken out lawfully and the objector is asking that we apply to court that the LOBO loan borrowing is unlawful. The 2014/15 financial statements will need to be signed prior to the 2015/16 financial statements being signed. See 2014/15 section below.
Audit adjustments	We are pleased to report that our audit of the financial statements did not identify any significant adjustments. The Authority made a number of minor adjustments, all of which were of a presentational nature. There have been no changes that affect the General Fund or HRA balances or the Authority's net worth as at 31 March 2016.
Accounts production and audit process	We received complete draft accounts by 30 June 2016 in accordance with the DCLG deadline. The accounting policies, accounting estimates and financial statement disclosures are in line with the requirements of the Code. The Authority has implemented two out of the three recommendations in our *ISA 260 Report 2014/15* relating to the financial statements. At this stage we have not drafted and agreed with officers recommendations in relation to the current year, these will be reported to the Audit Committee at a subsequent meeting. We anticipate raising some recommendations in relation to grants. The Authority has good processes in place for the production of the accounts and good quality supporting working papers. Officers dealt efficiently with most audit queries. However, the additional work and supporting information needed in relation to the BV Inspection means that the audit process has not been completed within the planned timescales. As in previous years, we will debrief with the Accounts team to share views on the final accounts audit. Hopefully this will lead to further efficiencies in the 2016/17 audit process. In particularly we would like to thank Authority officers who were available throughout the audit visit to answer our queries.

Headlines

Financial statements audit risks	We identified the following significant financial statements audit risks in our 2015/16 External audit plan issued in June 2016. — Property Plant and Equipment (PPE); — Section 106 agreements; — Grant payments; and — Declarations of interest. We have worked with officers throughout the year to discuss these key risks and our detail findings are reported in section 3 of this report. In summary: — There are no matters of any significance arising as a result of our audit work in PPE. — In relation to section 106 agreements we have noted two small schemes where the Authority has not spent the monies received within the timescales specified, although we understand there is very limited risk that the funds could be lost. — For declarations of interest we have noted that there are potential shortcomings in the system in place now that all staff are required to make an annual declaration. — Our work on grant payments is incomplete. We have recently agreed to select our sample for testing from a list of grant programmes, rather than a complete list of grants made in 2015/16 as planned originally. We are also awaiting details of potential unlawful items of account where we understand that several grants were paid when the conditions set by Commissioners had not been met.

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Headlines (cont.)

In relation to the Authority's VFM arrangements we anticipate issuing a qualified VFM conclusion on similar grounds to that in 2013/14 and proposed for 2014/15.

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VFM conclusion and risk areas	We identified one significant risk and two areas of audit focus in relation to our VFM work in our External audit plan 2015/16 issued in June 2016 in relation to the implementation of the BV action plans and Section 11 recommendation. We have worked with officers throughout the year to discuss these VFM risks and our detailed findings are reported in section 4 of this report. In terms of our VFM conclusion our key consideration has been in relation to the progress made on the areas which led us to qualify our VFM conclusion in 2013/14 and proposed qualification for 2014/15. These areas were grant payments and connected decisions; disposal of property and the granting of leasehold interests; spending on publicity; and corporate governance arrangements in the three areas. Our proposed qualification for 2014/15 additionally referred to our Section 11 recommendation made in October 2015 reflecting our view that the Authority needed to ensure that its governance processes were appropriate in a wider sense for the Authority as a whole and as part of its programme of cultural change and not just the areas referred to in the BV Inspection report. Consequently, in terms of 2015/16 we have considered the reporting by the Commissioners to the Secretary of State for Communities and Local Government (SoS for CLG) and the extent to which the Authority's BV action plans were reported as actions completed. We have also considered the progress in relation to our Section 11 recommendation. In their March 2016 letter to the SoS for CLG the Commissioners set out their disappointment with early progress and lack of acknowledgement of the shortcomings in the culture of the Authority and the adverse impact on how some decisions were made (prior to June 2015 when the current Mayor was elected). The Commissioners also emphasised the need to make more progress on the organisational culture piece and the time it will take for this to be successful and become embedded. We have also considered the extent to which the Authority's BV Action Plans were implemented during 2015/16. The reports submitted to Cabinet meetings in September 2015 and March 2016 clearly show that while progress was meaningful there were a significant number of actions that were not completed within 2015/16. We further consider that many of the actions will require time to become established and embedded even once the arrangements/procedures have been put in place. In relation to our Section 11 recommendation the suggested governance review remains relevant and is to be undertaken in conjunction with the other actions currently being undertaken including the programme of cultural change. We have therefore concluded that the Authority has not made proper arrangements to secure economy, efficiency and effectiveness in its use of resources throughout 2015/16. We therefore anticipate issuing a qualified VFM conclusion on similar grounds to that in 2013/14 and proposed for 2014/15. A draft of our opinion covering both the financial statements and the VFM arrangemnets is included in Appendix 5.

Headlines (cont.)

Completion	At the date of this report our audit of the financial statements is nearing completion and we are targeting finalisation by the end of October. The principle matters outstanding relate to the following areas: — Cash (school bank reconciliations) — Payroll — Grants (we have recently agreed to select our sample for testing from a list of grant programmes, rather than a complete list of grants made in 2015/16 as planned originally) and related review and testing of income from property leases with the community and voluntary sector — Journals (Authority and Pension Fund). You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We will provide a draft of this representation letter to the Section 151 Officer in due course. We draw your attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are asking management to provide specific representations on the following: grant payments (particularly in relation to completeness and lawfulness); and section 106 agreements (where the timescale for the use of the monies received has been exceeded). 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.
Certificate	We have two objections from Local Government Electors relating to earlier years. One is in relation to parking matters and the Authority's 2013/14 financial statements. The other objection refers to the Authority's Lender Option Borrower Option loans and relates to 2014/15 (see Proposed Audit Opinion section above). In addition we have not yet completed the work necessary to issue our assurance statement in respect of the Authority's Whole of Government Accounts consolidation pack. Until the above matters have all been resolved we will not be in a position to formally conclude the audit and issue an audit certificate.
2014/15	In relation to the 2014/15 year end, as previously reported the audit was complete subject to consideration of the impact on our signing of the LOBO objection. Guidance has now been received from the NAO in this regard and, having considered this, we anticipate being able to sign the 2014/15 financial statements and VFM opinions in the near future. We will not be in a position to issue the audit certificate closing the audit pending the consideration of the outstanding objections including the LOBO objection.

KPMG

Section three: Financial Statements

Proposed opinion and audit differences

So far we have not identified any issues in the course of the audit that are considered to be material.

We have identified no 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 Authority's financial statements and the Fund's financial statements, as contained both in the Authority's Statement of Accounts and the Pension Fund Annual Report.

The wording of your Annual Governance Statement complies with guidance issued by CIPFA/SOLACE in June 2007.

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Proposed audit opinion

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority's financial statements following approval of the Statement of Accounts by the Audit Committee on 29 September 2016.

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 (see Appendix two for more information on materiality) level for this year's audit was set at £15 million. Audit differences below £750,000 are not considered significant.

We have not identified 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 2015/16 ('the Code'). We understand that the Authority will be addressing these where significant.

Pension fund audit

Our audit of the Fund also did not identify any significant misstatements.

For the audit of the Fund we used a materiality level of £20 million. Audit differences below £1 million are not considered significant.

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion following approval of the Statement of Accounts by the Audit Committee on 29 September 2016.

We identified a small number of presentational adjustments required to ensure that the accounts are compliant with the Code. We understand that the Fund will be addressing these where significant.

Annual governance statement

We have reviewed the Annual Governance Statement and confirmed that:

- It complies with *Delivering Good Governance in Local Government: A Framework* published by CIPFA/SOLACE; and
- It is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

Pension fund annual report

We have not yet completed our review of the Pension Fund Annual Report and consequently we are yet able to confirm that:

- The financial and non-financial information it contains is not inconsistent with the financial information contained in the audited financial statements.

We anticipate completing this work by the time we provide our opinion on the Statement of Accounts.

Significant audit risks

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 2015/16*, presented to you in June 2016, we identified the significant risks affecting the Authority's 2015/16 financial statements. We have not yet completed our testing of all of these areas. We have set out our evaluation following our substantive work or a position statement. There were no significant risks identified for the Pension Fund.

Property Plant and Equipment (PPE)

— Risk

The Council has a significant asset base primarily relating to Council dwellings; and operational buildings. The potential for impairment/valuation changes makes this balance inherently risky due to the high level of judgement and estimation uncertainty.

— Findings

We have considered the Authority's approach to valuation of PPE with reference to accounting standards and the Code; the information provided to the valuer; reports received by the Authority from its valuer and the judgements made by the Authority in response to those reports. We have compared your valuer's assumptions to benchmarks and to assumptions used for 2014/15 for consistency and ensured that the valuer explicitly considered upward trends as well as impairments in conducting the valuations; and also whether there were material changes in valuations for asset classes valued more than 12 months ago. We also considered disposals (in relation to the BV Inspection findings and consequent Direction); and the completeness of information held on the new fixed asset system. We have no matters to bring to your attention as a result of completing this work.

Grant payments

— Risk

The Best Value Inspection completed in 2014 concluded that the Authority had not achieved its best value duty with regard to the payment of grants totalling £12.2 million and connected decisions in the period from 25 October 2010 to 4 April 2014. Consequently, the award of grants became the responsibility of independent Commissioners who were appointed by the Secretary of State for CLG from January 2015. (2015/16 represented the first full year of the new arrangements being in place.)

— Findings

Our work in this area is not yet complete. Our planned approach was to consider the detailed approach and systems put in place by the Council and Commissioners and to assess whether any conditions/ delegation arrangements have been implemented effectively by Authority officers. At the time of writing this report we have recently agreed to select our sample for testing from a list of grant programmes, rather than a complete list of grants made in 2015/16 as planned originally. We are also awaiting details of potential unlawful items of account where we understand that several grants were paid when the conditions set by Commissioners had not been met.

Significant audit risks

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Section 106 agreements

— Risk

The Commissioners highlighted this as an additional area of concern from the enquiries they have made. The Authority has also had an independent review undertaken of its arrangements in relation to s106 systems, processes, controls and monitoring arrangements.

— Findings

We have tested a selection of schemes and the overall controls employed by the Authority to ensure that section 106 agreement funds are being used in accordance with the conditions agreed as part of the planning process. Our testing of 27 schemes did not identify any issues in terms of balances held and monies spent during 2015/16. We noted that there are two schemes which have gone beyond the time when the s106 agreement requires the funds to have been spent. (PA/06/01439 expired October 2015 and the balance at 31 March 2016 was £3m we understand this balance has been committed to two projects which have commenced in 2016/17 and that the developer making the original payment has been dissolved; and there is one further small scheme which has gone beyond the time when the s106 agreement required the funds to have been spent (PA/02/1852 - £40,000). We understand that due to the circumstances of each scheme that there is very limited risk of the funds being lost. We have also noted a further scheme which is due to expire in January 2017 with a balance of £2.1m at 31 March 2016 where there are approved schemes in place that are due to use the balance during 2016/17. We will review the position on this scheme as part of our 2016/17 audit (PA/06/2068).

We have also considered the results of the independent review and the Authority's response. The review raised a number of recommendations for improvements, which the Authority has responded to positively. The Authority has reported that all recommendations have been implemented except those that required the implementation of a new software system which has been procured and is in the process of being implemented.

Significant audit risks

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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Declarations of interest

— Risk

We reported in our 2014/15 ISA260 report to the Authority that the Authority had taken the actions agreed in response to our 2013/14 recommendations in this area (made in October 2015). However, the Commissioners have informed us that they remain concerned as to whether declarations are being made appropriately and completely by both officers and Members.

— Findings

We have reviewed the actions taken by the Council which now include a requirement for all staff to complete an annual declaration. Our testing of the declarations made has not identified any issues. However, we have noted a number of concerns:

- The initial response by staff to the new requirement was slow. We understand that the Authority has now received over 90% of expected returns, which has taken 6 months and a 100% return is essential to meet the aims of the exercise;
- We understand that the Authority is satisfied that every member of staff has been identified and therefore required to complete a declaration form, but our experience elsewhere suggests that it is worthwhile obtaining further assurance on this aspect, such as from an internal audit review;
- Human Resources have provided Corporate Directors and Heads of Service with reports that identify whether submitted declarations have been authorised or rejected by line managers to help inform whether to consider further appropriate action if there are areas of concern. In view of the concerns expressed by the BV Inspection and Commissioners we would anticipate that a further level of assurance is sought as to how robust the process has been in terms of considering the declarations made and any follow up action taken; and
- There is little in the way of comprehensive training so that staff are clear what the Authority's requirements and objectives are understood clearly by staff and that they have the necessary information to complete declarations properly and to support the Authority in terms of any issues that might arise from incomplete declarations.

We have therefore reflected these points in out consideration of the implementation of our recommendation in our *ISA 260 Report 2014/15* (see Appendix 1).

Significant audit risks

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In our *External Audit Plan 2015/16* 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 tables below set out the outcome of our audit procedures and assessment on these risk areas.

Fraud risk of revenue recognition

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 2015/16 we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

Subsequently, we have revised our assessment and consider that conditional grant income (which is predominantly made up of s106 ie developers' contributions (80% of the total of £76 million)) should be considered as a risk. This work has therefore been reported within the significant audit risks for section 106 agreements earlier in this section.

Management override of controls

Professional standards require us to communicate the fraud risk from management override of controls as significant because 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.

Our audit methodology incorporates the risk of management override as a default significant risk. 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.

Other areas of focus

In our External Audit Plan 2015/16, presented to you in June 2016, we identified four areas of audit focus. These are not considered as significant risks but areas of importance where we would carry out some substantive audit procedures to ensure there is no risk of material misstatement.

We have now completed our testing for two of the areas. The fourth area is closely related to our significant risk on grants (where our work is not yet complete). The table sets out our detailed findings or status for each area of audit focus.

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Pension assets/liabilities

— Risk

Pension valuations require a significant level of expertise, judgement and estimation and are therefore more susceptible to error. This is also a very complex accounting area increasing the risk of misstatement.

— Findings

We have:

- Confirmed that the information provided to the actuary from the Authority is reasonable;
- Reviewed the actuarial valuation and considered the disclosure implications; and
- Considered the approach adopted and assumptions made by your actuaries to benchmarks and other information available to us and to the assumptions used for 2015/16 for consistency with previous years.

No issues were noted as a result of our procedures.

Payroll

— Risk

Payroll represents a significant proportion of the Authority's annual expenditure (approaching 33% of gross spend at £464m in 2014/15). Whilst not considered overly complex from a material error perspective, we consider that it is important from an audit perspective to understand the nature of the Authority's expenditure in this area.

— Findings

As noted in the Headlines section our work in this area has not yet been completed. We plan to:

- Review and test reconciliations for gross pay and deductions (eg pensions, tax and national insurance).
- Complete substantive analytical review of payroll costs and testing supporting system information used to compile the review.

Other areas of focus

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Income from property leases

— Risk

Commissioners have identified concerns relating to the robustness and comprehensiveness of information relating to occupation of Council property and formal support to explain/justify related decisions when determining any charges to be paid by the organisation occupying Council property. This also impacts on VFM in that the amounts due/collected/written off are accurately recorded but the concern is with the process for agreeing arrangements formally and implementing them appropriately.

— Findings

Our work in this area is not yet complete. Our planned approach was to consider the Authority's approach to leasing its property and the information held to support its decision making and then to test a sample of agreements to assess whether the approach to leasing is followed in practice. This area is closely linked to our work on grants and therefore will be completed at the same time.

Youth services

— Risk

There have been several investigations and audits within the Authority's youth service in the last two years each giving cause for concern. We understand a root and branch review has been commissioned into Youth Services more generally to provide a holistic view. Although not material in financial statement terms the gross budget for the service is significant at approaching £9 million in 2015/16. Again this is an area that also impacts on VFM.

— Findings

The Council has taken considerable action with regards to the Youth Service in terms of improving its governance; spending controls; and service delivery. New senior officers have been appointed to manage the Service and it has been moved to a different Directorate to give it a greater opportunity with more of a 'fresh' start. There is a detailed action plan in place which is in the process of being implemented.

In addition the Youth Services Project Group will oversee the progress of investigations (current and future) into individuals and organisations that are known to the Youth Service from the various investigations that have been completed previously. This group will ensure that suitable pace is injected into the progress of the investigations and other arising issues enabling management within the Youth Service to conclude on historical matters and concentrate of the future of the Youth Service. The Project Group comprises senior officers from Children's Services, Human Resources, Internal Audit, Finance, Legal Services, and Communications.

Accounts production and audit process

We have noted that the quality of the accounts and the supporting working papers have been maintained.

Officers dealt efficiently with audit queries. However, the additional work and supporting information needed in relation to the BV Inspection means that the audit process has not been completed within the planned timescales.

The Authority has implemented two of the three recommendations in our ISA 260 Report 2014/15.

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 Authority has maintained its financial reporting process. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 30 June 2016.
Quality of supporting working papers	Our *Accounts Audit Protocol*, which we issued in June 2016 and discussed with the Financial Accountant, set out our working paper requirements for the audit. The quality of working papers provided met the standards specified in our *Accounts Audit Protocol*.
Response to audit queries	Officers resolved the majority of audit queries in a reasonable time. However, the additional work and supporting information needed in relation to the BV Inspection means that the audit process has not been completed within the planned timescales.

Element	Commentary
Pension Fund Audit	The audit of the Fund was undertaken alongside the main audit. There are no specific matters to bring to your attention relating to this at this stage, but we have work on journals and completion and review procedures which still need to be done.

Prior year recommendations

As part of our audit we have specifically followed up the Authority's progress in addressing the recommendations in last years ISA 260 report.

The Authority has implemented two of the three recommendations in our *ISA 260 Report 2014/15*. Appendix one provides further details of the remaining recommendation.

Completion

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.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

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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 and the London Borough of Tower Hamlets Pension Fund for the year ending 31 March 2016, we confirm that there were no relationships between KPMG LLP and the London Borough of Tower Hamlets 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 four 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, Resources for presentation to the Audit Committee. We require a signed copy of your management representations before we issue our audit opinion.

We expect to include specific representations in relation to grants, but need to complete our work in this area to determine what they will be.

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.

Section four: Value for Money

VFM Conclusion

Our VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We follow a risk based approach to target audit effort on the areas of greatest audit risk.

We have concluded that the Authority has not made proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

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Background

The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the authority 'has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources'.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to 'take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor's judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body's arrangements.'

The VFM approach is fundamentally unchanged from that adopted in 2014/2015 and the process is shown in the diagram below. However, the previous two specified reporting criteria (financial resilience and economy, efficiency and effectiveness) have been replaced with a single criteria supported by three sub-criteria.

These sub-criteria provide a focus to our VFM work at the Authority.

Conclusion

We have concluded that the Authority has not made proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

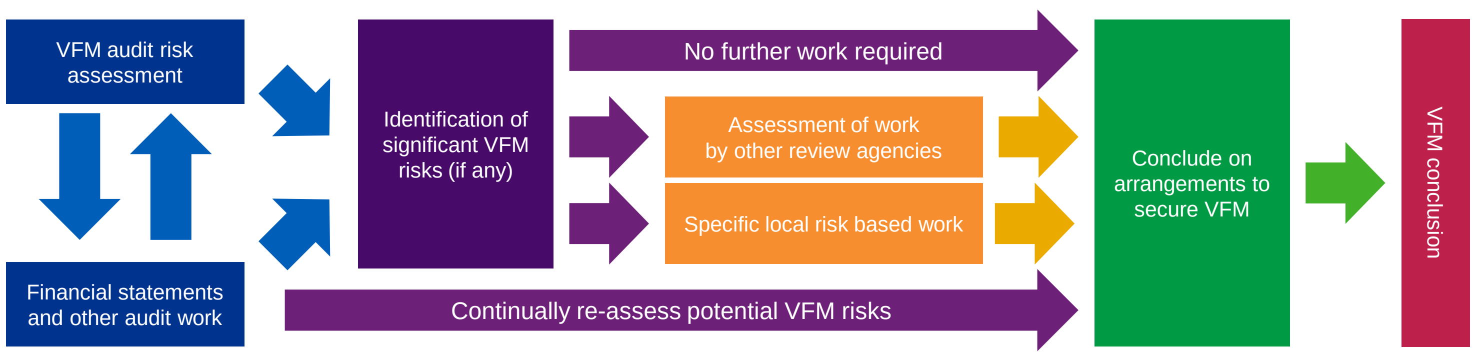
Overall criterion

In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Informed decision making

Sustainable resource deployment

Working with partners and third parties



Specific VFM Risks

We have concluded that the Authority has not made proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

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Consideration of BV Inspection report and subsequent action plans

In seeking to satisfy ourselves that the Authority has made proper arrangements for challenging how it secures economy, efficiency and effectiveness in its use of resources, we have continued our consideration of the findings of the BV Inspection report and more specifically the Authority's progress towards implementing the action plans that it produced in response.

In relation to 2015/16 it is important to note that we are looking at the financial year as a whole when considering the VFM conclusion.

The Commissioners have reported that the Authority did not make meaningful progress in accepting the BV Inspection findings and Directions and considering how to address the concerns identified until the current Mayor was elected in June 2015. Furthermore, in their March 2016 letter to the SoS for CLG they commented that although good progress was now being made, they still felt that the Authority had wasted a significant amount of time in the immediate period after the BV Inspection Report had been published.

Consequently, in terms of our VFM conclusion our key consideration has been in relation to the progress made on the areas which led us to qualify our VFM conclusion in 2013/14 and proposed qualification for 2014/15. These areas were grant payments and connected decisions; disposal of property and the granting of leasehold interests; spending on publicity; and corporate governance arrangements in the three areas. Our proposed qualification for 2014/15 additionally referred to our Section 11 recommendation made in October 2015 reflecting our view that the Authority needed to ensure that its governance processes were appropriate in a wider sense for the Authority as a whole and as part of its programme of cultural change and not just the areas referred to in the BV Inspection report.

In terms of 2015/16 we have considered the reporting by the Commissioners to the SoS for CLG and the extent to which the Authority's BV action plans were reported as actions completed.

The Mayor's letter to the SoS CLG was positive about progress being made whilst realising that the organisational aspect in particular will take some time to become embedded.

The Commissioners' response notes their disappointment with early progress and lack of acknowledgement of the shortcomings in the culture of the Authority and the adverse impact on how some decisions were made. The Commissioners also emphasised the need to make more progress on the organisational culture piece and the time it will take for this to be successful and become embedded.

We have also considered the extent to which the Authority's BV Action Plans were implemented during 2015/16. The reports submitted to Cabinet meetings in September 2015 and March 2016 clearly show that while progress was meaningful there were a significant number of actions that were not completed within 2015/16. We further consider that many of the actions will require time to become established and embedded even once the arrangements/procedures have been put in place.

Indeed the latest Cabinet report (6 September 2016) states the following:

The Council is now in a position to report that more than 95% of the actions within the Best Value Plans are complete. More significantly, progress has been made in delivering the related outcomes and further information on this is provided below.

It is also recognised that implementing significant organisational change is a long-term, iterative process. As such, this update report also addresses issues, which fall outside of the formal Best Value Plans agreed with the Secretary of State, that have been identified by the Council or the Commissioners as matters where further work is required and underway.

Specific VFM Risks

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Conclusion of arrangements to secure value for money

The matters raised in the BV Inspection report raise concerns in relation to the adequacy of the Authority's arrangements for challenging how it secures economy efficiency and effectiveness in its use of resources in the areas highlighted above.

We are required to conclude on the Authority's arrangements to secure economy, efficiency and effectiveness in its use of resources, for the whole of 2015/16. So although considerable progress is being reported, we anticipate issuing an adverse opinion in respect of the Authority's arrangements to secure value for money on similar grounds to our 2013/14 VFM conclusion and proposed 2014/15 VFM conclusion.

Work completed

In line with the risk-based approach set out on the previous page, and in our *External Audit Plan* we have:

- Assessed the Authority's key business risks which are relevant to our VFM conclusion;
- Identified the residual audit risks for our VFM conclusion, taking account of work undertaken in previous years or as part of our financial statements audit;
- Considered the results of relevant work by the Authority, inspectorates and review agencies in relation to these risk areas;
- Continued our consideration of the Authority's actions to address issues raised by the BV Inspection report produced by PwC;
- Considered other matters brought to our attention by the Tower Hamlets Commissioners; and the DCLG; and
- Followed up on relevant issues included in our *ISA 260 Report 2014/15* presented to the Audit Committee in March 2016.

Key findings

On the previous pages we have specifically considered the progress towards implementing the BV action plans that the Authority has drawn up in response to the BV Inspection and subsequent considerations from the Commissioners appointed by the DCLG.

On the following pages we have set out the findings in respect of those areas where we identified a residual audit risk for our VFM conclusion in our Audit Plan.

Specific VFM Risks

We have identified a number of specific VFM risks.

In most cases we are satisfied that external or internal scrutiny provides sufficient assurance that the Authority's current arrangements in relation to these risk areas are adequate.

We have undertaken work in response these risks as summarised in the assessment column.

Key VFM risk	Risk description and link to VFM conclusion	Assessment
Implementation of BV action plans and section 11 recommendation	The Authority monitors progress towards implementation regularly and reports on a monthly basis to the Best Value Programme Board. Internal Audit have an agreed programme to review the accuracy of each of the seven action plans as regards the implementation of the individual milestones. The next stage will be for the Authority to be able to demonstrate that the actions have had the planned impact; have addressed the weaknesses in the Authority's arrangements that were highlighted by the BV Inspection report; Electoral Court judgement; and SoS CLG's Directions; and are embedded into the Authority's culture. This is relevant to the informed decision making, sustainable resource deployment, working with partners and third parties sub-criteria of the VFM conclusion.	Our section 11 recommendation centred around the Authority undertaking a detailed review of its governance processes across the Authority to satisfy itself that they are appropriate and operating effectively. We are satisfied that the steps necessary for the Authority to address the matters raised have been integrated into the Organisational Culture BV action plan. Our consideration of the progress towards implementation of the BV action plans has been set out earlier in this Section **Specific risk based work required: Yes, see earlier in this Section.** As noted earlier in this section, our consideration of the Authority's progress towards implementing the BV action plans for 2015/16 as a whole is considered to have an adverse impact on the overall VFM conclusion.

Specific VFM Risks (cont.)

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Key VFM risk	Risk description and link to VFM conclusion	Assessment
Governance in schools	In 2013/14 Internal Audit reviews found that over half of the schools audited (14 out of 27) fell below the minimum standard of financial control, and management. Internal Audit have also investigated other schools where external referrals alleging irregularity at some schools have been received. Whilst these investigations have not been finalised, it is clear that there are also weaknesses in the governance arrangements of these schools. The Authority has taken action to reinforce the importance of governance and the role of Governors in managing schools. As part of our 2014/15 audit we commented that it would take time for the full impact of the actions to take effect. This is relevant to the informed decision making and working with partners and third parties sub-criteria of the VFM conclusion.	The Authority has taken action to reinforce the importance of governance and the role of Governors in managing schools. It has reviewed its guidance and issued the latest guidance to schools and governors. Also training and guidance on governance arrangements has been delivered to both Governors and Schools Business Managers. The Authority is also making further enhancements to arrangements by giving direct support to those schools which have been identified in internal audit reports as consistently receiving limited assurance through additional workshops delivered by Mazars and Schools Finance. We have considered the impact/progress by liaising with Internal Audit (IA) on results of recent audits. The annual report for schools in 2014/15 showed that 9 schools received a 'substantial' rating, but 5 had limited assurance and 2 had nil assurance. For 2015/16 the IA annual report shows that of the 25 schools receiving an audit 21 received a 'substantial' assurance rating and 4 had a limited assurance. Representing a significant improvement and positive direction of travel. We have also reviewed the 2015/16 annual report for schools which sets out the findings from the reviews and common issues, although we do not consider (in view of the overall assurances given) that these are significant in overall terms for the VFM conclusion. **Specific risk based work required: Yes as per above** No adverse impact on the overall VFM Conclusion.

Specific VFM Risks (cont.)

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Key VFM risk	Risk description and link to VFM conclusion	Assessment
Medium Term Financial Strategy	Local Authorities are subject to an increasingly challenged financial regime with reduced funding from Central Government whilst having to maintain a statutory and quality level of services to local residents. At the point of our planning the Authority is estimating a small over spend (of around £1.2 million) for 2015/16. The Authority's balanced budget for 2016/17, included the delivery of £21 million of approved savings plans, and the use of £23 million from General Fund reserves. The Authority estimated that a further £58 million in savings would need to be achieved during the three years 2017/18 to 2019/20, after using £4 million of reserves (General Fund reserves were estimated to be £36 million at 31 March 2020). The Authority was in the process of developing and agreeing proposals with Members for these future estimated savings. The need for savings could have a significant impact on the Authority's financial resilience. Consequently, the Authority will need to continue to manage its savings plans to secure longer term financial and operational sustainability. This is relevant to the informed decision making and sustainable resource deployment sub-criteria of the VFM conclusion.	We have reviewed overall management arrangements that the Council has for managing its financial position, including the processes to develop a robust Medium Term Financial Strategy (MTFS), ongoing monitoring of the annual budget, review of how savings plans have been developed and how their delivery is monitored, responsiveness to increasing costs of demand led services and changes in funding allocations and the governance arrangements of how the figures are reported through to Council. The Authority has set a balanced budget for 2016/17 and is in the process of developing its detailed MTFS to 2020 supported by detailed outcome based budgets. The next phase is due to be reported to Members in October 2016. **Specific risk based work required: Yes, see above and more detailed commentary on the next page.** No adverse impact on the overall VFM conclusion.

VFM – Financial position

2015/16 outturn

In terms of its financial standing the Authority is reporting that the revised budget has been met. Indeed there was an under spend of £8 million in total which meant that the planned use of reserves was not required (as contingencies in the budget were not needed to be applied) and the General Fund reserve increased slightly to £72 million.

2016/17 budget

In relation to the MTFS we note that the Council has agreed a balanced budget for 2016/17. The budget includes £21 million of agreed savings and £23 million use of reserves (which would reduce General Fund reserves to £49 million).

For the £21 million of savings, this was agreed by Members in two batches £4 million in year and £17 million as part of budget setting in February 2016. All of the savings schemes were supported by detailed statements explaining what was being planned and how it would be delivered/achieved. The supporting papers also set out any changes to services; explained any equality implications and included a formal Equalities Impact Assessment (supported by an action plan for any groups affected adversely). In terms of monitoring the savings are built into base budgets and so they are monitored as part of on-going budget monitoring.

MTFS 2017 – 2020

For the period covered by the MTFS (three years from 2017 – 2020) the Authority needs to identify £58 million in savings and is only looking to use £4.5 million from General Fund reserves over this period (leaving reserves at £44 million at 31 March 2020).

The Council is using 2016/17 to look in great detail at what it does and how it does it using outcomes-based budgeting. Cabinet received an update report in September 2016 setting out progress being made and future planned reporting that would enable the Authority to make informed decisions about resource prioritisation and allocation decisions in a way that provides a stable and considered approach to service delivery and funding the priorities agreed within the Authority's Strategic Plan and takes into account relevant risks and uncertainty. Further reporting and decision making to develop a balanced budget for the three years 2017-20 will take place between now and February 2017.

KPMG

Appendices

Follow up of prior year recommendations

The Authority has not implemented all of the recommendations in our *ISA 260 Report 2014/15*.

We re-iterate the importance of the outstanding recommendation and recommend that the matter noted from our 2015/16 consideration are addressed.

At this stage we have not drafted and agreed with officers recommendations in relation to the current year, these will be reported to the Audit Committee at a subsequent meeting, We anticipate raising some recommendations in relation to grants.

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This appendix summarises the progress made to implement the recommendations identified in our ISA 260 Report 2014/15 and re-iterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	3
Implemented in year or superseded	2
Remain outstanding (re-iterated below)	1

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at September 2016
1	❶	**Declarations of Interest** The BV Inspection report refers to several instances where there are relationships with other parties. The BV Inspection report does not conclude as to whether these relationships represented significant concerns or were improper. However, there appears to be the potential for interests that should be declared not being so, possibly due to due to incomplete knowledge about who the Authority is doing business with, or seeking to do business with. As a minimum this gives the potential for reputational damage to the Authority. **Recommendation** The Authority should: 1. Review its policies, procedures and processes for identifying potential interests and ensuring declarations are up to date and complete; 2. Consider whether improvements can be made to ensure relevant members and officers are aware of organisations and individuals seeking to do business with or interact with the Authority; and 3. Ensure that all relevant members and officers receive at least annual training and reminders about their responsibilities and the need to ensure interest declarations are complete and up to date.	Melanie Clay and Zena Cooke December 2015	As noted in Section 3 we have noted that there are some weaknesses in the Authority's systems and approach to the new requirement for all staff to complete an annual declaration of interest. In particular these relate to completeness of records to ensure all staff have completed a return; for those staff identified to date there has not yet been a 100% return of declarations; training should be enhanced to ensure staff understand the importance of the declarations and completing them fully and accurately; obtaining further assurance about the process and consideration/ assessment of the returns received and whether any further action is needed. We will therefore continue to follow up this recommendation next year.

Follow up of prior year recommendations (cont.)

The definition of the priority ratings we use is provided on this page.

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Priority rating for recommendations					
❶	***Priority one***: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	❷	***Priority two***: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸	***Priority three***: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

Audit differences

This appendix sets out the audit differences.

The financial statements have been amended for all of the matters identified through the audit process.

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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.

Uncorrected audit differences

We are pleased to report that there are no uncorrected audit differences.

Corrected audit differences

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

Materiality and reporting of audit differences

For 2015/16 our materiality is £15 million for the Authority's accounts. For the Pension Fund it is £20 million.

We report all audit differences over £750,000 million for the Authority's accounts and £1 million for the Pension Fund, to the Audit 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 2015/16, presented to you in June 2016.

Materiality for the Authority's accounts was set at £15 million which equates to around 1.2 percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Audit 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 Audit 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 Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £750,000 for the Authority.

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

Materiality – Pension fund audit

The same principles apply in setting materiality for the Pension Fund audit. Materiality for the Pension Fund was set at £20 million which is approximately 1.78 percent of gross assets. An individual difference could normally be considered to be clearly trivial if it is less than £1 million.

Declaration of independence and objectivity

Auditors appointed by Public Sector Audit Appointments Ltd must comply with the Code of Audit Practice.

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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:

"The auditor should carry out their work with integrity, objectivity and independence, and in accordance with the ethical framework applicable to auditors, including the ethical standards for auditors set by the Financial Reporting Council, and any additional requirements set out by the auditor's recognised supervisory body, or any other body charged with oversight of the auditor's independence. The auditor should be, and should be seen to be, impartial and independent. Accordingly, the auditor should not carry out any other work for an audited body if that work would impair their independence in carrying out any of their statutory duties, or might reasonably be perceived as doing so."

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.

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.

Declaration of independence and objectivity (cont.)

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.

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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.

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 and the London Borough of Tower Hamlets Pension Fund for the financial year ending 31 March 2016, we confirm that there were no relationships between KPMG LLP and the London Borough of Tower Hamlets 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 four

Audit Independence

Audit Fees

Our scale fee for the Authority audit and Pension Fund audits was £230,918 plus VAT (£300,890 in 2014/15). This fee was in line with that highlighted within our audit plan agreed by the Audit Committee in June 2016. Additional fees will be required for the additional work we have needed to undertake relating to the BV Inspection issues and the Council's response (the additional fees to date for 2014/15 are £22,000, although this does not include dealing with the LOBO objection which we are in the process of considering).

Our scale fee for certification for the HBCOUNT is £20,327 plus VAT (£30,450 in 2014/15), and fees for other grants and claims (Teachers' Pensions Return and Capital Receipts Return) was £6,500 plus VAT.

Non-audit services

We have summarised below the non-audit services that we have been engaged to provide, the estimated fee, the potential threats to auditor independence and the associated safeguards we have put in place to manage these.

Description of non-audit service	Fee	Potential threat to auditor independence and associated safeguards in place
Conducting business intelligence research on 14 companies of interest to the Authority. The research will include identifying any links between these companies as well as their known public profile.	£36,500	**Self interest** – This engagement is entirely separate from the audit through a separate contract, engagement team and lead partner. In addition, the audit fee scale rates were set independently to KPMG by the PSAA. Therefore, the proposed engagement will have no perceived or actual impact on the audit team and the audit team resources that will be deployed to perform a robust and thorough audit. **Self review** – The nature of this work was to conduct business intelligence research on 14 companies of interest to the Authority. The research will include identifying any links between these companies as well as their known public profile. We used information available in the public domain only. Therefore, it does not impact on our opinion and we do not consider that the outcome of this work will be a threat to our role as external auditors. The existence of a separate team for this work is a further safeguard. Consequently, we consider we have appropriately managed this threat. **Management threat** – This work was advice and support only – all decisions were made by the Authority. **Familiarity** – This threat is limited given the scale, nature and timing of the work. The existence of the separate team for this work is the key safeguard. **Advocacy** – We will not act as advocates for the Authority in any aspect of this work. We will draw on our experience in such roles to provide the Authority with a summary of information obtained but the scope of this work falls well short of any advocacy role. **Intimidation** – not applicable
Fees	**£36,500**	
Fees as a percentage of external audit fees	**16%**	

Draft audit opinion

Independent auditor's report to the members of the London Borough of Tower Hamlets

We have audited the financial statements of the London Borough of Tower Hamlets for the year ended 31 March 2016 on pages x to x. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

This report is made solely to the members of the Authority, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014. Our audit work has been undertaken so that we might state to the members of the Authority, as a body, those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the members of the Authority, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Corporate Director of Resources and auditor

As explained more fully in the Statement of the Corporate Director of Resources' Responsibilities, the Corporate Director of Resources is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Authority's and the Pension Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Corporate Director of Resources; and the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Narrative Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the financial position of the Authority as at 31 March 2016 and of the Authority's expenditure and income for the year then ended;
- give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2016 and the amount and disposition of the fund's assets and liabilities as at 31 March 2016; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

Matters on which we are required to report by exception

The Code of Audit Practice requires us to report to you if:

- the Annual Governance Statement which accompanies the financial statements does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007; or
- the information given in the Narrative Report for the financial year for which the financial statements are prepared is not consistent with the financial statements; or
- any matters have been reported in the public interest under Section 24 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of, the audit; or
- any recommendations have been made under Section 24 of the Local Audit and Accountability Act 2014; or
- any other special powers of the auditor have been exercised under the Local Audit and Accountability Act 2014.

We have nothing to report in respect of these matters.

Draft audit opinion (cont.)

Conclusion on the London Borough of Tower Hamlets' arrangements for securing economy, efficiency and effectiveness in the use of resources

Authority's responsibilities

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

Auditor's responsibilities

We are required under Section 20(1) (c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Comptroller and Auditor General (C&AG) requires us to report to you our conclusion relating to proper arrangements.

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We report if significant matters have come to our attention which prevent us from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

We have undertaken our review in accordance with the Code of Audit Practice, having regard to the guidance on the specified criterion issued by C&AG in November 2015, as to whether London Borough of Tower Hamlets had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. The C&AG determined this criterion as that necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether London Borough of Tower Hamlets put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2016.

We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, London Borough of Tower Hamlets had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Basis for adverse conclusion

In considering whether the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources we have we have reviewed the progress made against the findings of the Best Value Inspection of the London Borough of Tower Hamlets Report (the Report) produced by PricewaterhouseCoopers LLP (PwC) for the Department for Communities and Local Government (DCLG) dated 16 October 2014 and published on 4 November 2014, as well as the evidence gathered from our own audit work.

The DCLG instructed PwC to cover specific matters as part of the Best Value Inspection. The report concluded that the Authority had not achieved the best value duty with regard to the following areas:

- The Authority's payment of grants and connected decisions;
- The disposal of property and the granting of leasehold interests; and
- Spending on publicity.

The Report also commented that the Authority's corporate governance arrangements did not appear to be capable of preventing or responding appropriately to failures of the best value duty in the areas highlighted above. Subsequently the Secretary of State for Communities and Local Government appointed independent Commissioners to undertake an executive decision-making role in relation to all grant decisions, and to oversee the work of the Authority in these areas of operation. The Commissioners also play a consultative role in the development of plans to deal with weaknesses in the processes for entering into contracts identified in the report, but are not able to issue binding directions to the Authority except in circumstances where they fail to adopt recommendations of the statutory officers.

Draft audit opinion (cont.)

These matters, taken together with comments within the Mayoral election judgment (as set out in the High Court of Justice, Queen's Bench Division, in the matter of the Representation of the People Act 1983, and in the matter of a Mayoral election for the London Borough of Tower Hamlets held on 22 May 2014) and other matters raised with us as auditors, indicate that governance processes were not operating effectively for the periods covered by these inspections and judgments.

The Authority has developed and published comprehensive action plans including a programme of cultural change (the "BV Action Plans") to address the findings of the reports detailed above. During the course of 2015/16, the Commissioners provided regular, quarterly updates to the Secretaries of State on the improvements being delivered at the Council, including detailed six monthly progress reports in September 2015 and March 2016.

We have considered the extent to which the Authority's BV Action Plans were implemented during 2015/16. The reports submitted to Cabinet meetings in September 2015 and March 2016 clearly show that while progress was meaningful, particularly in the latter part of the year, there were a significant number of actions that were not completed within 2015/16. Whilst we note the progress made we also consider that many of the actions will require time to become established and fully embedded even once the arrangements/procedures have been put in place.

In October 2015, in relation to our audit for the year ended 31 March 2014, we raised a recommendation under section 11(3) of the Audit Commission Act 1998 that the Authority should undertake a detailed review of its governance processes to satisfy itself that they were appropriate and operating effectively. This governance review is to be undertaken in conjunction with the other actions currently being undertaken including the programme of cultural change. The reasons for recommending such a review in respect of the year ended 31 March 2014 are equally applicable to our consideration of the adequacy of the Authority's arrangements to secure economy, efficiency and effectiveness in the use of resources for the year ending 31 March 2016.

Adverse conclusion

On the basis of our work, having regard to the guidance issued by the C&AG in November 2015, we are not satisfied that, in all significant respects, London Borough of Tower Hamlets put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2016.

Delay in certification of completion of the audit

Due to matters brought to our attention by local authority electors and work on the WGA Return not being completed by the x Xxx 2016

We cannot formally conclude the audit and issue an audit certificate until we have completed our consideration of one matter brought to our attention by a local authority elector under the Audit Commission Act 1998, relating to the year ending 31 March 2014; and one matter brought to our attention by a local authority elector under the Audit Commission Act 1998, relating to the year ending 31 March 2015. We are satisfied that this work does not have a material effect on the financial statements or on our conclusion on arrangements to secure value for money.

In addition we have not yet completed the work necessary to issue our assurance statement in respect of the Authority's Whole of Government Accounts consolidation pack. We are satisfied that this work does not have a material effect on the financial statements or on our value for money conclusion.

Andrew Sayers

for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants

15 Canada Square, London, E14 5GL

x Xxx 2016

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The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

Document is Restricted

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