Nottinghamshire County Council

Nottinghamshire Pension Fund Committee

Tuesday, 24 September 2013 at 14:00

County Hall, County Hall, West Bridgford, Nottingham NG2 7QP

AGENDA

Notes

(1) Councillors are advised to contact their Research Officer for details of any Group Meetings which are planned for this meeting.

(2) Members of the public wishing to inspect "Background Papers" referred to in the reports on the agenda or Schedule 12A of the Local Government Act should contact:-

Customer Services Centre 0300 500 80 80

(3) Persons making a declaration of interest should have regard to the Code of

Conduct and the Council's Procedure Rules. Those declaring must indicate the nature of their interest and the reasons for the declaration.

Councillors or Officers requiring clarification on whether to make a declaration of interest are invited to contact Chris Holmes (Tel. 0115 977 3714) or a colleague in Democratic Services prior to the meeting.

(4) Councillors are reminded that Committee and Sub-Committee papers, with the exception of those which contain Exempt or Confidential Information, may be recycled.

minutes

Nottinghamshire County Council

Meeting NOTTINGHAMSHIRE PENSION FUND COMMITTEE

Date Monday, 10th June 2013 (commencing at 2.00 pm)

membership
Persons absent are marked with `A'

COUNCILLORS

Stella Smedley MBE JP (Chairman)
Ken Rigby (Vice-Chairman)

	Reg Adair	Glynn Gilfoyle
A	Chris Barnfather	Sheila Place
	John Clarke	Parry Tsimbiridis
	Mrs Kay Cutts	

OFFICERS IN ATTENDANCE

John Fairbanks	(Environment & Resources)
Chris Holmes	(Policy, Planning & Corporate Services)
Nigel Stevenson	(Environment & Resources)
Sarah Stevenson	(Environment & Resources)
Marje Toward	(Environment & Resources)

APPOINTMENT OF CHAIRMAN AND VICE CHAIRMAN

RESOLVED 2013/010

That the appointment by the County Council on its Annual Meeting on 16th May 2013 of Councillor Stella Smedley MBE JP as Chairman and Councillor Ken Rigby as Vice-Chairman of the Committee be noted.

MEMBERSHIP OF THE COMMITTEE

RESOLVED 2013/011

That the membership of the committee as set out on the agenda be noted.

MINUTES

The Minutes of the last meeting of the Committee held on 18th April 2013, having been previously circulated, were confirmed and signed by the Chairman.

APOLOGIES FOR ABSENCE

An apology for absence was received from Councillor Chris Barnfather (Other Reasons).

DECLARATIONS OF INTEREST BY MEMBERS AND OFFICERS

None

TERMS OF REFERENCE AND ESTABLISHMENT OF WORING PARTY

Consideration was given a report which set out the terms of reference of the Committee and its Sub-Committees and proposed the re-establishment of a Working Party.

RESOLVED 2013/012

1) That approval be given to the re-establishment of the Working Party as set out in the report.

2) That the terms of reference of the Committee and Sub-Committees be noted.

ELECTION OF SCHEDULED BODIES REPRESENTATIVE ON PENSIONS SUB-COMMITTEE AND PENSIONS INVESTMENT SUB-COMMITTEE

RESOLVED 2013/013

That it be noted that the Chief Executive will appoint the Scheduled Bodies representative to the Sub-Committee following consultation with the Chair and Vice-chair when the outcome of the election is determined.

APPLICATIONS FOR SCHEME ACCESS VIA A TRANSFEREE ADMISSION AGREEMENT

RESOLVED 2013/014

That the admission of the following two transferee admission bodies into the Nottinghamshire Pension Scheme be noted:-

- Carillion Services Ltd
- Family Action

PRESENTATION ON PENSION FUND GOVERNANCE

Nigel Stevenson, Group Manager (Financial Strategy and Compliance) gave a presentation to the Committee on Pension Fund Governance.

He indicated that the committee was responsible for administering the Fund and its members acted in a quasi – trustee capacity.

He outlined the trustee responsibilities.

PENSION INVESTMENT SUB-COMMITTEE MEETINGS

Consideration was given to a report which sought approval to holding three of the Pension Investment Sub-Committee meetings at the offices of the Fund's main investment managers.

During the discussion it was suggested that two meetings per year rather than three be held at the offices of the Fund's main investment managers.

RESOLVED 2013/015

That approval be given to holding two of the Pensions Investment Sub-Committee meetings at the offices of the Fund's main investment managers during the next year and that this arrangement be then reviewed.

LOCAL GOVERNMENT EMPLOYERS FUNDAMENTALS TRAINING

RESOLVED 2013/016

That approval be given for new members of the Nottinghamshire Pensions Fund Committee and its Sub-Committees to attend the Local Government Employers Fundamentals Course.

The meeting closed at 2:55 pm.

CHAIRMAN

Nottinghamshire County Council

Report to Nottinghamshire Pension Fund Committee

24 September 2013

Agenda Item: 5

REPORT OF SERVICE DIRECTOR – FINANCE & PROCUREMENT

PENSION FUND ACCOUNTS 2012/13

Purpose of the Report

1. To present the Nottinghamshire Pension Fund accounts for 2012/13.

Information and Advice

2. The Nottinghamshire Pension Fund accounts for 2012/13 are attached. These show the value of the fund as at 31 March 2013 was £3,496 million with net additions from dealings with members during 2012/13 of £5 million and net returns on investments of £419 million.

3. The external auditors, KPMG, have substantially completed their audit work and anticipate issuing an unqualified audit opinion. No material adjustments were identified and only a small number of non-trivial adjustments, most of which were of a presentational nature. The auditor's ISA260 report is also attached for information.

Statutory and Policy Implications

4. This report has been compiled after consideration of implications in respect of finance, the public sector equality duty, human resources, crime and disorder, human rights, the safeguarding of children, sustainability and the environment and those using the service and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

RECOMMENDATION/S

1) That the Pension Fund accounts for 2012/13 be noted.

Name of Report Author: Simon Cunnington
Title of Report Author: Senior Accountant – Pensions & Treasury Management

For any enquiries about this report please contact: Simon Cunnington

Constitutional Comments (NAB 13.09.12)

5. The Nottinghamshire Pension Fund Committee has authority to consider the matters set out in this report by virtue of its terms of reference.

Financial Comments (SRC 12/09/13)

6. There are no direct financial implications arising from the report.

Background Papers

None

Introduction

Nottinghamshire County Council is the administering authority for the Local Government Pension Scheme (LGPS) within Nottinghamshire. The LGPS is a statutory scheme administered by individual pension funds. The benefits within the scheme are determined by regulation and are guaranteed by statute. The pension fund exists to help defray the cost of paying the pension benefits. Members make contributions to the Fund as specified in the regulations and employers make contributions as determined by the Fund's actuary as part of the triennial valuation of the Fund. All new employees are brought into the scheme automatically, unless a positive election not to participate is received from the employee.

The County Council administers the pension fund for over 100 participating employers and over 100,000 members. The employers include the County Council, the City Council, District Councils and organisations which used to be part of local government (such as Nottingham Trent University, Colleges and Police civilian staff). They also include organisations which satisfy the conditions to participate in the LGPS and have been admitted to the Fund by the County Council. In general, these organisations are non-profit making, or are undertaking a service which was, or could be, carried out by the local authority.

The operation of the Fund is set out in a number of published policy statements. Under the Governance Compliance Statement, the functions as administering authority of the Fund are delegated to the Pensions Committee supported by two advisory sub-committees.

The Funding Strategy Statement sets out the aims and purpose of the Fund and details the responsibilities of the administering authority as regards funding the scheme.

The Statement of Investment Principles sets out more detailed responsibilities relating to the overall investment strategy of the Fund including the proposed asset allocation, restrictions on investment types, the type of investment management used and performance monitoring. It also states the Fund's approach to responsible investment and corporate governance issues.

The Communications Strategy Statement details the overall strategy for involving stakeholders in the Fund. A key part of this strategy is a dedicated Fund website which is available at: www.nottspf.org.uk.

A separate annual report for the Fund is also produced and this, along with previous years' reports, will be accessible via the the pension fund website. The annual report includes the accounts and the published policies as well as information on the investment performance of the fund.

The accounts of the fund are set out over the following pages. The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 requires:

- a fund account showing the changes in net assets available for benefits;
- a net assets statement showing the assets available at the year end to meet benefits;
- supporting notes.

NOTTINGHAMSHIRE COUNTY COUNCIL PENSION FUND

FUND ACCOUNT

	Notes	2011/12 £000	2012/13 £000
Contributions	4		
Employer contributions		(134,907)	(127,132)
Member contributions		(42,242)	(42,829)
		(177,149)	**(169,961)**
Transfers in from other pension funds		(10,197)	(11,535)
Benefits	5		
Pensions		117,060	127,078
Commutation of pensions and lump sum retirement benefits		37,467	28,187
Lump sum death benefits		3,588	3,714
		158,115	**158,979**
Payments to and on account of leavers		10,738	16,048
Administration Expenses	6	1,301	1,409
Net additions from dealings with members		**(17,192)**	**(5,060)**
Investment Income	7	(84,830)	(88,307)
Profits & losses on disposal of investments & changes in value		32,988	(334,869)
Taxes on income		674	580
Investment management expenses	8	3,871	3,506
Net Returns on Investments		**(47,297)**	**(419,090)**
Net (increase)/decrease in net assets available for benefits during the year		**(64,489)**	**(424,150)**
Opening net assets of the Fund		3,007,807	3,072,296
Net assets available to fund benefits		**3,072,296**	**3,496,446**

NET ASSETS STATEMENT FOR THE YEAR ENDED

	Notes	31 March 2012 £000	31 March 2013 £000
Investment Assets	9 & 13		
Fixed Interest Securities		288,011	323,555
Index Linked Securities		75,344	80,738
Equities		1,439,871	1,675,534
Pooled Investment Vehicles		854,489	1,028,119
Property		266,603	288,075
Forward Foreign Exchange		-	621
Cash deposits		137,382	81,269
Other Investment Balances	11	14,316	16,360
Investment liabilities	11	(3,232)	(3,157)
		3,072,784	**3,491,114**
Current assets	12	14,994	18,481
Current liabilities	12	(15,482)	(13,149)
		(488)	**5,332**
Net assets of the fund available to pay benefits at the year end		**3,072,296**	**3,496,446**

The actuarial present value of promised retirement benefits, as required by IAS 26, is shown at note 2.

NOTES TO THE ACCOUNTS

1. Accounting Policies

(a) Basis of Preparation
The Pension Fund accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 (the Code). On issues where there is no clear guidance in the Code, reference has been made under the hierarchy of standards to Financial Reports of Pension Schemes: a Statement of Recommended Practice 2007 (the Pensions SORP) or to individual International Acccounting Standards (IAS). Disclosures in the Pension Fund accounts have been limited to those required by the Code.

(b) Debtors and Creditors
The accruals concept is applied to these accounts in compliance with the Code.

(c) Investments
Pension fund investments are carried at fair value in accordance with the Code. Fair value is defined as 'the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arm's-length transaction'. Where an active market exists, the quoted market price is used. Where there is no active market, fair value is established by using valuation techniques.

Specific details on the valuation methods for particular classess of assets are listed below:
i) Equities traded through a stock exchange are valued at the latest quoted price. Where more than one price is quoted the 'bid' price is used.

ii) Unit Trusts and managed funds are valued at the closing single price or the bid price where applicable. These reflect the market value of the underlying investments.

iii) Unquoted securities and pooled private equity investments are valued at fair value by the fund managers at the year end in accordance with industry accepted guidelines.

iv) The market value of fixed interest investments is based on the 'clean price', i.e. excludes income accrued at 31 March but not yet due for payment.

v) Property investments are stated at open market value based on a quarterly independent valuation at the Net Assets Statement date.

Acquisition costs are included in the purchase cost of investments.

The change in fair value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments and unrealised changes in market value.

Forward foreign exchange contracts are over the counter contracts under which two parties agree to exchange two currencies on a specified future date at an agreed rate of exchange. These are used to manage the economic exposure to bond markets and hedge against foreign currency movements. These contracts are included at fair value by determining the gain or loss that would arise from closing out the contract at the Net Assets Statement date by entering into an equal and opposite contract at that date. The movements on these contracts during the year are shown in the reconciliation of opening and closing balances of investments at note 9(b).

(d) Investments Income
Income is accounted for on an accruals basis for the following:

i) interest on cash deposits and fixed interest securities are accrued on a daily basis;
ii) dividends from equities are accrued when the stock is quoted ex-dividend;
iii) rents from property are accrued in accordance with the terms of the lease.

(e) Taxes on Income
UK equity dividends are quoted and accounted for at the net rate. The tax credit, which the Fund is unable to recover, is not recognised (in accordance with the Pensions SORP). Overseas equity dividends are accounted for gross of withholding tax, where this is deducted at source. Partial reclaims of withholding tax, where allowed, are adjusted at the year end by outstanding claims.

(f) Foreign Currencies
Where forward exchange contracts are in place in respect of assets and liabilities in foreign currencies, the contract rate is used. Other assets and liabilities in foreign currencies are expressed in sterling at the rates of exchange ruling at the year-end. Income from overseas investments is translated into sterling at the rate ruling on the date of the transaction. Surpluses and deficits arising on conversion or translation are dealt with as part of the change in market value of investments.

(g) Contributions
Normal contributions, both from the members and from employers, are accounted for in the payroll month to which they relate at rates as specified in the rates and adjustments certificate. Additional contributions from the employer are accounted for on an accruals basis.

(h) Benefits Payable
Under the rules of the Scheme, members can receive a lump sum retirement grant in addition to their annual pension. Lump sum retirement grants are accounted for from the date of retirement. Where a member can choose whether to take a greater retirement grant in return for a reduced pension these lump sums are accounted for on an accruals basis from the date the option is exercised. Other benefits are accounted for on the date the member leaves the Scheme or on death.

(i) Transfers to and from Other Schemes
Transfer values represent the capital sums either receivable (in respect of members from other pension schemes of previous employers) or payable (to the pension schemes of new employers for members who have left the Scheme). They take account of transfers where the trustees (or administering authority) of the receiving scheme have agreed to accept the liabilities in respect of the transferring members before the year end, and where the amount of the transfer can be determined with reasonable certainty.

(j) Other Expenses
Administration and investment management expenses are accounted for on an accruals basis. Expenses are recognised net of any recoverable VAT. Nottinghamshire County Council charges the Fund with the costs it incurs in administering the scheme and the Fund.

2. Operation of the fund

(a) Contributions and Solvency

With effect from 1 April 2008 The Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 were introduced. The principal changes from the 1997 regulations were: the replacement, for future service, of the existing benefits structure (based on a pension of 1/80th of pensionable pay for each year of pensionable service plus an automatic lump sum of three times this amount) by one based on 1/60th of pensionable pay for each year of pensionable service and no automatic lump sum.

Employees are required by the current Regulations to make percentage contributions by deduction from earnings at a rate between 5.5% and 7.5% depending on salary. Employers are required to make such balancing contributions, determined by the Actuary, as will maintain the fund in a state of solvency, having regard to existing and prospective liabilities.

From 1 April 2014 the new Local Government Pension Scheme will be introduced for service accruing after that date. This will be a career average revalued earnings (CARE) scheme with an accrual rate of 1/49th of pensionable pay and a retirement age linked to the state retirement age. Contribution rates will increase for employees earning over £21,000, up to 12.5% for those earning more than £150,000.

(b) Actuarial Valuations

As required by the Regulations an Actuarial Valuation of the Fund was carried out as at 31 March 2010. The market value of the Fund's assets at the valuation date was £2,732 million. The Actuary has estimated that the value of the Fund was sufficient to meet 84% of its expected future liabilities in respect of service completed to 31 March 2010. The certified contribution rates are expected to improve this to 100% within a period of 20 years.

The Actuarial Valuation was carried out using the projected unit method and the assumptions used within the valuation were as follows:

	March 2010	
	% pa	**Real % pa**
Investment return:		
Equities/absolute return funds	7.5%	4.0%
Gilts	4.5%	1.0%
Bonds & Property	5.6%	2.1%
Discount Rate	6.9%	3.4%
Risk Adjusted Discount Rate	6.8%	3.3%
Pay Increases	5.0%	1.5%
Price Inflation	3.5%	-
Pension Increases	3.0%	(0.5%)

The full actuarial valuation report is available on the Fund's website at: www.nottspf.org.uk.

The employers' contribution rates to be paid in years 2011/12 to 2013/14 were set by the latest valuation carried out as at 31 March 2010. At that valuation, the Actuaries certified a common rate of contribution of 18.0% of pensionable payroll with individual adjustments for certain employers. The following list shows the rates payable by the main employers:

Percentages of Pensionable Pay	**2011/12 to 2013/14 %**
Nottinghamshire County Council	18.3%
Nottingham City Council	18.0%
Ashfield District Council	22.4%
Bassetlaw District Council	22.1%
Broxtowe Borough Council	18.7%
Gedling Borough Council	18.2%
Mansfield District Council	20.5%
Newark and Sherwood District Council	21.9%
Rushcliffe Borough Council	19.5%

(c) Actuarial Present Value of Promised Retirement Benefits

The actuarial present value of promised retirement benefits has been calculated by the Fund's actuaries in accordance with IAS 19. To do this, the actuaries rolled forward the value of the Employers' liabilities calculated for the Triennial valuation as at 31 March 2010 allowing for the different financial assumptions required under IAS19. The assumptions used for the purposes of the IAS 19 calculations are as follows:

	31 March 2011		31 March 2012		31 March 2013	
	% pa	Real % pa	% pa	Real % pa	% pa	Real % pa
RPI Increases	3.5%	-	3.3%	-	3.4%	-
CPI increases	2.7%	(0.8%)	2.5%	(0.8%)	2.6%	(0.8%)
Salary Increases	5.0%	1.5%	4.7%	1.4%	4.8%	1.4%
Pension Increases	2.7%	(0.8%)	2.5%	(0.8%)	2.6%	(0.8%)
Discount Rate	5.5%	1.9%	4.6%	1.3%	4.5%	1.1%

The net liability under IAS 19 is shown below.

	31 March 2011 £000	31 March 2012 £000	31 March 2013 £000
Present value of funded obligation	4,057,629	4,966,881	5,476,127
Fair value of scheme assets	2,957,085	3,061,212	3,477,023
Net Liability	**1,100,544**	**1,905,669**	**1,999,104**

The present value of funded obligation consists of £4,307,303,000 in respect of Vested Obligation and £1,168,824,000 in respect of Non-Vested Obligation.

These figures are presented only for the purposes of IAS 19. In particular, they are not relevant for calculations undertaken for funding purposes or for other statutory puposes under UK pensions legislation.

(d) Investment Strategy

The Nottinghamshire Pension Fund Committee, advised by the Pensions Investment Sub-Committee, is responsible for determining the investment strategy of the Fund and the type of investment management to be used.

The investment strategy of the Fund is designed to maximise growth within acceptable risk parameters to help meet the future liabilities. The powers of investment are governed by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. Strategic decisions on investment policy are made by the Pensions Committee, advised by a Pensions Sub-Committee. The policy is set out in the Fund's Statement of Investment Principles, a copy of which is available on the pension fund website (www.nottspf.org.uk).

The Sub-Committee consists of nine elected County Councillors, three representatives of Nottingham City Council, two representatives of the District Councils, two representatives of the trade unions and a representative elected by the other scheduled and admitted bodies. Meetings are also attended by an independent adviser and representatives of the Chief Financial Officer.

The investments are managed by officers of the County Council or by organisations specialising in the management of pension fund assets. The Investments Sub-Committee is responsible for monitoring performance of the fund and meets on a quarterly basis to review managers and investments.

(e) External Audit

A separate fee is payable to KPMG LLP for audit of the pension fund. All fees have been included in the accounts for the period to which they relate. The fee for 2012/13 is £29,926 (for 2011/12 the fee of £44,460 was paid to the Audit Commission).

3. Contributors and Pensioners

	Members at 31 March 2013				
	County Council	City Council	District Councils	Other	Total
Contributors	15,162	8,084	3,285	11,309	37,840
Deferred Beneficiaries	16,319	7,831	3,409	7,628	35,187
Pensioners	14,276	5,874	4,421	5,226	29,797
					102,824

	Members at 31 March 2012				
	County Council	City Council	District Councils	Other	Total
Contributors	16,587	8,681	3,569	9,546	38,383
Deferred Beneficiaries	15,863	7,719	3,307	6,949	33,838
Pensioners	13,720	5,601	4,307	4,847	28,475
					100,696

4. Analysis of Contributions

	Employers		Members		Total	
	2011/12 £000	2012/13 £000	2011/12 £000	2012/13 £000	2011/12 £000	2012/13 £000
County Council	51,062	41,794	15,352	13,612	66,414	55,406
Scheduled Bodies	78,216	81,371	25,469	27,832	103,685	109,203
Admitted Bodies	5,629	3,967	1,421	1,385	7,050	5,352
	134,907	**127,132**	**42,242**	**42,829**	**177,149**	**169,961**

5. Analysis of Benefits

	2011/12 £000	2012/13 £000
Pensions	117,060	127,078
Commutation and lump sum	37,467	28,187
Lump sum death benefits	3,588	3,714
	158,115	**158,979**
Comprising of:		
County Council	64,797	64,206
Scheduled Bodies	88,686	90,511
Admitted Bodies	4,632	4,262
	158,115	**158,979**

6. Administration Expenses

	2011/12 £000	2012/13 £000
Printing & stationery	41	37
Subscriptions and membership fees	3	6
Actuarial fees	9	5
Audit fees	-	15
Other external fees	112	121
Administering Authority Costs	1,136	1,225
	1,301	**1,409**

7. Investment Income

Analysis by type of investment	2011/12 £000	2012/13 £000
Interest from fixed interest securities	(11,598)	(12,575)
Income from index-linked securities	(1,487)	(1,304)
Dividends from equities	(49,585)	(51,357)
Income from pooled investment vehicles	(6,118)	(5,099)
Income from property pooled vehicles	(445)	(1,531)
Net rents from property	(13,838)	(14,683)
Interest on cash deposits	(818)	(1,088)
Other	(941)	(670)
	(84,830)	**(88,307)**

Directly held property		
Rental income	(16,789)	(17,623)
Less operating expenses	2,951	2,940
Net rents from property	**(13,838)**	**(14,683)**

8. Invesment Management Expenses

	2011/12 £000	2012/13 £000
Training & conferences	7	5
Printing & stationery	10	-
Subscriptions and membership fees	23	19
Actuarial fees	2	-
Audit fee	44	15
Custody fees	240	263
Investment management fees	3,001	2,589
Other external fees	238	249
Administering Authority Costs	306	366
	3,871	3,506

9. Investments

(a) Investment Analysis	31 March 2012 £000	31 March 2013 £000
Fixed Interest Securities		
UK Public Sector	123,086	118,757
UK Other	110,864	119,028
Overseas Public Sector	43,629	69,666
Overseas Other	10,432	16,104
Index Linked Securities		
Public Sector	48,164	50,140
Other	27,180	30,599
Equities		
UK	962,695	1,101,770
Overseas	475,032	571,770
Unlisted	2,145	1,994
Pooled Investment Vehicles		
Unit Trusts	338,670	324,988
Other Managed Funds	394,426	581,176
Pooled Vehicles Invested in Property		
Property Unit Trusts	31,365	26,551
Other Managed Funds	90,028	95,404
Property	266,603	288,075
Forward Foreign Exchange	-	250
Cash and Currency	137,382	81,269
Total Investments	**3,061,701**	**3,477,541**

The original values of investments are based on purchase cost plus expenses. If any investments have been held since 1 April 1974 (when the County Council was given the responsibility for the Fund) these are included at the market value as at that date.

	31 March 2012 £000	31 March 2013 £000
Market Value	3,061,701	3,477,541
Original Value	2,575,895	2,600,107
Excess/(Deficit) of Market Value over Original Value	**485,806**	**877,434**

At 31 March 2013 the fund held no investment representing over 5% of the value of the fund (31 March 2012 also nil).

(b) Reconciliation of Opening and Closing Values of Investments 2012/13

	Value at 1 April 2012 £000	Purchases at Cost £000	Proceeds of Sales £000	Change in Market Value £000	Value at 31 March 2013 £000
Fixed Interest Securities	288,011	272,909	(254,623)	17,258	323,555
Index Linked Securities	75,344	25,440	(27,402)	7,357	80,739
Equities	1,439,872	228,930	(196,257)	202,989	1,675,534
Pooled Investment Vehicles	733,096	64,318	(12,649)	121,399	906,164
Property Pooled Vehicles	121,393	1,284	-	(722)	121,955
Property	266,603	34,340	-	(12,868)	288,075
	2,924,319	**627,221**	**(490,931)**	**335,413**	**3,396,022**
Forward Foreign Exchange	-	158,842	(158,048)	(544)	250
	2,924,319	**786,063**	**(648,979)**	**334,869**	**3,396,272**
Cash deposits	137,382				81,269
	3,061,701				**3,477,541**

Reconciliation of Opening and Closing Values of Investments 2011/12

	Value at 1 April 2011 £000	Purchases at Cost £000	Proceeds of Sales £000	Change in Market Value £000	Value at 31 March 2012 £000
Fixed Interest Securities	266,901	227,091	(226,015)	20,034	288,011
Index Linked Securities	62,471	21,205	(15,861)	7,529	75,344
Equities	1,470,613	162,035	(135,803)	(56,973)	1,439,872
Pooled Investment Vehicles	663,107	84,521	(23,074)	8,542	733,096
Property Pooled Vehicles	122,737	8,801	(401)	(9,744)	121,393
Property	272,017	28,500	(32,003)	(1,911)	266,603
	2,857,846	**532,153**	**(433,157)**	**(32,523)**	**2,924,319**
Forward Foreign Exchange	-	27,113	(26,648)	(465)	-
	2,857,846	**559,266**	**(459,805)**	**(32,988)**	**2,924,319**
Cash deposits	132,186				137,382
	2,990,032				**3,061,701**

For Forward Foreign Exchange contracts, the purchase cost and sale proceeds represent the sterling value of the currency purchases and sales at the settlement dates specified in the contracts.

Transaction costs are included in the cost of purchases and sale proceeds. The costs charged directly to the fund, such as fees, commissions and stamp duty, amounted to £1,844,156 in 2012/13 (£1,601,583 in 2011/12). In addition, indirect costs are incurred through the bid-offer spread on investments. This amount is not separately provided.

(c) Management Arrangements

An analysis of the investment management arrangements as at the Net Assets Statement date is shown below:

	31 March 2012 £000	%	31 March 2013 £000	%
In-house	1,118,010	36.5%	1,216,945	35.0%
Schroder Investment Management	785,415	25.7%	950,260	27.3%
Kames Capital	420,908	13.7%	467,034	13.4%
Aberdeen Property Investors	302,748	9.9%	323,414	9.3%
Legal & General	213,230	7.0%	268,870	7.7%
RWC Partners Ltd	116,522	3.8%	141,751	4.1%
Standard Life	52,828	1.7%	52,019	1.5%
Keills	25,222	0.8%	26,551	0.8%
Governance 4 Owners	12,305	0.4%	13,247	0.4%
Martin Currie	14,513	0.5%	17,450	0.5%
Total	**3,061,701**	**100.0%**	**3,477,541**	**100.0%**

(Note: RWC Partners Ltd was formerly Hermes Asset Management)

(d) Asset Allocation

The asset allocation of the Fund as at the Net Assets Statement date is shown below:

	31 March 2012 £000	%	31 March 2013 £000	%
UK Fixed Interest	233,950	7.6%	237,785	6.8%
Overseas Fixed Interest	54,061	1.7%	85,770	2.5%
Index Linked Securities	75,344	2.5%	80,738	2.3%
UK Equities	1,048,940	34.3%	1,211,834	34.8%
Overseas Equities:				
US	358,487	11.7%	423,694	12.2%
Europe	272,702	8.9%	337,287	9.7%
Japan	97,805	3.2%	102,688	3.0%
Pacific Basin	125,443	4.1%	151,890	4.4%
Emerging Markets	130,544	4.2%	198,907	5.7%
Global	14,513	0.5%	17,450	0.5%
UK Property	299,023	9.8%	322,672	9.3%
Overseas Property	88,974	2.9%	87,358	2.5%
Private Equity	66,979	2.2%	75,209	2.2%
Multi-Asset	57,554	1.9%	62,740	1.8%
Forward Foreign Exchange	-	-	250	-
Cash	137,382	4.5%	81,269	2.3%
Total	**3,061,701**	**100.0%**	**3,477,541**	**100.0%**

(e) Property

Direct property is shown at open market value (as defined by the International Valuation Standards Committee) as determined by Savills Commercial Limited. The analysis of property is:

	31 March 2012 £000	31 March 2013 £000
Freehold	259,653	268,375
Leasehold more than 50 years	6,950	19,700
	266,603	**288,075**
Original Value	279,458	313,798

(f) Analysis of Pooled Investment Vehicles

The underlying economic exposure of pooled investment vehicles is shown below:

	31 March 2012 £000	31 March 2013 £000
UK Equities	110,453	134,421
Overseas Equities:		
US	138,762	158,177
Japan	62,074	62,525
Europe	53,127	71,198
Pacific Basin	125,443	151,890
Emerging Markets	106,336	172,554
Global	14,513	17,450
UK Property	32,420	34,597
Overseas Property	88,974	87,358
Private Equity	64,834	75,209
Multi-Asset	57,553	62,740
Total	**854,489**	**1,028,119**

(g) Private Equity Funds

The Fund has made commitments to a number of private equity funds. The original commitment amounts are shown below in the fund currencies.

Funds	**Currency**	**Commitment** millions
Wilton Private Equity Fund LLC	USD	14
Pantheon Europe Fund III	EUR	10
East Midlands Regional Venture Capital Fund	GBP	5
Coller International Partners IV	USD	10
Schroders Private Equity Fund of Funds III	EUR	22
DCM Private Equity Fund II	USD	18
Pantheon Europe Fund V	EUR	15
Coller International Partners V	USD	18
Catapult Growth Fund LP	GBP	4
Altius Associates Private Equity Fund	USD	10
Partners Group Secondary 2008	EUR	13
DCM Private Equity Fund III	USD	16
Coller International Partners VI	USD	16
Altius Associates Private Equity Fund II	USD	15
Partners Group Global Infrastructure	EUR	12

These commitments are drawn by the funds over time as investments are made in underlying companies. The undrawn commitment as at 31 March 2013 was £53.1 million (£21.2 million at 31 March 2012). From the funds above, the following were new commitments made during 2012/13:

	Currency	**Commitment** millions
DCM Private Equity Fund III	USD	16
Coller International Partners VI	USD	16
Altius Associates Private Equity Fund II	USD	15
Partners Group Global Infrastructure	EUR	12

(h) Analysis of derivatives

Open Forward Foreign Exchange contracts

Settlement	Currency Bought	Local Value 000	Currency Sold	Local Value 000	Asset Value £000	Liability Value £000
Up to one month	GBP	10,500	USD	(15,946)	-	(2)
Up to one month	GBP	13,436	USD	(20,000)	263	-
Up to one month	GBP	9,661	EUR	(11,000)	358	-
Up to one month	USD	31,325	GBP	(21,000)	-	(368)
					621	**(371)**
Net forward foreign exchange contracts at 31 March 2013						**250**

There were no open forward foreign exchange contracts at 31 March 2012.

10. Contingent Liabilities

The fund has 15 private equity funds which have undrawn commitments as at 31 March 2013 of £53.1m (£21.3m at 31 March 2012).

11. Other Investment Balances and Liabilities

	31 March 2012 £000	31 March 2013 £000
Other investment balances		
Outstanding investment transactions	42	1,760
Investment income	14,274	14,600
	14,316	**16,360**
Investment Liabilities		
Outstanding investment transactions	(310)	(536)
Investment income	(2,922)	(2,621)
	(3,232)	**(3,157)**

12. Current Assets and Liabilities

	31 March 2012 £000	31 March 2013 £000
Current assets		
Contributions due from employers	11,814	17,297
Other	3,180	1,184
	14,994	**18,481**
Current Liabilities		
Payments in advance	(4,651)	(3,261)
Sundry creditors	(926)	(1,455)
Other	(9,905)	(8,433)
	(15,482)	**(13,149)**

13. Financial Instruments

(a) The various financial instruments held by the Fund are valued at fair value. The following tables analyse the fair value of financial assets and liabilities by asset class.

	31 March 2013			
	Designated at Fair Value through profit and loss £000	**Loans and Receivables £000**	**Financial liabilities at amortised cost £000**	**Totals £000**
Financial Assets				
Fixed Interest Securities	323,555	-	-	323,555
Index Linked Securities	80,739	-	-	80,739
Equities	1,675,534	-	-	1,675,534
Pooled Investment Vehicles	906,164	-	-	906,164
Property Pooled Vehicles	121,955	-	-	121,955
Forward Foreign Exchange	621	-	-	621
Cash deposits	-	81,269	-	81,269
Other investment balances	-	16,360	-	16,360
Current Assets	-	18,481	-	18,481
	3,108,568	**116,110**	**-**	**3,224,678**
Financial Liabilities				
Investment Liabilities	-	-	(3,157)	(3,157)
Current Liabilities	-	-	(13,149)	(13,149)
	-	**-**	**(16,306)**	**(16,306)**
	3,108,568	**116,110**	**(16,306)**	**3,208,372**

	31 March 2012			
	Designated at Fair Value through profit and loss £000	**Loans and Receivables £000**	**Financial liabilities at amortised cost £000**	**Totals £000**
Financial Assets				
Fixed Interest Securities	288,011	-	-	288,011
Index Linked Securities	75,344	-	-	75,344
Equities	1,439,872	-	-	1,439,872
Pooled Investment Vehicles	733,095	-	-	733,095
Property Pooled Vehicles	121,393	-	-	121,393
Cash deposits	-	137,382	-	137,382
Other investment balances	-	14,316	-	14,316
Current Assets	-	14,994	-	14,994
	2,657,715	**166,692**	**-**	**2,824,407**
Financial Liabilities				
Investment Liabilities	-	-	(3,232)	(3,232)
Current Liabilities	-	-	(15,482)	(15,482)
	-	**-**	**(18,714)**	**(18,714)**
	2,657,715	**166,692**	**(18,714)**	**2,805,693**

No financial assets were reclassified during the accounting period.

(b) Valuation of financial instruments carried at fair value

The valuation of financial instruments has been classified into three levels according to the quality and reliability of information used to determine fair values.

Level 1	Fair values derived from quoted market price. - this includes all quoted equity, fixed interest and index linked instruments.
Level 2	Fair values derived from valuation techniques based significantly on observable inputs. - this includes all pooled property investments.
Level 3	Fair values derived from valuation techniques where at least one significant input is not based on observable market data. - this includes unlisted shares and investments in private equity funds.

As at 31 March 2013	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial Assets				
Fair value through profit and loss	2,909,408	121,955	77,205	3,108,568
Loans and receivables	116,110			116,110
Total	**3,025,518**	**121,955**	**77,205**	**3,224,678**
Financial Liabilities				
Fair value through profit and loss	-	-	-	-
Financial liabilities	(16,306)	-	-	(16,306)
Total	**(16,306)**	**-**	**-**	**(16,306)**
Net	**3,009,212**	**121,955**	**77,205**	**3,208,372**

As at 31 March 2012	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial Assets				
Fair value through profit and loss	2,469,342	121,394	66,979	2,657,715
Loans and receivables	166,692	-	-	166,692
Total	**2,636,034**	**121,394**	**66,979**	**2,824,407**
Financial Liabilities				
Fair value through profit and loss	-	-	-	-
Financial liabilities	(18,714)	-	-	(18,714)
Total	**(18,714)**	**-**	**-**	**(18,714)**
Net	**2,617,320**	**121,394**	**66,979**	**2,805,693**

(c) Nature and extent of risks arising from financial instruments

The aims of the Fund are to:

- manage employers' liabilities effectively
- ensure that sufficient resources are available to meet all liabilities as they fall due
- maximise the returns from investments within reasonable risk parameters
- enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the taxpayers, scheduled, resolution and admitted bodies.

The key risks to the achievement of these aims, as well as measures to mitigate those risks, are set out in the various Fund policies (available at www.nottspf.org.uk) including:

- Statement of Investment Principles
- Funding Strategy Statement
- Governance Compliance Statement
- Risk Management Strategy and Risk Register

The Risk Register identifies the highest risks as arising from:

- Significant variations from assumptions used in the actuarial valuation
- Fund assets assessed as insufficient to meet long term liabilities.

The Fund's primary risk is therefore that its assets fall short of its long term liabilities. The Funding Strategy Statement aims:

- 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 requirement to maintain as nearly constant employer contribution rates as possible
- to take a prudent longer-term view of funding those liabilities

The most significant effect on the funding level arises from changes in the discount rate used by the actuaries. The sensitivity analysis below shows the impact of a movement of 0.1% in the discount rate.

Adjustment to discount rate	0.1%	0.0%	(0.1%)
Present Value of Total Obligation (£000)	5,351,569	5,476,127	5,604,384

The Fund deficit at the last triennial valuation was £520 million. With no other change in assumptions, an increase in the discount rate of just over 0.4% would reduce the deficit to nil.

As contribution income currently exceeds benefit payments and the Fund receives significant investment income, it is unlikely that assets will have to be realised in order to meet pension benefits. This allows the Fund to implement a long term investment strategy and minimise the impact of short term fluctuations in investment and currency markets. The strategy, and the assumptions that underpin it, are reviewed on a regular basis and cash flows are monitored closely to ensure there is sufficient liquidity to meet forecast cash flows.

The investment strategy is aimed at achieving best returns in line with the requirements of the triennial valuation whilst minimising risk and overall variability in future employers' contribution rates. A key part of managing the investment risk is by ensuring an adequate number of suitably qualified investment managers and by requiring managers to hold a diversified spread of assets. The level of risk in the equities block is managed by a balance between passive and active management.

Policies are reviewed regularly to reflect changes in activity and in market conditions. Responsibility for reviewing and revising the policies rests with the Nottinghamshire Pension Fund Committee.

14. Members Additional Voluntary Contributions

The Nottinghamshire Fund provides an additional voluntary contribution (AVC) scheme to enable members to purchase additional benefits. Contributions are paid over to, and invested separately by, the two scheme providers, Prudential and Scottish Widows. The contributions are not included in the Fund's accounts in accordance with regulation 4(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. The value of the separately invested AVCs is shown below:

	31 March 2012 £000	31 March 2013 £000
Prudential	27,289	25,611
Scottish Widows	3,058	3,254
	30,347	**28,865**

15. Related Party Transactions

Under IAS 24, a party is related to an entity if:

- the party is a member of the key management personnel;
- the party is a post-employment benefit plan for the benefit of employees of the entity.

The purpose of related party disclosures is to provide information on transactions and balances that could have an effect on the operations or financial position of an entity. For example, related parties may enter into transactions that unrelated parties would not and transactions between related parties may not be made at the same amounts as between unrelated parties.

Disclosures are required for:

- the nature of the related party relationship
- key management personnel compensation
- information about the transactions and outstanding balances necessary for an understanding of the potential effect of the relationship on the financial statements.

Nottinghamshire County Council is the administering authority for the Local Government Pension Scheme (LGPS) within Nottinghamshire and is one of the major employers within the scheme. Information regarding key management personnel is provided within the main accounts of Nottinghamshire County Council. Members and officers of the Council involved in managing the Fund are allowed to be members of the LGPS. All transactions between Nottinghamshire County Council and the Fund and all benefit payments from the Fund are in accordance with the regulations governing the LGPS. There are no transactions therefore that are made on a different basis from those with non-related parties.

KPMG

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Report to those charged with governance (ISA 260) 2012/13

Nottinghamshire Pension Fund

11 September 2013

Contents

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Report sections

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

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Neil Bellamy, the appointed engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 03034448330.

Section one

Introduction

This report summarises the key issues identified during our audit of Nottinghamshire Pension Fund's (the Fund's) financial statements for the year ended 31 March 2013.

Scope of this report

The Audit Commission's *Code of Audit Practice* requires us to summarise the work we have carried out to discharge our statutory audit responsibilities together with any governance issues identified and report to those charged with governance (in this case the Audit Committee). We are also required to comply with International Standard on Auditing ('ISA') 260 which sets out our responsibilities for communicating with those charged with governance.

This report meets both these requirements. It summarises the key issues identified during our audit of the Fund's financial statements for the year ended 31 March 2013.

Some of our responsibilities under ISA 260 relate to Nottinghamshire County Council ('the Authority') as administering authority as a whole and are discharged through our reporting to the Authority's Audit Committee. This includes:

- Declaring our independence and objectivity;
- Obtaining management representations; and
- Reporting matters of governance interest, including our audit fees.

Audit of the pension fund

As with the main audit of the Authority, our audit of the Fund follows a four stage audit process.

Planning → Control Evaluation → Substantive Procedures → Completion

This report focuses on the second and third stages of the process: control evaluation and substantive procedures. Our on site work for these took place in two tranches during March 2013 (interim audit) and July 2013 (year end audit).

We carried out the following work:

Control Evaluation

- Evaluate and test selected controls over key financial systems
- Review accounts production process
- Review progress on critical accounting matters

Substantive Procedures

- Plan and perform substantive audit procedures
- Conclude on critical accounting matters
- Identify audit adjustments

Structure of this report

This report is structured as follows:

- Section two summarises the headline messages.
- Section three sets out the findings from our audit work on the Fund's accounts in more detail.

Acknowledgements

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

Headlines

This table summarises the headline messages. The remainder of this report provides further details on each area.

Proposed audit opinion	We 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 by 30 September 2013. At the date of this report our audit of the Fund's financial statements is substantially complete. Our remaining completion procedures are carried out jointly with those for the main County Council audit. This includes obtaining a signed management representation letter, which covers the financial statements of both the Authority and the Fund.
Audit adjustments	We are pleased to report that our audit of the Fund's financial statements did not identify any material adjustments. The Authority made a small number of non trivial adjustments, most of which were of a presentational nature.
Accounts production and audit process	The Authority has good processes in place for the production of the Fund's financial statements and good quality supporting working papers. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales. We have worked with Officers throughout the year to discuss the specific risk areas for this year's audit. The Authority addressed the issues appropriately.
Control environment	Controls over the Fund's key financial systems are sound. We did not identify any specific issues we wish to highlight to you.

Proposed opinion and audit differences

We have identified no issues in the course of the audit that are considered to be material.

We 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 by 30 September 2013.

Proposed audit opinion

Subject to our final checks and review, we anticipate issuing an unqualified audit opinion following approval of the Statement of Accounts by the Audit Committee on 11 September 2013.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you which are not considered to be trivial in nature. 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.

We did not identify any material 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 the United Kingdom 2012/13 ('the Code')*. We understand that the Authority will be addressing these where significant.

Completion

At the date of this report, our audit of the Fund's financial statements is substantially complete.

Before we can issue our opinion we require a signed management representation letter. The representations in relation to the Fund will be included in the Authority's representation letter a draft of which is included in the Authority's ISA 260 report.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Fund's financial statements. A full declaration of our independence is set out in the main *ISA 260 Report* for the Authority.

Annual Report

The Pension Fund Annual Report has not been prepared yet and we are yet to confirm that:

- it complies with the requirements of the Local Government Pension Scheme (Administration) Regulations 2008; and
- the financial and non-financial information it contains is not inconsistent with the financial information contained in the audited financial statements.

We anticipate being able to complete our required work on the Pension Fund Annual Report before issuing our opinion on the Pension Fund Statement of Accounts.

Accounts production and audit process

The Authority has good processes in place for the production of the Fund's financial statements and good quality supporting working papers.

Officers dealt efficiently with audit queries and the audit process could be completed within the planned timescales.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the significant qualitative aspects of the accounting practices and financial reporting relating to the Fund. We have also assessed the Authority's process for preparing the Fund's financial statements and its support for an efficient audit, our findings are set out below.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	The Authority has good financial reporting arrangements over the Fund's financial statements in place. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 26 June 2013.
Quality of supporting working papers	Our 'Prepared by Client' list, which we issued at the planning stage of the audit and discussed with Simon Cunnington, set out our working paper requirements for the audit. The quality of working papers provided met the standards specified in our 'Prepared by Client' list.
Response to audit queries	Officers resolved our audit queries in a reasonable time. We worked with the Authority to plan our work around staff availability in order to effectively deliver the audit.

Control Environment

Controls over the Fund's key financial systems are sound.

During March 2013 we completed our control evaluation work. We did not issue an interim report as there were no significant issues arising from this work. For completeness we reflect on key findings from this work.

Organisational and IT control environment

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit. We therefore obtain an understanding of the Authority's overall control environment and determine if appropriate controls have been implemented.

The Authority also relies on information technology (IT) to support both financial reporting and internal control processes. In order to satisfy ourselves that we can rely on the use of IT, we test controls over access to systems and data, system changes, system development and computer operations.

Most of the controls we look at do not just relate to the Fund but the Authority as a whole.

We found that your organisational and IT control environment is effective overall.

Controls over key financial systems

Where we have determined that this is the most efficient audit approach to take, we test selected controls that address key risks within the financial systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Based on the work of your internal auditors, and our own work on controls over the year end process, the controls over the financial systems are sound.

Work on behalf of admitted body auditors

The auditors of admitted bodies requested us to complete specific work on controls operated by the Fund on behalf of the admitted bodies over certain data used by actuaries in order to determine the pensions liabilities and related disclosures for the admitted bodies.

Our work did not identify any specific issues.

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Nottinghamshire County Council

Report to Nottinghamshire Pension Fund Committee

24 September 2013

Agenda Item: 6

REPORT OF SERVICE DIRECTOR – FINANCE & PROCUREMENT

CALL FOR EVIDENCE ON THE FUTURE STRUCTURE OF THE LOCAL GOVERNMENT PENSION SCHEME

Purpose of the Report

1. To seek the Nottinghamshire Pension Fund Committee's approval to the proposed response to the recent call for evidence on the future structure of the Local Government Pension Scheme.

Information and Advice

2. The government has launched a call for evidence into ways of significantly reducing the costs of the Local Government Pension Scheme (LGPS) by increasing fund co-operation, transparency and accountability to taxpayers. Responses to the call for evidence will help inform a consultation due to be published in the early autumn on a number of broad principles for change aimed at improving the efficiency and cost-effectiveness of the scheme.

3. The call for evidence was launched by Brandon Lewis MP at the NAPF local authority conference in May 2013. He stated that the consultation 'will not set out some pre-determined solution to what is undoubtedly a complex and contentious issue' but also declared that he was 'not wedded to the existing number of 89 funds in England and Wales'.

4. The document jointly issued by the Department for Communities and Local Government and the Local Government Association is attached along with the proposed response from the Nottinghamshire Fund.

Statutory and Policy Implications

5. This report has been compiled after consideration of implications in respect of finance, the public sector equality duty, human resources, crime and disorder, human rights, the safeguarding of children, sustainability and the environment and those using the service and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

RECOMMENDATION/S

1) That approval be given to the proposed response to the call for evidence on the future structure of the Local Government Pension Scheme.

Name of Report Author: Simon Cunnington
Title of Report Author: Senior Accountant – Pensions & Treasury Management

For any enquiries about this report please contact: Simon Cunnington

Constitutional Comments (NAB 13.09.12)

6. The Nottinghamshire Pension Fund Committee has authority to approve the recommendation set out in this report by virtue of its terms of reference.

Financial Comments (SRC 12/09/13)

7. There are no direct financial implications arising from the report.

Background Papers

None

Call for evidence on the future structure of the Local Government Pension Scheme

Background

In 2010, the Government commissioned Lord Hutton to chair the Independent Public Service Pensions Commission. The purpose of the Commission was to review public service pensions and to make recommendations on how they could be made sustainable and affordable in the long term, while being fair to both taxpayers and public sector workers. Lord Hutton's final report was published on 10 March 2011. Among its recommendations, the report made clear that the benefits of co-operative working between local government pension scheme funds and achieving administration efficiencies more generally should investigated further. The Local Government Pension Scheme currently costs local taxpayers £6billion a year in employer contributions.

Recommendation 23*: Central and local government should closely monitor the benefits associated with the current co-operative projects within the LGPS, with a view to encouraging the extension of this approach, if appropriate, across all local authorities. Government should also examine closely the potential for the unfunded public service schemes to realise greater efficiencies in the administration of pensions by sharing contracts and combining support services, including considering outsourcing.*

Lord Hutton went on to comment about the need for change and improved scheme data. At paragraph 6.1 he said:

In its interim report, the Commission noted the debate around public service pensions is hampered by a lack of consensus on key facts and figures and a lack of readily available and relevant data. There are also inconsistent standards of governance across schemes. Consequently it is difficult for scheme members, taxpayers and commentators to be confident that schemes are being effectively and efficiently run. It also makes it more difficult to compare between and within schemes and to identify and apply best practice for managing and improving schemes.

On 16 May 2013, the LGA and DCLG held a roundtable event on the potential for increased co-operation within the Local Government Pension Scheme, including the possibility of structural change to the current 89 funds. 25 attendees represented administering authorities, employers, trade unions, the actuarial profession and academia.

The roundtable aimed to bring objectivity and transparency to the subject through open debate. There was a full discussion of the possible aims of reform and the potential benefits of structural change, together with the further work needed to provide robust evidence to support emerging options. The meeting focused on the issues to be addressed by reform rather than the detailed arguments for any of the potential ways forward that have been proposed.

The roundtable heard about the projects being undertaken to look at the options for structural reform of the Scheme in London and Wales and considered the range and relative priorities of the desired outcomes of reform, the data requirements for determining a start point and target and the next steps for delivering those outcomes.

On 22 May at the National Association of Pension Funds' local authority conference, the Local Government Minister Brandon Lewis said:

I am determined that we make progress and make it as quickly as reasonably possible. I can therefore announce this morning, that we will consult later in the year on a number of broad principles for change. This will be your opportunity to tell us what reforms could be made to both help improve your investment performance and reduce your fund management costs.

The consultation will not set out some pre-determined solution to what is undoubtedly a complex and contentious issue. I am neither ruling anything in nor ruling anything out at this stage. However, the clear message from me this morning is that I am not wedded to the existing number of 89 funds in England and Wales. If it takes a smaller number of funds to improve the efficiency and cost-effectiveness of the scheme, I shall not shy away from pursuing that goal.

I have talked a fair amount about the need for robust data to inform decisions. I am therefore working with the LGA and others to launch a call for evidence, which will both inform our consultation and help all involved formulate their views in response to the consultation.

You will be aware that work is well underway to establish a shadow national pensions board for the Scheme. I have met with the LGA and local government trades unions on several occasions to discuss the sort of work that I would like the board to undertake.

This document sets out the call for evidence from DCLG and the LGA, working with the Shadow Scheme Advisory Board, and explains how it will feed into the forthcoming consultation.

The call for evidence

At the roundtable, the following high level and secondary objectives for structural reform were proposed:

<u>High level objectives</u>

1. Dealing with deficits
2. Improving investment returns

<u>Secondary objectives</u>

1. To reduce investment fees
2. To improve the flexibility of investment strategies

3. To provide for greater investment in infrastructure
4. To improve the cost effectiveness of administration
5. To provide access to higher quality staffing resources
6. To provide more in-house investment resource

The roundtable also agreed that, although there is a wide range of data available on Local Government Pension Scheme funds, it is currently widely dispersed and would benefit from enhancement, collation and further analysis. It also considered how best to achieve a high level of accountability to local taxpayers, particularly if services are to be shared or funds merged.

In your response to this call for evidence, it would be helpful if you could have particular (although not exclusive) regard to the following questions and provide evidence in the form of annexes to support your answers.

Question 1 – How can the Local Government Pension Scheme best achieve a high level of accountability to local taxpayers and other interested parties - including through the availability of transparent and comparable data on costs and income - while adapting to become more efficient and to promote stronger investment performance.

Question 2 – Are the high level objectives listed above those we should be focussing on and why? If not, what objectives should be the focus of reform and why? How should success against these objectives be measured?

Question 3 – What options for reform would best meet the high level objectives and why?

Question 4 – To what extent would the options you have proposed under question 3 meet any or all of the secondary objectives? Are there any other secondary objectives that should be included and why?

Question 5 – What data is required in order to better assess the current position of the Local Government Pension Scheme, the individual Scheme fund authorities and the options proposed under this call for evidence? How could such data be best produced, collated and analysed?

Timetable

Responses to this call for evidence should be submitted in electronic form to Victoria Edwards at: LGPSReform@communities.gsi.gov.uk

The closing date for submissions is 27 September 2013.

The submissions will then be analysed by DCLG and the LGA, working with the Shadow Scheme Advisory Board. You may be asked to provide further clarification and/or evidence to support your answers during that process.

The analysis of submissions will then inform a formal consultation on the options for change to be published by DCLG in the early autumn.

This matter is being dealt with by:
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Nottinghamshire County Council

Victoria Edwards
LGPS Reform
Communities & Local Government

24 September 2013

Call for evidence on the future structure of the Local Government Pension Scheme
Response from Nottinghamshire County Council Pension Fund

The call for evidence issued by the Department for Communities & Local Government and the Local Government Association posed five questions seeking to gain views on accountability, deficits and investment returns within the Local Government Pension Scheme (LGPS). The full response to the call for evidence as approved by the Nottinghamshire Pension Fund Committee is attached and key points are highlighted below.

Accountability to local taxpayers and other interested parties
The LGPS already has a very high level of accountability to local taxpayers, fund employers and member representatives and this will be increased further by the governance changes being introduced by the Public Service Pensions Act 2013. Merging funds will inevitably reduce accountability as governance is removed from the communities in which the fund operates.

The Nottinghamshire fund, in common with many, already publishes a whole range of documentation and data. This should be collated centrally and presented in one place and the new Scheme Advisory Board should play a key role in collating and analysing this data across the LGPS. Comparability between funds could be improved by better pension fund specific accounting guidance but, as each fund has to interpret the guidance to meet its own particular circumstances, full comparability will never be achieved (even with merged funds).

Investment performance and deficits
The current focus on fund deficits is fundamentally flawed and is not helpful to the long term sustainability of pensions. Deficits are estimated and the biggest impact comes from the discount rate used by the actuaries. A movement of just 0.1% in the discount rate changes the Nottinghamshire fund's liabilities by over £125 million. Across the LGPS as a whole, such movements in liabilities would far outweigh any cost savings that can be achieved through merged funds.

Reform should focus on finding a better way to assess the financial position of funds and their ability to pay future pensions.

Investment performance will be volatile so should be viewed over a long term horizon (eg 10, 20 or more years). A sensible investment strategy, simply executed is more likely to out-perform over the long term than a complex strategy. The main change needed is to encourage the focus of reporting and decision-making to be far less on short term returns and more on the medium to long term, both by funds themselves and by asset managers. The evidence of the benefits of in-house management should be discussed more widely.

Simpler investment strategies will inevitably mean lower fees. Collaboration between funds is already providing savings on many services and may also act to reduce investment fees. This would be improved further with central assistance from the Government Procurement Service (GPS). Closer liaison with actuaries and fund employers to manage risks will help to maximise contribution income and this will potentially far outweigh the cost of additional resources to be able to do this effectively. Merging funds will not reduce the number of employers and will make close liaison more difficult.

Next Steps

The call for evidence acknowledges the need to provide robust evidence to support options for change. Before considering merging funds proper evidence should be collated to determine whether 'bigger means better' in terms of investment returns. Analysis should also be carried out of the correlation of returns by manager to assess the risk of all funds underperforming at the same time. Having locally administered funds has the benefit of diversification of investment risk which may protect the LGPS as a whole compared to super-funds.

The new Scheme Advisory Board should play a key role in collating and analysing data in order to report openly about the advantages **and** disadvantages of any proposals for change before any decision is made on the future structure of the LGPS.

Yours faithfully,

Cllr Stella Smedley MBE JP
Chair – Nottinghamshire Pension Fund Committee

Appendix 3 to Item 6

Call for evidence on the future structure of the Local Government Pension Scheme

Response from Nottinghamshire County Council Pension Fund

Question 1 – How can the Local Government Pension Scheme best achieve a high level of accountability to local taxpayers and other interested parties – including through the availability of transparent and comparable data on costs and income - while adapting to become more efficient and to promote stronger investment performance.

High level of accountability to local taxpayers and other interested parties
The LGPS already has a very high level of accountability to local taxpayers through the quasi-trustee role of locally elected councillors. The level of involvement by other employer and member representatives is also high in the majority of funds including Nottinghamshire. The governance changes being introduced by the Public Service Pensions Act 2013 will increase this accountability further. Increased central co-ordination and oversight of governance arrangements by the Pensions Regulator or scheme advisory board would ensure that the high standards that exist across the majority of the LGPS can be widened to include all funds.

Merging funds into larger funds will inevitably reduce the accountability to local taxpayers as there would be a greatly reduced role for locally elected councillors. The governance arrangements for a merged fund are, as yet, unclear but they are unlikely to involve the same degree of oversight by persons directly elected by taxpayers. Accountability to the employers would also reduce as governance is removed from the communities in which these employers operate.

Availability of transparent and comparable data on costs and income
There is a huge amount of data already available on the LGPS. Each fund is required to produce accounts and an annual report as well as publish a range of policy statements. Increasingly, authorities are publishing these on-line – the Nottinghamshire fund website currently has annual reports going back to 2002/03 and the last three triennial valuation reports (dating back to 2004). Annual reports are also submitted each year to both CIPFA and the Department for Communities and Local Government (CLG). These could easily therefore be published in a central location to make access even easier.

Pension fund accounts are currently produced under the CIPFA Code on the basis of International Financial Reporting Standards (IFRS). One of the main aims of IFRS is to increase comparability of accounting statements. However, a greater involvement by CIPFA in the debates around pension fund accounting and more emphasis on pension fund specific guidance (rather than just example accounts) would help to increase this comparability. It must be remembered, however, that each fund has a different funding position, membership profile and, consequently, investment strategy and so full comparability will never be achieved. This would still not be achieved with merged funds as each super-fund would still be required to interpret the accounting guidance to meet the individual needs of that fund.

Adapting to become more efficient and to promote stronger investment performance
The LGPS, in common with the whole of local government, is constantly adapting to become more efficient. Collaboration between funds in sharing information and in procurement is increasing rapidly and the framework agreements currently in place have been well received. These frameworks, and the ongoing work to produce new agreements, has so far relied on the goodwill and resources of a few funds. There appears to be no central assistance, for instance, from the Government Procurement Service (GPS). Pension fund procurement requirements are very different from the those of the rest of local government (and even the wider public sector) and this should be recognised by the GPS.

It is important to remember that investment performance is not necessarily driven by how cheap (or expensive) the management arrangements are or how efficiently the investment services were procured. Investment performance relies to a large extent on existing market conditions and current and future economic situations. This means that performance will be volatile so should therefore be viewed over a long term horizon (eg 10, 20 or more years). The WM Company has recently produced research that indicates that simpler investment management structures tend to out-perform over the long term. The Nottinghamshire Fund's performance has been good partly because we have not constantly switched strategies and managers. Both need time to demonstrate whether they are working, particularly as the costs involved in changing can be high.

Question 2 – Are the high level objectives listed above those we should be focussing on and why? If not, what objectives should be the focus of reform and why? How should success against these objectives be measured?

Are the high level objectives listed above those we should be focussing on and why? If not, what objectives should be the focus of reform and why?
The aims of the Nottinghamshire fund are to:

- enable employer contribution rates to be kept as nearly constant as possible and at reasonable cost to the taxpayers, scheduled, resolution and admitted bodies
- manage employers' liabilities effectively
- ensure that sufficient resources are available to meet all liabilities as they fall due
- maximise the returns from investments within reasonable risk parameters

These aims clearly encompass within them the desire to 'deal with deficits' and 'improve investment returns'. This demonstrates that we are already focusing on the high level objectives stated as part of day to day business.

It is necessary to note that deficits are estimated and, because the cashflows involved are over a considerably long time, the biggest impact comes from the discount rate used by the actuaries (which is itself determined from a variety of assumptions). Sensitivity analysis carried out by the actuaries shows that, for Nottinghamshire, a movement of just 0.1% in the discount rate changes the fund's liabilities by over £125 million. As one of the main components of the discount rate, increasing bond yields could, at a stroke, wipe out the deficit. Across the LGPS as a whole, such movements in liabilities would far outweigh any cost savings that can be achieved through merged funds.

Deficits are therefore only one indicator of a fund's position. Equally important is ensuring sufficient cashflow to pay pensions. Reform should focus on finding a better way to assess the financial position of funds and their ability to pay future pensions.

How should success against these objectives be measured?
A successful pension fund is one that can pay pensions as they fall due at reasonable cost to employees and employers (and, by extension, taxpayers for a public service scheme). The key to measuring success is therefore establishing a reasonable method of assessing a fund's ability to pay future pensions. Current discussion and reporting focuses almost exclusively on the actuarial calculation of liabilities (and consequent deficit). This approach is fundamentally flawed as this 'calculation' is an estimate based on a number of assumptions and is not helpful to the long term sustainability of pensions. The result of this focus can clearly be seen in the private sector where very few defined benefit schemes exist leaving high levels of risk and uncertainty around pension provision. Ultimately this will place extra burdens on tax payers through additional state pension and benefit payments.

Question 3 – What options for reform would best meet the high level objectives and why?

Dealing with deficits
It is necessary to change the triennial valuation priorities to focus on a fund's real ability to pay pensions over the short, medium and long term. Focusing on one liability figure, affected hugely by the assumptions within the discount rate, is unhelpful and creates unnecessary concern within the wider public. Pension funding is not a simple issue and shouldn't be treated as such.

IFRS is currently being challenged as being unsuitable for accounting for banks. International Accounting Standard 19 (IAS19 Employee Benefits) is equally unsuitable for reporting pension liabilities (particularly for public sector schemes where sponsor risk is negligible). The treatment and reporting of an employer's pension liability as if it were a trade creditor due to be paid within 30 days is wholly inappropriate for pension benefits payable over decades.

Closer liaison with actuaries and fund employers to manage risks and maximise income to the fund would be of huge benefit and this is something that Nottinghamshire, along with other funds, is already doing.

Improving investment returns
There is no secret formula to improve investment returns. As pointed out above, returns depend on a wide range of factors, mostly out of the direct control of even the biggest funds. Chasing 'flavour of the month' investment strategies and changing every year or two will not help to provide sufficient long term returns (and may dramatically increase costs). A sensible strategy, simply executed is far better than a complex strategy involving multiple managers in multiple asset classes. Esoteric investments dreamed up by asset managers and investment banks are more likely to create unintended consequences and cause massive damage to long term returns.

In-house investment may also improve long term returns as there will generally be less focus on short term gains and trends. Both of these approaches are backed up by evidence from WM.

The main change needed is to encourage the focus of reporting and decision-making to be far less on short term returns and more on the medium to long term, both by funds themselves and by asset managers. Responsible ownership will play a huge role in ensuring this happens and should therefore be encouraged.

Question 4 – To what extent would the options you have proposed under question 3 meet any or all of the secondary objectives? Are there any other secondary objectives that should be included and why?

To reduce investment fees

Simpler investment strategies inevitably mean lower fees:

- Managers feel far less able to charge high fees
- Trading costs may be lower
- Transition costs from one strategy to another will be lower

Collaboration between funds may act to reduce fees, although investment management is not ideally suited to framework agreements owing to the individual nature of investment mandates.

To improve the flexibility of investment strategies

Investment strategies designed to meet long term aims should not need to be changed regularly. If decision-making, monitoring and reporting focuses more on medium to long term performance, short term volatility can be weathered. Trends in performance can still be monitored to indicate problems with strategy or manager, allowing changes to be made where conditions have clearly altered.

To provide for greater investment in infrastructure

Whether to invest in infrastructure is a decision to be made on the basis of the valuation and the return requirements of each fund. An assumption that infrastructure is good for all funds is wrong. Regeneration is not a primary role of pension funds (although could have wider benefits to the fund if successful) and the risk/return profile of infrastructure investments must be considered.

To improve the cost effectiveness of administration

The key word here is 'effectiveness'. The whole purpose of the fund is to meet pension payments. Ensuring contributions are received from employers and liaising with employers through difficult periods will potentially far outweigh the cost of additional resources to be able to do this effectively. Merging funds will not reduce the number of employers and larger, regional funds may find it harder to liaise with employers as they will be further removed from the communities in which they are based.

To provide access to higher quality staffing resources
To provide more in-house investment resource
It should be recognised that the LGPS already has access to high quality staff resources. However, examining the medium to long term benefits of closer liaison with employers and of in-house investment management will allow a proper assessment of the cost of providing additional high quality staff. The evidence of the benefits of in-house management should be discussed more widely.

Question 5 – What data is required in order to better assess the current position of the Local Government Pension Scheme, the individual Scheme fund authorities and the options proposed under this call for evidence? How could such data be best produced, collated and analysed?

There is a huge amount of data already in existence for the LGPS. All funds have to produce policy statements, accounts and annual reports and the latter are already provided to CLG and (for the most part) CIPFA. All funds have to submit returns to CLG and the Office for National Statistics. The data should therefore be collated centrally and presented in one place.

Before considering creating regional funds (or any other form of merged fund) proper evidence should be collated to determine whether 'bigger means better' in terms of investment returns.

Analysis should also be carried out of the correlation of returns by manager to assess the risk of all funds underperforming at the same time. Having locally administered funds has the benefit of diversification of investment risk which may protect the LGPS as a whole compared to super-funds.

The new Scheme Advisory Board should play a key role in collating and analysing data in order to report openly about the advantages and disadvantages of any proposals for change.