

# London Borough of Hillingdon Pension Fund Annual Report 2017/18

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## CHAIRMAN'S FOREWORD

By the end of 2017/18 the Fund had grown to just over £1 billion, a record level for the Fund. Membership of the scheme also continued to increase over the previous year; however, by the end of the year active membership had fallen slightly. As a result, the Fund is seeing the scheme maturing with new contributions equivalent to monies paid out in benefits; making cash flow an ongoing focus for the Committee.

Monitoring the Fund's specific investments and its strategy has kept Committee busy over the last 12 months, particularly looking at opportunities to invest via the London Collective Investment Vehicle (LCIV); which is becoming business as usual for the Fund. The Fund moved its income focused investment from Newton into the LCIV pool managed by Epoch during 2017/18 generating further fee savings for the Fund from pooling investments. As of 31 March 2018, 52% of the Fund's assets were held with the LCIV compared to 41% at the end of 2016/17. We have taken active participation in the development of the LCIV to date with membership on the Joint Committee and on the Investment Advisory Committee. We are keen to see how the governance of the pool and investment offerings develop over the coming year as a result of a governance review recently carried out by the LCIV.

The Fund has a further layer of governance through the Pension Board where key focuses to date have related to improving and drafting policy documentation and in ensuring compliance with the Pension Regulator's code of practice. In 2017/18 we saw the Pensions Board complete its second self-assessment against the Pension Regulator's compliance checklist and agreement of actions for improvement. The board was restructured to give greater independence in November 2017; however, the new board configuration had yet to meet by March 2018.

The Fund has now seen a full year with the new administration arrangements in place, which is now undertaken by the pension team at Surrey County Council, with whom we have a collaborative working arrangement. The transfer from Capita was a major project and the Fund, along with Surrey, is still working through legacy historic cases, which were transferred; however, day-to-day activity and new cases have seen significantly improved key performance indicators, through contract management and the strong relationship with the teams.

The Committee and Fund have many challenges coming up, including a strategy to transition further towards a fully pooled position over the longer-term whilst also reducing fees. Other challenges will arise out of known and unknown political and economic challenges, including how to ensure the Fund continues to invest responsibly in changing worldviews and priorities. The Fund has a number of strategic changes lined up to reduce the Fund risk while continuing to match investment return to meet the agreed funding strategy.

Cllr Philip Corthorne  
Chairman Pensions Committee

# FUND GOVERNANCE and STATUTORY INFORMATION

## FUND GOVERNANCE

The London Borough of Hillingdon Pension Fund ('the Fund') is part of the Local Government Pension Scheme (LGPS). The benefits paid out and the regulations are set nationally, but the Fund is administered locally. As the Administering Authority, the London Borough of Hillingdon has legal responsibility for the effective management of the Fund. The Council delegates this responsibility to the Pensions Committee ('the Committee'), which is the formal decision making body for the Fund. The Corporate Director of Finance has delegated authority for the day-to-day running of the Fund. The local Pension Board ('the Board') was established in 2015 to assist the scheme manager in securing compliance with regulations relating to the governance and administration within the requirements set by the Pension Regulator.

### Pension Committee

The Pension Committee consists of five Councillor Members. During 2017/18 these were:



Councillor  
Philip Corthorne  
(Chairman)



Councillor  
Michael Markham  
(Vice-Chairman)



Councillor  
Peter Davis



Councillor  
Tony Eginton  
(Labour Lead)



Councillor  
Beulah East

The Committee meets quarterly to discuss investment strategy, legislative changes and developments that may affect the Fund, and to review the performance of the Fund Managers and the Fund Administrators. Committee training has been incorporated into these quarterly meetings to ensure that Committee Members

maintain their knowledge and skills at a sufficient level to enable them to discharge their duties in relation to the Fund.

### **Local Pension Board**

The London Borough of Hillingdon local Pension Board was established in 2015 and like the Committee met on a quarterly basis. The Board was reconfigured in November 2017 with a change to membership and terms of reference.

The members of the Board meetings during 2017/18 were:

#### ***Employer Representatives:***

Councillor David Simmonds (Chairman)  
Councillor Alan Chapman (Vice-Chairman)  
Councillor John Morse

#### ***Scheme Member Representatives:***

Venetia Rogers	Active Member
Andrew Scott	Active Member
Roger Hackett	Retired Member

The Board is not a decision making body, rather it has a compliance and scrutiny role to ensure the Pensions Committee complies effectively and efficiently with the code of practice on the governance and administration of public service pension schemes issued by the Pension Regulator. Additionally the Pension Board will help ensure that the London Borough of Hillingdon Pension Fund is managed and administered effectively and efficiently and complies with the code of practice.

### **Corporate Director of Finance**

Paul Whaymand in his role of Corporate Director of Finance has delegated responsibility for the day-to-day running of the Pension Fund.

## **FUND MANAGEMENT and ADVISORS**

The work of the Committee is supported by a number of officers, advisors and external managers.

### **Officers Responsible for the Fund**

The Pensions, Treasury and Statutory Accounts team ensures that both the Committee and Board receive relevant advice on investment strategy, monitoring of the performance of the fund and on administration matters, in addition to undertaking the accounting duties of the Fund.

Sian Kunert	Head of Pensions Treasury and Statutory Accounts
Ken Chisholm	Corporate Pensions Manager
Tunde Adekoya	Pension Fund Accountant
James Lake	Lead Corporate Accountant

### **Scheme Administration**

Administration of the scheme was contracted out to Surrey County Council (SCC) to provide the pensions administration under delegated authority for the London Borough of Hillingdon. Surrey maintains pension scheme membership records and calculates benefits.

Email: [myhelpdeskpensions@surreycc.gov.uk](mailto:myhelpdeskpensions@surreycc.gov.uk)

Telephone: 020 8213 2802

Address: Pension Services, Surrey County Council, Room 243, County Hall, Penrhyn Road, Kingston upon Thames, KT1 2DN

### **Fund Custodian and Performance Monitoring**

The Northern Trust Company acts as the global custodian of the Fund's assets. As part of its normal procedures Northern Trust holds all assets in safe custody, settles trades, collects dividend income, provides data for corporate actions, liaises closely with all of the investment managers and reports on all activity on a monthly and quarterly basis. Where holdings are in pooled funds, the underlying assets held by the relevant funds' custodian are reported to Northern Trust. Regular service reviews take place with Northern Trust to ensure continuous monitoring of the Funds requirements. Additionally Northern Trust provide performance analytics, comparing the performance of the Fund and individual managers to agreed benchmarks and market indices on a monthly, quarterly and annual basis.

*Northern Trust  
50 Bank Street  
Canary Wharf  
LONDON  
E14 5NT*

## **Fund Actuary**

The Fund's actuary is Hymans Robertson

*Catherine McFadyen FFA  
Hymans Robertson LLP  
20 Waterloo Street  
GLASGOW  
G2 6DB*

## **Fund Managers**

Day-to-day investment management of the Fund's assets is delegated to specialist managers in accordance with the LGPS (Management and Investment of Funds) Regulations 2016. During 2017/18, the Fund used the following external managers:

<b>Fund Manager</b>
Adam Street Partners
AEW UK
JP Morgan Asset Management
Legal & General Investment Management
London CIV - Epoch
London CIV - Ruffer
LGT Capital Partners
M&G Investments (Direct Investment)
Macquarie Investment
Newton Investment Management (defunded Nov 2017)
Permira LLP
UBS Global Asset Management

## **Advisors to the Fund**

The Fund's Investment Advisor is KPMG who was appointed July 2014. They advise the Committee on the Fund's strategic asset allocation and assist in the monitoring of fund managers.

*David O'Hara  
Director  
Investment Advisory  
Tax & Pensions  
KPMG LLP (UK)  
191 West George Street  
GLASGOW  
G2 2LJ*

In addition, the Fund has an Independent Advisor - Scott Jamieson.

The Fund has also appointed AON Hewitt to provide support on governance arrangements to the Board.

*Aon Hewitt  
25 Marsh Street  
BRISTOL  
BS1 4AQ*

### **Legal Services**

Legal support to the Fund is provided in-house by the Council. The Council's Borough Solicitor is Raj Alagh.

### **Auditor**

The Fund's external auditor, appointed by the Public Sector Audit Appointments (PSAA) is Ernst & Young.

*Ernst & Young LLP  
Wessex House  
19 Threefield lane  
SOUTHAMPTON  
SO14 3QB*

### **Banker**

Banking services are provided to the Fund by the Council's banker Lloyds.

*Lloyds Bank plc  
25 Gresham Street  
LONDON  
EC2V 7HN*

### **AVC Provider**

The Fund's provider for additional voluntary contributions is Prudential.

*Prudential AVC Customer Services  
Prudential  
CRAIGFORTH  
FK9 9UE*



## OVERVIEW OF THE SCHEME

The London Borough of Hillingdon Pension Fund is part of the Local Government Pension Scheme (LGPS) and is governed by statute. The scheme moved to a career average revalued earning (CARE) scheme, from a final salary scheme in 2014 as a result of the Local Government Pension Scheme Regulations 2013. In 2016/17, the regulations surrounding investments were amended with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

Hillingdon is the Administering Authority for the Fund. 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 2019.

The conditions of the Local Government Pension Scheme (LGPS) Regulations set out in clear terms the benefits that are payable to Scheme members. The benefits are guaranteed for those members and therefore members are not reliant on investment performance for their pension benefits. 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 are required to meet any shortfall in funding the pension liabilities of Scheme members.

The Pension Scheme during the financial year 2017/18 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 (CPI).

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. 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 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 (CPI).

**Contracting Out Status** (with effect from 1 April 2002 until 5 April 2016) - The LGPS was contracted-out of the State Second Pension Scheme (S2P), up to 5 April 2016 when contracting-out ceased. This meant that members paid reduced National Insurance contributions and they did not earn a pension under S2P. Instead, the LGPS must guarantee to pay a pension that in general is as high as the pension that would have been earned in the State Earnings Related Pension Scheme (SERPS) / S2P. For contracted-out membership between 6 April 1978 and 5 April 1997, the Inland Revenue calculates a Guaranteed Minimum Pension (GMP), which is the minimum pension, which must be paid from the London Borough of Hillingdon Pension Fund to the member. For membership after 5 April 1997, the LGPS has guaranteed that the benefits it provides will generally be no less favourable than those provided under a Reference Scheme prescribed under the Pensions Act 1995.

**Additional Voluntary Contributions** - A facility is available for scheme members to make Additional Voluntary Contributions (AVCs). The Pension Fund Committee has appointed Prudential as the nominated provider for this purpose. This is run separately to the Hillingdon Pension Fund. Further details are available from the Prudential Pensions Connection Team on 0800 032 6674.

## **REGULATIONS**

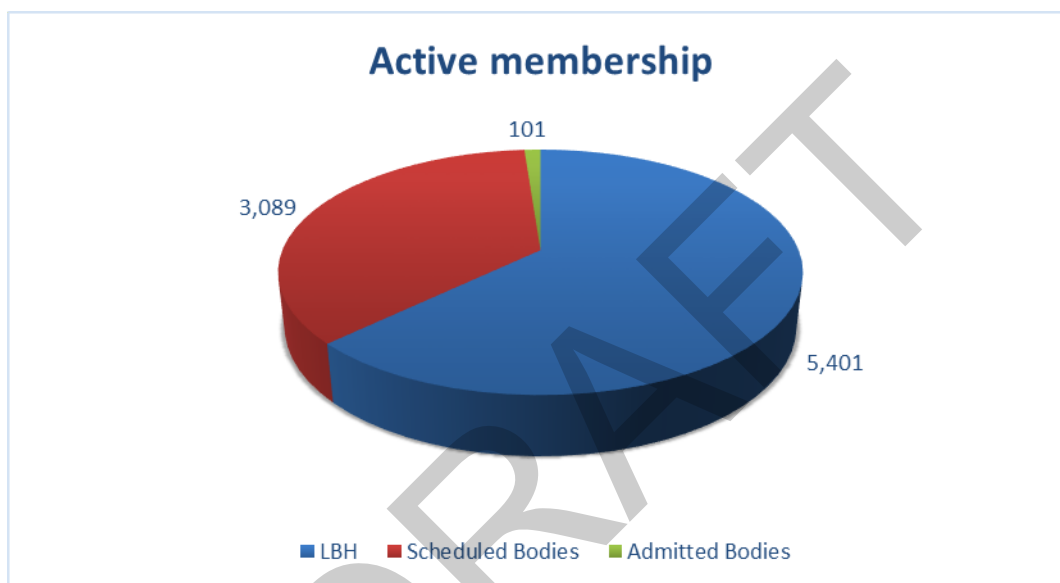
- The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016
- The Local Government Pension Scheme Regulations 2013 (as amended)
- The Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014.

## FUND MEMBERSHIP

The London Borough of Hillingdon Pension Fund is open to employees of the Council, non-teaching staff of local authority schools and certain other bodies eligible to join the Fund. Membership of the LGPS is not compulsory, although employees are automatically admitted to the fund unless they elect otherwise. Over the last few years, total membership of the fund has continued to grow, as have the number of employers participating in the Fund.

### Active Membership

As at 31 March 2018 there were 8,591 members actively contributing to the Fund. The diagram below shows a breakdown by employer type:



### General Scheme membership

Membership of the scheme is split between

- Active members - those still contributing to the scheme;
- Deferred members - those who are no longer active but have accrued benefits to be held until retirement or transfer to a new employer's scheme; and
- Pensioner members - who are both former active members now drawing their benefits and dependents of former active members.

The membership of the scheme analysed over the relevant membership profile is shown below:

## Membership Type 2017/18



As can be seen from the following chart, active membership continued to grow over the last financial year. The most significant movement year-on-year is the increase in deferred membership by 1,285 and overall scheme membership increased year-on-year by 6.2% to 23,554 scheme members. The membership profile over the last five years is shown below:

## 5 Year Membership Profile

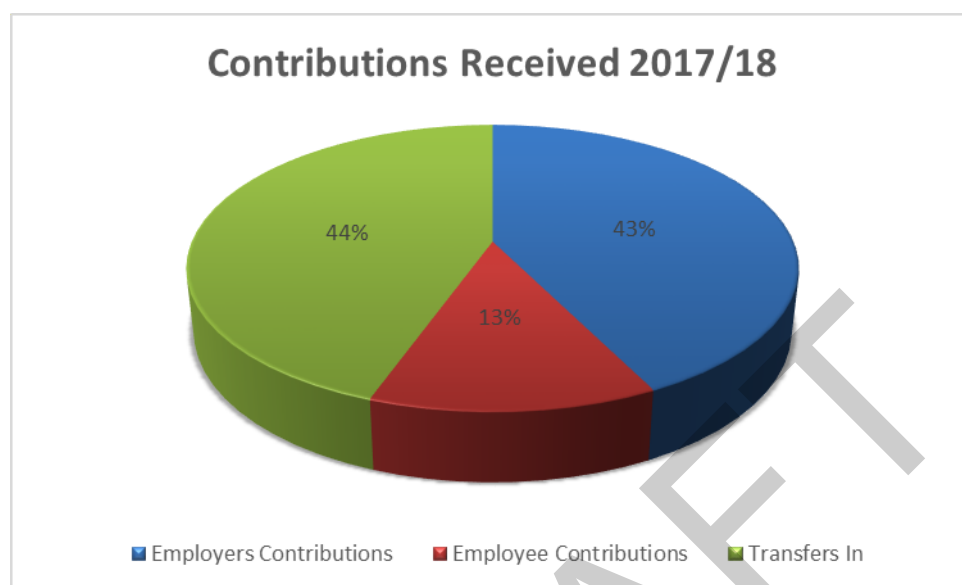


## CONTRIBUTIONS

Total Employee contributions (including transfers) into the Fund during 2017/18 amounted to £77.2m compared to £42.7m for the previous year. The 45% increase from previous year is attributable to the receipt of Bulk transfer sum of £30.1m from Harrow College because of its merger with Uxbridge College. Employee contributions ranged from 5.5% to 12.5% dependent on pensionable pay. The Fund

actuary sets employer contribution rates and the rates that applied during 2017/18 were set from the 2016 valuation.

The chart below shows the split between employee and employer contributions and transfers in. Employers contributed £32.9m compared to Employee's contributions of £9.9m and Transfers In of £34.3m during 2017/18.



The current employer contribution rates and the total contributions paid by each Employer in 2017/18 are shown in the table below.

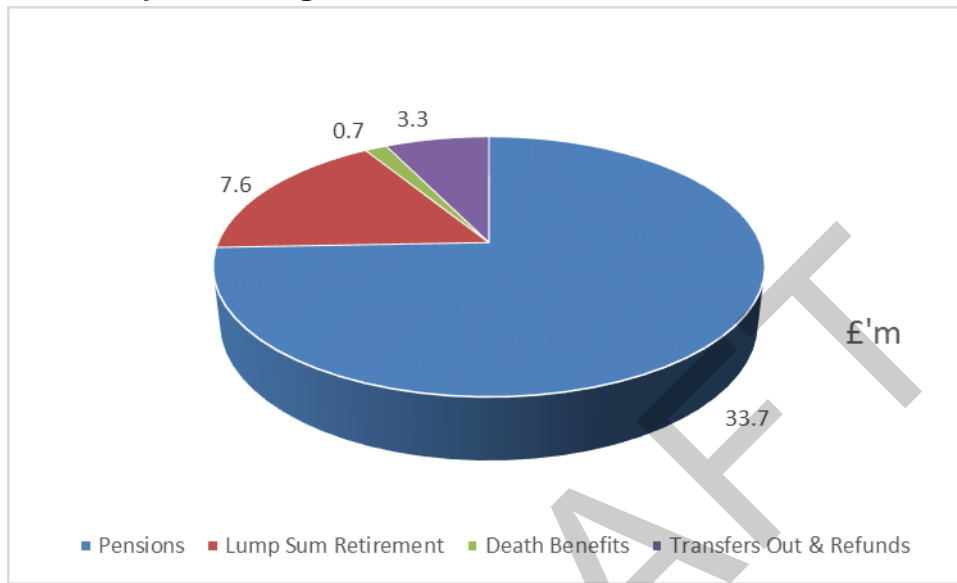
Employer	Type	Total Contributions	Contribution Rate %
London Borough of Hillingdon	Administering Authority	23,510,163.32	23.1
Barnhill Academy	Scheduled Body	292,676.48	24.9
Belmore Academy	Scheduled Body	202,478.97	24.1
Bishop Ramsey Academy	Scheduled Body	283,996.43	25.2
Bishopshalt Academy	Scheduled Body	299,879.27	28.8
Charville Academy	Scheduled Body	235,716.77	24.3
Coteford Academy	Scheduled Body	119,427.77	27.1
Cowley St. Laurence School	Scheduled Body	171,551.51	24.9
Cranford Park Academy	Scheduled Body	309,028.29	24.8
Douay Martyrs Academy	Scheduled Body	238,739.36	26.9
Eden Academy	Scheduled Body	192,870.64	21.7
Global Academy	Scheduled Body	53,049.00	17.3
Grangewood School	Scheduled body	284,998.32	21.7
Guru Nanak Academy	Scheduled Body	294,006.90	22.4
Harefield Academy	Scheduled Body	227,538.39	22.3
Haydon Academy	Scheduled Body	368,608.78	25.1
Heathrow Aviation	Scheduled Body	39,158.87	18.8
Hillingdon Primary School	Scheduled Body	187,285.15	23.5
John Locke Academy	Scheduled Body	64,024.87	19.1
Lake Farm School	Scheduled Body	101,003.59	18.9
Laurel Lane Academy	Scheduled Body	124,934.95	24.9

London Housing Consortium	Scheduled Body	264,453.03	23.1
Moorcroft School	Scheduled Body	201,264.30	21.7
Nanaksar Primary School	Scheduled Body	42,579.31	20.4
NHS – Michael Sobel House	Scheduled Body	13,526.99	23.1
Northwood Academy	Scheduled Body	103,472.02	23.8
Park Federation	Scheduled Body	68,510.42	24.8
Park West Academy	Scheduled Body	124,409.77	21.0
Pentland Field School	Scheduled Body	244,441.46	21.7
Pinkwell School	Scheduled Body	285,644.22	26.6
Queensmead Academy	Scheduled Body	271,396.01	21.8
Rosedale Hewens Academy	Scheduled Body	268,427.92	23.9
Ruislip Academy	Scheduled Body	185,450.17	25.9
Ryefield Academy	Scheduled Body	136,869.29	28.9
Skills HUB	Scheduled Body	84,644.07	29.6
St. Matthews Primary School	Scheduled Body	113,379.95	24.9
St. Martins primary School	Scheduled Body	55,299.81	24.9
Swakeleys Academy	Scheduled Body	201,340.31	23.9
Uxbridge College	Scheduled Body	1,459,432.75	21.8
Uxbridge Academy	Scheduled Body	271,533.17	21.5
Vyners Academy	Scheduled Body	235,455.74	25.7
Willows Academy	Scheduled Body	50,886.96	32.5
Wood End Academy	Scheduled Body	254,384.26	23.0
Young Peoples Academy	Scheduled Body	62,801.62	29.6
Bellrock	Admitted Body	18,673.39	47.0
Braybourne Facilities	Admitted Body	12,740.65	29.3
Caterlink	Admitted Body	1,119.30	28.3
Caterlink – Frays Academy	Admitted Body	25,166.97	28.3
Caterplus	Admitted Body	5,593.18	31.1
Churchill (was Mitie Cleaning)	Admitted Body	13,157.86	42.1
Cucina - Haydon Academy	Admitted Body	17,377.89	34.4
Cucina – Ruislip Academy	Admitted Body	1,708.21	25.9
Greenwich Leisure	Admitted Body	84,332.48	26.2
Hayward Services	Admitted Body	2,178.60	34.2
Heathrow Travel Care	Admitted Body	35,841.26	18.9
Hillingdon & Ealing Citizens Advice	Admitted Body	43,882.47	25.2
Kingdom Security	Admitted Body	14,140.94	26.3
Mitie Facilities Management	Admitted Body	2,133.69	29.5
Queensmead QED – Paul Holliday	Admitted Body	14,580.00	21.8
Taylor Shaw/Pantry – Whiteheath Infant & Warrender Schools	Admitted Body	3,905.47	29.6
Taylor Shaw/Frithwood & Hillside Schools	Admitted Body	2,896.05	31.8
Taylor Shaw/ West Drayton Primary School	Admitted Body	9,081.53	32.4
<b>Total</b>		<b>32,909,251.12</b>	

## BENEFITS

The benefits paid out from the Fund comprise annual pensions, lump sum retirement payments, death benefits and transfers to other funds. Total benefits paid out during 2017/18 amounted to £45.3m, an increase of £3.7m compared to the previous year of £41.6m.

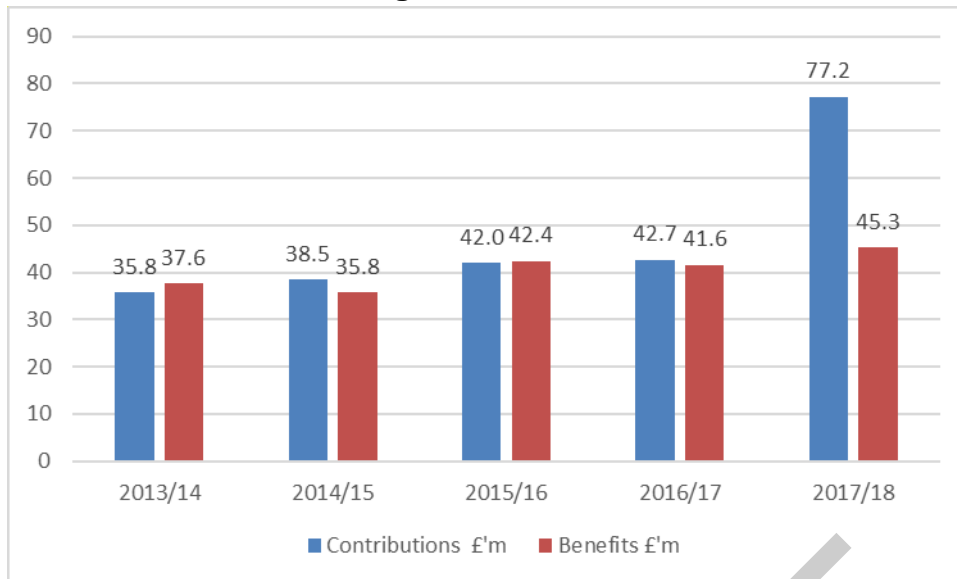
### Benefits paid during 2017/18



## CASHFLOW

The graph below illustrates contributions received and benefits paid out over the last five years. Over the illustrated period, benefits have marginally outstripped contributions twice and there is a significant difference in contributions compared to benefits in 2017/18 of about £31.9m, due to bulk transfers received as a result of acceptance of Harrow college into the fund after its' merger with Uxbridge College in October 2017.

## Contributions Received against Benefits Paid



## Management Expenses

Management expenses for 2017/18 were £7.3 million, a decrease of £1.1 million compared to 2016/17. The decrease in management expenses is mostly attributable to more assets being held within the passive mandate and the savings from passive management via the London CIV pool.

Whilst the positive cash-flow in member dealings is currently favourable to the fund, cash-flow may become an increasing concern for the Committee in the next few years.

Existing strategies are in place to address these concerns in the form of a very defensive investment portfolio, including a number of income generating investments that will reduce the necessity to sell investments should there be a sustained cash-flow shortfall. The ongoing strategy will continue to focus on generating income to meet cash-flow requirements.



# PERFORMANCE REVIEWS and REPORT of the FUND ACTUARY

## INVESTMENT REVIEW

### Market background for the year ended 31 March 2018

#### Economic Summary

The period from the end of March 2017 to end of January 2018 was arguably the best for risk-adjusted returns in equity market in history. For example, US markets never had a down month and many indices printed new all-time highs; at one stage, world equities had returned nearly 11%. These outcomes were the result of strong and synchronised economic growth almost everywhere in the world, monetary policies – set by the major central banks – that remained very accommodative and surging corporate profitability in most markets. Reinforcing these positive influences was the election of Emmanuel Macron in France as President meaning that, with the spectre of M. Le Penn avoided, the Eurozone once again became an investible region; international investors returned in their droves. To round 2017 off, President Trump lived up to his promise and fast-tracked a significant set of tax cuts that, as we now know, fuelled fresh gains in US equity markets and quickened the pace of domestic economic activity.

The early weeks of 2018 saw these influences continue to drive 'risk' markets with equity analysts engaging in a bidding war (trying to out-do each other with, ever more buoyant, forecasts of corporate profits growth). This phase could not endure, and by mid-February, a soberer perspective was adopted as equity markets encountered a sharp correction. The catalyst was Trump's next promise fulfilment - to ensure that from a trade perspective, America came first. As this year has progressed, the threat of a trade war has intensified with Trump repeatedly challenging trade-relations orthodoxy head-on.

Another significant feature has been the sharp slowing of economic activity in the UK and Eurozone economies. Initially the 'Beast from the East' (poor weather kept shoppers indoors and led to sharp increases in workplace absenteeism in Germany) explained this; with the onset of summer this excuse is starting to wear thin as pan-European economic growth remains sub-par. The Eurozone now has to contend with fresh existential threats from Italy and to an extent Spain, where populist politics have come to the fore.

Finally, we have seen an interesting succession of mini emerging market crises. First in Argentina, then Turkey, then Brazil and most recently Pakistan and South Africa. Every major cycle of US monetary tightening in the past fifty years has spawned a crisis – sometimes in the US, sometimes elsewhere; why should this phase be any different? This week the US Federal Reserve raised its policy rate for the seventh time and the strains are beginning to show.

The year ahead looks much more challenging than it did a year ago. The World's largest economy (the US) is growing, raising the global cost of capital just at the time

when significant economies in the rest of the World have seen activity soften. At the same time US, trade policy is determined to ensure that less US demand is satisfied by imports. The oil price is rising on strong US growth and falling stockpiles and, in contrast with previous cycles, this is unlikely to check the US economy; thanks to shale production, the US is not now dependent on energy imports. These are challenging contrasts and breaks with precedent. Investors have enjoyed good gains for several years; future victories will be harder won.

### **Key asset class information**

In the fiscal year 2017/18, financial market gains were extremely modest: UK equities returned 1.2% while world equity markets, from a UK perspective, delivered +2.6%. Ten-year gilt yields rose 0.3% to 1.4%, consumer price inflation rose to 2.5% and the UK real economy expanded by 1.2% - below the global average; Sterling rose 2.9%. UK base rates have returned to 0.5% with the Bank of England reversing the 'emergency' cut of 0.25% implemented after the EU Referendum in 2016; base rates expected to remain very low for the foreseeable future.

### **Investment Strategy**

The setting and maintenance of the Fund's investment strategy are undertaken through the work of the Pensions Committee. The main consideration when devising an investment strategy for the Fund is recognising that the objective of the Fund is to pay benefits to members and their dependants, both now and in the future. These benefits, which form the liabilities of the Fund, are very long term in nature. For that reason, a reasonably high proportion of assets invests in growth assets such as equities, property, private equity and other alternative investments, which are expected to deliver higher returns over the longer term.

### **Fund Managers**

**AEW UK Property** is a manager of direct property mandate to complement the existing pooled property investment strategy of UBS and generate premium returns commensurate with their investment cycle and strategy. AEW looks to build diversified portfolios of small lot commercial properties. Lot size is typically in the £3-5m range. Properties are located all over the UK with negligible exposure to London. The manager seeks to find properties that are well located and subject to strong tenant demand. The manager looks to add significant value through asset management e.g. re-positioning, refurbishing properties at lease expiry and has a bias to shorter leases because of the greater asset management opportunities that can arise. Efforts are focused on generating income for investors.

**JP Morgan** mandate, a corporate bond portfolio with an investment objective to achieve a return in excess of benchmark by investing in an unconstrained portfolio of debt securities and currencies and using financial derivative instruments where appropriate.

**London CIV (LCIV)** is a collective investment vehicle set up by all London boroughs in line with DCLG directive to pool investment assets of local authority pension funds

striving to reduce cost of managing assets through economies of scale. As part of the process, the Fund has to date transferred 23% of its investments to be managed by the LCIV as consolidated mandates in both LCIV-Epoch Income Equity and LCIV-Ruffer Absolute Return Funds, resulting in savings from reduced fees. The plan is for all fund assets to be migrated into management by LCIV in the future and further reduce fund management costs. Ruffer is an Absolute Return manager and the manager has two goals: not to lose money on a rolling 12-month basis and to grow funds at a rate higher than would be achieved by depositing in cash. The asset allocation is driven by two selections: those investments likely to deliver the required growth over the longer term ('Greed' assets) and those, which should rise in response to conditions under which the Greed assets lose value ('Fear' assets). Historically Fear and Greed weightings have been broadly comparable. Epoch manage a Global Equity Income Fund geared towards achieving total returns over the long-term, with a bias towards income and aims to achieve a level of income greater than the MSCI World Index (Net).

**LGIM** - The manager was appointed through partnership with the LCIV benefiting from lower negotiated fees to manage passive assets. Its aim is to capture benchmark returns by replicating the indices backing the assets.

**M&G** - The objective of the Fund is to create attractive levels of current income for investors, while maintaining relatively low volatility of Net Asset Value. The fund was set up to provide medium to long term debt financing to mid-cap UK companies with strong business fundamentals that are facing difficulties refinancing existing loans in the bank market. As at the end of March 2018, all three invested funds are fully drawn down. The pension fund has already received more than the value of cash invested in the M&G Companies Fund, including promised returns on investment. Some returns have been received from investments in the Debt opportunities funds. Repayment of invested cash in all three funds should accelerate over the next year as they mature.

**Macquarie** - The mandate spans four regional funds – Europe, China, India and the US. Macquarie tends to pursue large-scale projects often directly operating the assets invariably in partnership with local asset owners, wealthy individuals. Since Inception of the portfolio, progress has been steady with allocation to all four funds are about 90% drawn-down. Returns on investments with this manager is expected to start coming back in the next few years.

**Permira** were appointed in November 2014 and aims to deliver a superior return from lending directly to corporate borrowers. The manager will generally lend on a fully secured basis although may lend sparingly on a weaker basis. To augment the lending rate, Permira will generally secure arrangement fees in respect of each loan advanced. The manager will normally secure strong position or fully control the board of most companies it lends money. Current investments with the manager in both the Permira Credit Solutions II and III equates to 5.73% of total fund assets as at 31 March 2018.

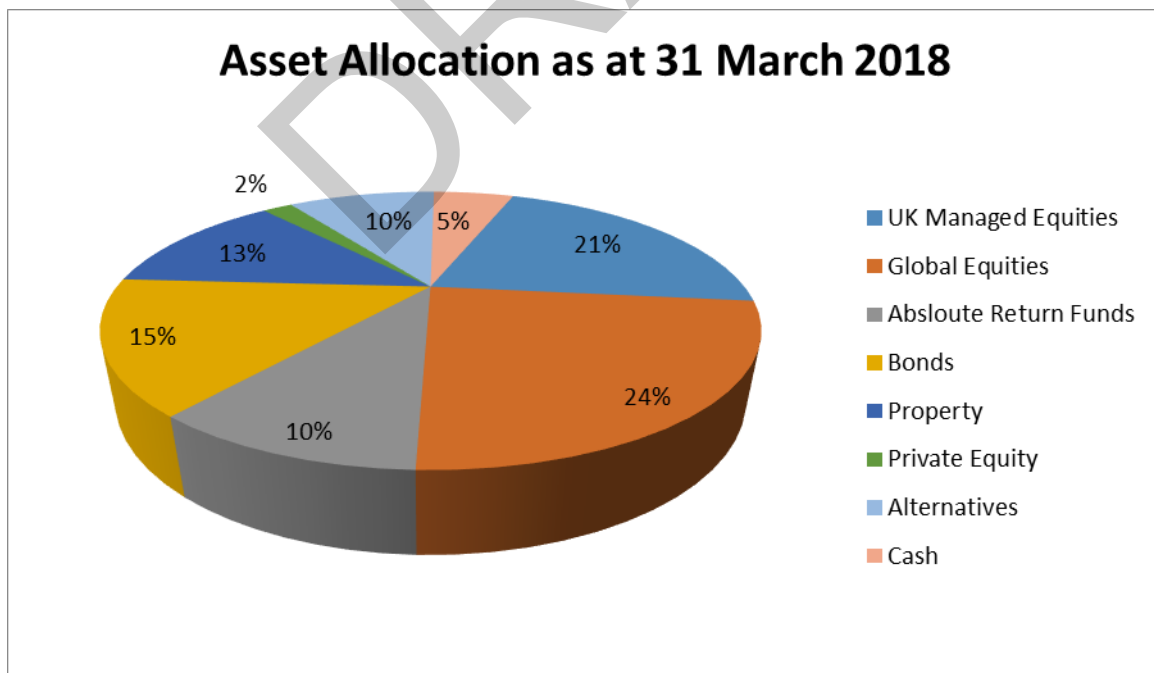
**Private equity** is an illiquid asset with a long-term horizon. The Fund has approximately 2% of assets invested in private equity; the assets are split between Adams Street Partners, which is based in the US, and Liechtenstein Global Trust Capital Partners (LGT), which operates out of Switzerland. Both managers invest globally. Within each manager, private equity assets are spread across several funds launched in different years in order to provide time diversification. The majority of the investments are being returned and should be wound down over the next four years. There are currently no plans to make further commitments to this asset class by the Pension Committee, but the decision could be reviewed if it meets the future strategic direction of the fund.

**UBS** manages UK equities using a value approach to stock selection. The manager's core belief is that success will come from adopting a robust investment and valuation approach applied consistently across the economic and stock market cycles.

**UBS Property** - The property mandate managed by UBS operates a fund of funds UK property structure. The manager has full discretion to invest in both its own in-house pooled property fund and those of other third party fund managers. The aim is to keep the portfolio investments diversified, thus mitigating concentration risks.

### Fund Value and Asset allocation

At 31 March 2018, the total value of the pension fund investment assets and liabilities was £1,015,771k. The following diagram identifies the allocation by asset class:



Whilst managers are able to use their discretion to make minor variations in the allocation of investments between markets, the major movements are a combination of market gains, revised asset allocation and maturation of Private Equity and alternative investments during the year. The table below shows the total of investment assets and liabilities held by each manager as at 31 March 2018.

INVESTMENT MANAGER	as at 31 March 2018		as at 31 March 2017	
	£'000	%	£'000	%
Adams Street	13,206	1.30	17,532	1.84
AEW UK	54,361	5.36	47,565	4.98
JP Morgan	56,312	5.56	54,622	5.72
LGIM	295,839	29.19	287,498	30.10
LGT	6,339	0.63	9,596	1.00
London CIV – Ruffer/Epoch	233,020	22.99	104,454	10.94
M&G	13,220	1.30	22,447	2.35
Macquarie	27,374	2.70	27,002	2.83
Newton	0	0	137,948	14.44
Permira	58,114	5.73	38,233	4.00
UBS Equities	133,133	13.14	130,119	13.62
UBS Property	75,192	7.42	68,499	7.17
Other	47,460	4.68	9,675	1.01
<b>Total</b>	<b>1,013,570</b>	<b>100.0</b>	<b>955,190</b>	<b>100.0</b>

Note: Includes other transition assets, pending trades and recoverable tax.

The largest five holdings in the fund as at 31 March 2018 were:

Top 5 Holdings	Market Value as at 31 March 2018 £000s	Percentage of Fund Value
EPOCH INVESTMENT P INCOME EQUITY A GBP DIS	129,750	12.80%
LONDON LGPS CIV LT RF ABSOLUTE RETURN A GBP DI	103,270	10.19%
Legal & General Investments UK EQUITY INDEX (OFC)	86,500	8.53%
JPMORGAN ASSET MGM GLOBAL BOND OPPORTUNITIES X	56,312	5.56%
AEW UK Investment Management LLP AEW UK Core Property Fund A	54,361	5.36%

The largest 10 directly held equity holdings were as follows:

Top 10 Directly Held Equity Holdings	Market Value as at 31 March 2018 £000s	Percentage of Fund Value
Royal Dutch Shell 'B'ord Eur0.07	10,302	1.02%
Bp Ord Usd0.25	10,275	1.01%
Hsbc Hldgs Ord Usd0.50(Uk Reg)	7,634	0.75%
Barclays Plc Ord Gbp0.25	6,436	0.63%
Lloyds Banking Gp Ord Gbp0.1	5,743	0.57%
Glaxosmithkline Ord Gbp0.25	5,579	0.55%
Glencore Plc Ord Usd0.01	5,085	0.50%
Anglo American Usd0.54945	4,692	0.46%
3i Group Ord Gbp0.738636	4,553	0.45%
Rio Tinto Ord Gbp0.10	4,229	0.42%

### Investment Performance

Over the financial year under review, the fund grew by 2.96%, underperforming its' benchmark figure of 3.71%. Over a three-year period to 31 March 2018, the fund has outperformed with a relative return, exceeding the benchmark by 0.32% pa.

### Performance by asset class

Performance Asset Class	1 Year			3 Year		
	Fund	B' mark	+/-	Fund	B' mark	+/-
UK Equities	3.24	1.25	1.97	8.20	5.86	2.21
Overseas Equities	3.50	3.06	0.43	7.62	11.25	(3.26)
Balanced Funds (LCIV)	(5.34)	(2.69)	(2.72)	-	-	-
Bonds	2.37	3.41	(1.01)	4.57	3.65	0.88
Index Linked Gilts	0.99	0.99	0.00	8.57	7.48	1.01
Private Equity	7.36	6.62	0.69	14.87	14.68	0.17
Property	10.78	10.05	0.66	9.10	8.06	0.96
Infrastructure	9.49	3.41	5.88	18.12	3.59	14.03
Private Credit	9.53	4.41	4.91	9.84	4.59	5.02
<b>Total Portfolio</b>	<b>2.96</b>	<b>3.71</b>	<b>(0.73)</b>	<b>7.42</b>	<b>7.08</b>	<b>0.32</b>

Note: Excess returns calculated using relative methodology

## Performance by manager

Performance Manager	1 Year			3 Year			Since Inception		
	Fund	B' mark	+/-	Fund	B' mark	+/-	Fund	B' mark	+/-
Adams Street	3.37	6.62	(3.05)	11.54	14.68	(2.74)	6.34	-	-
AEW UK	14.29	10.05	3.85	10.85	8.57	2.10	11.84	10.03	1.64
JP Morgan	3.09	3.41	(0.31)	4.06	3.60	0.44	3.99	3.63	0.34
London CIV - Epoch	-	-	-	-	-	-	(8.41)	(5.20)	(3.38)
London CIV- Ruffer	(1.12)	0.41	(1.52)	2.87	0.59	2.27	5.48	0.81	4.63
LGIM I	2.11	2.24	(0.13)	-	-	-	5.26	5.26	0.00
LGIM II	5.04	5.38	(0.32)	-	-	-	6.35	6.66	(0.29)
LGT Capital	15.21	6.62	8.05	21.14	14.68	5.63	10.85	-	-
Macquarie	9.33	3.41	5.72	17.74	3.59	13.66	4.66	3.66	0.97
M&G	10.23	4.41	5.58	10.61	4.59	5.76	7.58	4.67	2.79
Permira	7.83	4.41	3.27	9.92	4.59	5.10	9.36	4.55	4.60
UBS Equities	4.31	1.25	3.02	8.99	5.86	2.95	10.10	8.66	1.32
UBS Property	8.31	10.05	(1.58)	8.83	8.06	0.71	3.99	3.94	0.05
<b>Total Portfolio</b>	<b>2.96</b>	<b>3.71</b>	<b>(0.73)</b>	<b>7.42</b>	<b>7.08</b>	<b>0.32</b>	<b>7.03</b>	<b>6.92</b>	<b>0.11</b>

Note: Excess returns calculated using relative methodology

Performance over one year was 0.73% behind the benchmark return of 2.96%, with UBS Property, Ruffer and Adams Street accountable for a large proportion of the underperformance, whilst LGT Capital, Macquarie and M&G were the best performing managers over the period.

Three year and since inception figures were ahead of the fund benchmark with relative outperformance of 0.32% and 0.11% respectively.

### Custody

The Northern Trust Company acts as the global custodian of the Fund's assets. As part of its normal procedures Northern Trust holds all assets in safe custody, settles trades, securities lending, collects dividend income, provides data for corporate actions, liaises closely with all of the investment managers and reports on all activity on a monthly and quarterly basis. Where holdings are in pooled funds, the underlying assets held by the relevant funds' custodian are reported to Northern Trust. Regular service reviews take place with Northern Trust to ensure continuous monitoring of the Funds requirements.

### Responsible Investing

The Fund is committed to being a long-term steward of the assets in which it invests and expects this approach to protect and enhance the value of the Fund in the long term. External investment managers are expected to undertake appropriate monitoring of underlying investments with regard to their policies and practices on all issues that could present a material financial risk to the long-term performance of the

Fund such as corporate governance and environmental factors, integrating material ESG factors within its investment analysis and decision-making.

Where the Fund invests on a segregated basis, it requests the exclusion of investment within the Tobacco sector as part of the mandate. The Fund will not pursue policies that are contrary to UK foreign policy or UK defence policy.

The Fund's approach to engagement recognises the importance of working in partnership to magnify the voice and maximise the influence of investors as owners. The Fund expects its investment managers to work collaboratively with others if this will lead to greater influence and deliver improved outcomes for shareholders and more broadly. The Fund appreciates that to gain the attention of companies in addressing governance concerns; it needs to join with other investors sharing similar concerns. To ensure effective and consistent use of the voting rights, investment managers are tasked with exercising the voting rights accruing to the Fund. If important issues affecting local residents do emanate from actions of invested companies, the Pensions Committee will contact investment managers in charge of assets of such a company to make their opinion known and ask for such to be presented at meetings with the company or reflected in their voting pattern.

The Fund complies with the UK Stewardship Code and a statement of compliance that explains the arrangements supporting its commitment to each of the seven principles.

#### Exercise of voting rights

Fund Manager	Meetings Voted	Resolutions	Votes With Management	Votes Against Management	Abstentions
UBS	9,940	101,956	91,128	10,828	-
JP Morgan	1,374	18,853	16,897	1,937	20
LGIM	3,785	46,446	40,408	6,038	1

The above table details some of the Fund's investment managers voting activities for the period under review.



## **REPORT OF THE FUND ACTUARY**

### **London Borough of Hillingdon Pension Fund (“the Fund”) Actuarial Statement for 2017/18**

This statement has been prepared in accordance with Regulation 57(1) (d) of the Local Government Pension Scheme Regulations 2013. It has been prepared at the request of the Administering Authority of the Fund for the purpose of complying with the aforementioned regulation.

#### **Description of Funding Policy**

The funding policy is set out in the Administering Authority’s Funding Strategy Statement (FSS), dated March 2017. In summary, the key funding principles are as follows:

- 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 (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.

The FSS sets out how the Administering Authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable. For employers whose covenant was considered by the Administering Authority to be sufficiently strong, contributions have been stabilised to return their portion of the Fund to full funding over 25 years if the valuation assumptions are borne out. Asset-liability modelling has been carried out which demonstrate that if these contribution rates are paid and future contribution changes are constrained as set out in the FSS, there is a better than 70% chance that the Fund will return to full funding over 25 years.

#### **Funding Position as at the last formal funding valuation**

The most recent actuarial valuation carried out under Regulation 62 of the Local Government Pension Scheme Regulations 2013 was as at 31 March 2016. This valuation revealed that the Fund’s assets, which at 31 March 2016 were valued at

£810 million, were sufficient to meet 75% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2016 valuation was £269 million.

Each employer had contribution requirements set at the valuation, with the aim of achieving full funding within a time horizon and probability measure as per the FSS. Individual employers' contributions for the period 1 April 2017 to 31 March 2020 were set in accordance with the Fund's funding policy as set out in its FSS.

### Principal Actuarial Assumptions and Method used to value the liabilities

Full details of the methods and assumptions used are described in the 2016 valuation report.

#### Method

The liabilities were assessed using an accrued benefits method, which takes into account pensionable membership up to the valuation date, and makes an allowance for expected future salary growth to retirement or expected earlier date of leaving pensionable membership.

#### Assumptions

A market-related approach was taken to valuing the liabilities, for consistency with the valuation of the Fund assets at their market value.

The key financial assumptions adopted for the 2016 valuation were as follows:

Financial assumptions	31 March 2016
Discount rate	4.0%
Salary increase assumption	2.6%
Benefit increase assumption (CPI)	2.1%

The key demographic assumption was the allowance made for longevity. The life expectancy assumptions are based on the Fund's VitaCurves with improvements in line with the CMI 2013 model, assuming the current rate of improvements has reached a peak and will converge to long-term rate of 1.25% p.a. Based on these assumptions, the average future life expectancies at age 65 are as follows:

	Males	Females
Current Pensioners	22.6 years	24.6 years
Future Pensioners*	24.0 years	26.5 years

\*Aged 45 at the 2016 Valuation.

Copies of the 2016 valuation report and Funding Strategy Statement are available on request from the Administering Authority to the Fund.

## **Experience over the period since 31 March 2016**

Since the last formal valuation, real bond yields have fallen placing a higher value on the liabilities and there have been strong asset returns, particularly during 2016/17. Both events are of broadly similar magnitude with regards to the impact on the funding position.

The next actuarial valuation will be carried out as at 31 March 2019. The Funding Strategy Statement will also be reviewed at that time.

Catherine McFadyen FFA  
For and on behalf of Hymans Robertson LLP  
20 April 2018

Hymans Robertson LLP  
20 Waterloo Street, Glasgow, G2 6DB

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# SCHEME ADMINISTRATION REPORT

## Administrators

Administration of the scheme is undertaken under delegated authority by the Pensions Team at Surrey County Council. Surrey are responsible for:

- Administering the LGPS on behalf of London Borough of Hillingdon as an Employing Authority in accordance with relevant legislation and Committee decisions;
- Administering the Council's early retirement arrangements in accordance with relevant legislation and Committee decisions;
- Providing advice to scheme members and external scheme Employers on options available under the Council's Pension Scheme; and
- Exploiting information technology to improve service standards and efficiency.

Surrey and LB Hillingdon are working closely together to provide a full administration service covering the collecting, and reconciling of pension contributions, transfers of pension rights in to and out of the LGPS and deferred benefits, payment of pensions, calculations for retirements, re-employment, and death benefits.

The agreement with Surrey details agreed performance targets and key performance indicators are reviewed quarterly at Pensions Committee and Pensions Board.

## Early Retirement

The total number of scheme members who retired on the grounds of redundancy or efficiency of the service is given below, together with the number of scheme members who retired on the grounds of permanent ill health. The figures are as at 31 March of each year.

Type of Retirement	2013/14	2014/15	2015/16	2016/17	2017/18
Redundancy or Efficiency	50	23	19	63	45
Ill Health	3	8	6	5	6
<b>Total</b>	<b>53</b>	<b>31</b>	<b>25</b>	<b>68</b>	<b>51</b>

## Complaints

The Council's complaints procedure is available to any person who wishes to make a suggestion or complaint about the service. Details of individual complaints along with the overall number of complaints are reported each year. There is also a two stage statutory Independent Dispute Resolution Procedure within the LGPS regulations. Details of this procedure are available on the Pensions web pages at [www.hillingdon.gov.uk](http://www.hillingdon.gov.uk) or on request. An application at stage one of the process is to the Corporate Pensions Manager, London Borough of Hillingdon.

## RISK MANAGEMENT

The Administering Authority recognises that effective risk management is an essential element of good governance in the LGPS and is part of the ongoing decision making process of Committee. By identifying and managing risks, the Administering Authority can:

- demonstrate best practice in governance
- improve financial management
- minimise the risk and effect of adverse conditions
- identify and maximise opportunities that might arise
- minimise threats

The Administering Authority adopts best practice risk management, which supports a structured and focused approach to managing risks, and ensures risk management is an integral part in the governance of the Fund at a strategic and operational level.

In relation to understanding and monitoring risk, the Administering Authority aims to:

- integrate risk management into the culture and day-to-day activities of the Fund
- raise awareness of the need for risk management by all those connected with the management of the Fund (including advisers, employers and other partners)
- anticipate and respond positively to change
- minimise the probability of negative outcomes for the Fund and its stakeholders
- establish and maintain a robust framework and procedures for identification, analysis, assessment and management of risk, and the reporting and recording of events, based on best practice
- ensure consistent application of the risk management methodology across all Fund activities, including projects and partnerships.

A risk report, including the latest risk register and showing the status and direction of each risk, is maintained and updated regularly and reported to Pension Committee on a quarterly basis. The key types of risk facing the Fund are explained briefly below. Further detail on the risks and the mitigating actions are included in the Funding Strategy Statement.

**Key Risk 1 – Financial Risks** - a team of experienced officers and advisors support the Pension Committee who ensure the monitoring of all financial risks for impact. The financial risks cover all aspects of the Fund's investment strategy, the impact of changes on the returns on investments, the impact of active manager performance, and the impact of pay and price inflation. Currently only the risk of the Fund's investment returns failing to match arising liabilities is reported corporately to the Council.

**Key Risk 2 – Demographic Risks** - The risk of pensioners living longer is the key risk in this area. Active monitoring of retirement patterns allow additional employer contributions to be requested if required.

**Key Risk 3 – Regulatory Risks** - Changing regulations remain a long-term risk to the fund; however, Hillingdon fully participates in consultation exercises where their influence can impact on this risk.

**Key Risk 4 – Governance Risks** - These risks relate mainly to an employer failing to notify the administering authority of changes to their structure or operation. Good employer communication is vital to keep this risk under control and officer support to the Fund helps to further mitigate these risks.

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# FINANCIAL STATEMENTS and INDEPENDENT AUDIT REPORT

## Statement of Responsibilities for the Pension Fund Statement of Accounts

### 1. Council's Responsibilities

The Council is required to:

- Make arrangements for the proper administration of its financial affairs and to ensure that one of its officers has the responsibility for the administration of those affairs. In this Council that officer is the Corporate Director of Finance;
- Manage its affairs to secure economic, efficient and effective use of resources and safeguard its assets; and
- Approve the Pension Fund of Accounts

### 2. Corporate Director of Finance Responsibilities

The Corporate Director of Finance is responsible for the preparation of the Pension Fund accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 ('the Code').

In preparing this statement of accounts, the Corporate Director of Finance has:

- Selected suitable accounting policies and then applied them consistently;
- Made judgements and estimates that were reasonable and prudent; and
- Complied with the Local Authority Code.

The Corporate Director of Finance has also:

- Kept proper accounting records that were up to date; and
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

### 3. Corporate Director of Finance Approval of Pension Fund Accounts

I certify that these accounts present a true and fair view of the financial position of the London Borough of Hillingdon Pension Fund, in terms of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in United Kingdom ('the Code'), as at 31<sup>st</sup> March 2018 and its income and expenditure for the year then ended.

Paul Whaymand  
CORPORATE DIRECTOR OF FINANCE  
{INSERT DATE}

## **Pension Committee Certificate for the Approval of the Pension Fund Accounts**

I confirm that these accounts were considered and approved by Pensions Committee at the meeting held on 18 July 2018.

Cllr Philip Corthorne  
On behalf of London Borough of Hillingdon Pension Fund  
CHAIRMAN (PENSION COMMITTEE)  
{INSERT DATE}

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**INDEPENDENT AUDITOR'S STATEMENT TO THE MEMBERS OF LONDON  
BOROUGH OF HILLINGDON ON THE PENSION FUND FINANCIAL  
STATEMENTS**

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# Pension Fund Account

## FUND ACCOUNT

	Note	31 March 2018 £000's	31 March 2017 £000's
Contributions	4	42,829	41,466
Transfers In from other pension funds	5	34,362	1,241
		<b>77,191</b>	<b>42,707</b>
Less: Benefits	6	(42,003)	(39,353)
Less: Payments to and on account of leavers	7	(3,297)	(2,243)
		<b>(45,300)</b>	<b>(41,596)</b>
<b>Net additions/(withdrawals) from dealings with members</b>		<b>31,891</b>	<b>1,111</b>
Less: Management expenses	8	(7,332)	(8,385)
<b>Net additions/(withdrawals) including fund management expenses</b>		<b>24,559</b>	<b>(7,274)</b>
<b>Return on investments</b>			
Investment income	9	15,289	16,004
Profit and losses on disposal of investments and changes in market value of investments	10A	19,302	137,690
Taxes On Income		(86)	0
<b>Net return on investments</b>		<b>34,505</b>	<b>153,694</b>
<b>Net Increase in the fund during the year</b>		<b>59,064</b>	<b>146,420</b>
<b>Net Assets at start of year</b>		<b>956,707</b>	<b>810,287</b>
<b>Net Assets at end of year</b>		<b>1,015,771</b>	<b>956,707</b>

## NET ASSETS STATEMENT

		31 March 2018 £000's	31 March 2017 £000's
Investment Assets	10	1,013,896	955,190
Investment Liabilities	10	(326)	0
<b>Total net investments</b>		<b>1,013,570</b>	<b>955,190</b>
Current Assets	11	2,480	2,198
Current Liabilities	12	(279)	(681)
<b>Net assets of the fund available to fund benefits at the end of the reporting</b>		<b>1,015,771</b>	<b>956,707</b>

The Pension Fund Accounts summarise the transactions of the scheme and show the net assets at the disposal of members. They do not take account of liabilities to pay pensions and other benefits after the period end. The actuarial present value of promised retirement benefits is disclosed at note 18.

Paul Whaymand  
Corporate Director of Finance  
31 May 2018

# Notes to Pension Fund Account

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## 1. DESCRIPTION OF THE FUND

### a. General

The London Borough of Hillingdon Pension Fund ("the fund") is part of the Local Government Pension Scheme (LGPS) and is administered by the London Borough of Hillingdon ("the administering body"). The Council is the reporting entity for this pension fund. The fund is a contributory defined benefits scheme established in accordance with statute to provide benefits to members and retired members of the London Borough of Hillingdon and Admitted and Scheduled bodies in the fund. Benefits in respect of service from 1 April 2014 are based on career average revalued earnings (CARE) scheme. Benefits in respect of past service up to 31 March 2014 are based on final salary. Pensions move in line with the Consumer Price index (CPI) annually. Benefits paid out include a pension payable to former members and their dependants, lump sum retirement benefits, payment of death benefits where death occurs in service or retirement, and early payment of benefits on medical grounds.

The fund is governed by the Public Service Pensions Act 2013 and administered in accordance with the following secondary legislation:

- Local Government Pension Scheme Regulations 2013 (as amended)
- Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 (as amended)
- Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016

### b. Membership

Membership of the LGPS is voluntary and employees are free to choose whether to join the scheme, remain in the scheme or make their own personal arrangements outside of the scheme. Due to government legislation, since 1 February 2013 all new employees who are not in the scheme are automatically enrolled. Members have the option to opt out of the scheme. Employees who have opted out are then re-enrolled every 3 years, when they can again opt out.

Employers who contribute to the fund in addition to London Borough of Hillingdon are:

#### Admitted Bodies:

Bellrock	Heathrow Travel Care
Braybourne Facilities	Hillingdon & Ealing Citizens Advice
<i>Bishop Ramsey Cleaners</i>	Kingdom Security
Caterlink	Mitie Facilities Management
Frays Academy	NHS - Michael Sobel House
Caterplus	The Pantry
Churchill Services - Mitie & McMillan Cleaning	<i>Whiteheath Infant</i>
Cucina	<i>Warrender School</i>
<i>Haydon Academy</i>	<i>Frithwood School</i>
<i>Ruislip High School</i>	<i>Hillside School</i>
Greenwich Leisure	Taylor Shaw
Hayward Services	<i>West Dayton Primary School</i>

#### Scheduled Bodies:

Barnhill Academy	London Housing Consortium
Belmore Academy	<i>Orchard Hill College Academy Trust</i>
Bishop Ramsey Academy	Skills HUB (formerly Hillingdon Tuition Centre)
Bishopshalt Academy	Young Peoples Academy
Charville Academy	<i>Park Federation Trust</i>
Douay Martyrs Academy	Central Payroll
<i>Eden Academy Trust</i>	Cranford Park Academy
Moorcroft School	Lake Farm Park Federation

# Notes to Pension Fund Account

Pentland Field School	Wood End Academy
Grangewood School	West Drayton Academy
<i>Elliot Foundation Trust</i>	<i>QED Academy Trust</i>
Hillingdon Primary School	Coteford Academy
John Locke Academy	Queensmead Academy
Pinkwell School	Northwood Academy
<i>Guru Nanak Academy Trust</i>	<i>Rosedale Hewens Academy Trust</i>
Nanak Sar Primary School	Rosedale College
Guru Nanak Sikh Academy	Mellowlane School
Global Academy	Brookside Primary School
Harefield Academy	Ruislip High School
Harrow & Uxbridge College	Ryefield Primary School
Haydon Academy	Vyners Academy
Heathrow Aviation Engineering	Stockley Academy
<i>LBDS Frays Academy Trust</i>	Swakeleys Academy
Cowley St. Lawrence Academy	Uxbridge Academy
Laurel Lane Academy	William Byrd School
St. Matthews Primary School	Willows Academy
St. Martins Primary School	
Central Payroll	

As at 31 March 2018 there were 8,591 active members contributing to the fund, with 6,453 members in receipt of benefit and 8,510 members entitled to deferred benefits.

London Borough of Hillingdon Pension Fund	31 March 2018	31 March 2017
Number of employers with active members	62	53
<b>Number of employees in scheme</b>		
London Borough of Hillingdon	5,401	5,862
Other employers	3,190	2,822
<b>Total</b>	<b>8,591</b>	<b>8,684</b>
<b>Number of Pensioners</b>		
London Borough of Hillingdon	6,106	5,314
Other employers	347	880
<b>Total</b>	<b>6,453</b>	<b>6,194</b>
<b>Deferred Pensioners</b>		
London Borough of Hillingdon	7,135	6,279
Other employers	1,375	946
<b>Total</b>	<b>8,510</b>	<b>7,225</b>

## c. Funding

The fund is financed by contributions from the employers, pension fund members and by income from the fund's investments. The pension fund accounts do not take account of liabilities to pay pensions and other benefits in the future. The contributions from the London Borough of Hillingdon and other participating employers are set through the triennial actuarial valuation at a rate sufficient to meet the long-term liabilities of the fund.

## d. Investments

The pension fund investments are managed externally by fund managers: Adams Street Partners, AEW UK, JP Morgan Asset Management, Legal & General Investment Management, LGT Capital Partners, London CIV, Macquarie Investments, Newton Asset Management (assets transferred to London CIV Nov 2017), Permira LLP, and UBS Global Asset Management. In addition, there are two direct investments into pooled funds with M&G Investments.

# Notes to Pension Fund Account

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## e. Governance

The fund is overseen by the Pensions Committee (comprised of Councillors) and the Pensions Board (comprised of an even number of employer and member representatives). The performance of the fund managers is monitored by the Pensions Committee and governance is overseen by the Pensions Board. Pensions Committee and Pensions Board consisted of the following members in 2017/18:

### Pensions Committee

Cllr Phillip Corthorne (Chairman)  
Cllr Michael Markham (Vice-Chairman)  
Cllr Peter Davis

Cllr Tony Eginton  
Cllr Beulah East

### Pensions Board

Cllr David Simmonds (Chairman)  
Cllr Alan Chapman (Vice-Chairman)  
Mr Andrew Scott (Employee Representative)

Cllr John Morse  
Venetia Rogers (Employee Representative)  
Roger Hackett (Employee Representative)

## 2. BASIS OF PREPARATION

The accounts have been compiled in accordance to the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2017/18 which is based on International Financial Reporting Standards (IFRS) as amended for the public sector and underpinned by the Local Government Pension Scheme Regulations. The accounts have been prepared on an accruals basis, except for transfer values which are accounted for on a cash basis, and summarise the fund transactions and report on the net assets available to pay pension benefits as at 31 March 2018.

The accounts do not take into account obligations to pay benefits and pensions that fall due after the reporting date (31 March 2018).

## 3. ACCOUNTING POLICIES

### a. Valuation of assets

- Market quoted investments: Equities are valued at bid market prices available on the final day of the accounting period.

- Fixed income securities including short-term instruments are priced based on evaluated prices provided by independent pricing services.

- For pooled funds, if bid prices are provided by the fund administrators then these are used, otherwise the Net Asset Value is used.

- Private Equity is valued using the latest audited valuation from the Limited Partner/General Partner. This is adjusted for any capital calls/distributions that have taken place since the date of the statement. Unquoted investments for Private Placements and Infrastructure are priced using discounted cash flow methodology.

b. Foreign currency translation of assets and liabilities and forward foreign exchange contracts are converted into sterling at the closing middle rates of exchange in the Net Assets Statement. Overseas income is converted at rates of exchange ruling when remitted.

c. Acquisition costs of investments occur as brokerage commission when investments are purchased. They are recorded in the cost figure on an accruals basis.

d. Investment management expenses are recorded at cost when the fund managers/custodian invoice the fund on a quarterly basis or provide a fee schedule deducted at source. Expenses are recorded on an accruals basis.

e. Administration expenses are paid when invoiced by third party providers through the administering authority's payment system and recharged to the Pension fund.

# Notes to Pension Fund Account

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- f. Interest on property developments - property is held in unit trusts for the pension fund, the return received is calculated in accordance with the unit price at the Net Assets Statement date.
- g. Contributions are accounted for in the period in which they fall due. Normal contributions received during the year are in accordance with the rates and adjustments certificate.
- h. Benefits are accounted for in the period in which they fall due. All benefits are calculated in accordance with the statutory regulations in force at the relevant benefit date.
- i. Transfers are accounted for on a cash basis, as the amount payable or receivable by the scheme is not determined until payment is actually made and accepted by the recipient. Group transfers are accounted for under the agreement which they are made.
- j. Cash and cash equivalents are held in the custody accounts by fund managers as agreed in the individual Investment Management Agreements (IMA). Cash held is at the discretion of the manager but must not exceed the stipulated permitted range in the IMA.
- k. Investment Income - dividends from quoted securities are accrued when the securities are quoted ex-dividend. Interest on cash deposits are accrued on daily basis.

## Critical Judgements and Uncertainties

- l. Unquoted Alternative Investments - Fair values of alternative investments are highly subjective in nature. They are inherently based on forward-looking estimates and judgements involving many factors. Unquoted alternative investments are valued by investment managers using methods such as IFRS fair value principles, discounted cash flow method and guidelines set out by the International Private Equity and Venture Capital Association (IPEV), of which the British Venture Capital Association is a founding member. The value of alternative investments as at 31 March 2018 was £118,347k (£114,851k at 31 March 2017).
- m. Assumptions made about the future and other major sources of estimation uncertainty - The pension fund accounts contains estimated figures that are based on assumptions made by the fund 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 the assumptions and estimates.

# Notes to Pension Fund Account

Items where there is a significant risk of material adjustment in the forthcoming financial year are as follows:

Item	Uncertainties	Effect if actual results differ from assumptions
Private equity	Private equity investments are valued at fair value in accordance with British Venture Capital Association guidelines or commensurate overseas equivalent. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total private equity investments in the financial statements are £19,545k. There is a risk that this investment may be under or overstated in the accounts.
Item	Uncertainties	Effect if actual results differ from assumptions
Infrastructure - Macquarie Infrastructure Real Assets	Infrastructure Valuation represents the fair value of investments held at 31 March 2018. The valuations have been completed by MIRA (Macquarie Infrastructure Real Assets) in accordance with ASC 820-10 (Fair Value Measurements), under which the fair value is determined to be the price that would be received upon sale of the investments in an orderly transaction between market participants. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total infrastructure alternative investments in the financial statements are £27,374k. There is a risk that this investment may be under or overstated in the accounts. There are no openly traded market prices available for this asset category.
Item	Uncertainties	Effect if actual results differ from assumptions
Private Finance - M&G	Private Finance investments are valued at par as they are mostly floating rate notes tied to LIBOR. Final valuation is undertaken by the analysts employed by the fund manager as they are not traded on the open market.	The total private finance investments in the financial statements are £13,220k. There is a risk that this investment may be under or overstated in the accounts. There are no openly traded market prices available for this asset category.
Item	Uncertainties	Effect if actual results differ from assumptions
Direct Lending - Permira Credit Solutions	Private Debt Investments are valued on a quarterly basis and in accordance with International Private Equity and Venture Capital valuation guidelines. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The total Private Debt investments in the financial statements are £58,114k. There is a risk that this investment may be under or overstated in the accounts. There are no openly traded market prices available for this asset category.
Item	Uncertainties	Effect if actual results differ from assumptions
Actuarial present value of promised retirement benefits	Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rates used, the rates at which salaries are projected to increase, changes in retirement ages, mortality rates and expected returns on pension fund assets. A firm of actuaries, Hymans Robertson, are engaged to provide the fund with expert advice about the assumptions to be applied.	The effects on the net pension liability of changes in individual assumptions can be measured. For instance, an increase in the discount rate assumption would result in a decrease in pension liability. An increase in assumed earnings would increase the value of liabilities and an increase in assumed life expectancy would increase the liability. This would not effect the Fund Account or Net Asset Statement, but would impact the Council Accounts. Below are the details of the sensitivity analysis to the method of assumptions used for year ended 31 March 2018 by the fund's actuaries.

Sensitivity to Unquoted Alternative Assets valuation and Pricing: Information on sensitivities of the valuation and pricing methodologies of these asset classes are disclosed in notes 14 and 16.

# Notes to Pension Fund Account

## Sensitivity Analysis

Sensitivity to the assumptions for the year ended 31 March 2018	Approximate % increase to liabilities	Approximate monetary amount (£m)
0.5% p.a. increase in the Pension Increase Rate	8%	122
0.5% p.a. increase in the Salary Increase Rate	1%	20
0.5% p.a. decrease in the Real Discount Rate	10%	150

The principal demographic assumption is the longevity assumption. For sensitivity purposes, it is estimated that a 1 year increase in life expectancy would approximately increase the liabilities by around 3-5%.

## 4. CONTRIBUTIONS

By category	31 March 2018 £000's	31 March 2017 £000's
Employees	9,920	9,356
<b>Employers Contributions:</b>		
Normal	27,356	27,134
Deficit Funding	5,553	4,976
	<b>42,829</b>	<b>41,466</b>

Deficit Funding: At the actuarial valuation on 31 March 2016 the fund was 75% funded, with the remaining 25% deficit to be recovered over a period of 25 years.

By authority	31 March 2018 £000's	31 March 2017 £000's
LB Hillingdon	30,938	30,535
Scheduled Bodies	11,484	10,459
Admitted Bodies	407	472
	<b>42,829</b>	<b>41,466</b>

## 5. TRANSFERS IN

	31 March 2018 £000's	31 March 2017 £000's
Individual transfers in from other schemes	3,313	1,241
Bulk Transfers In	31,049	0
	<b>34,362</b>	<b>1,241</b>

## 6. BENEFITS

By category	31 March 2018 £000's	31 March 2017 £000's
Pensions	(33,721)	(32,435)
Commutations and Lump Sum Retirement Benefits	(7,607)	(6,236)
Lump Sum Death Benefits	(675)	(682)
	<b>(42,003)</b>	<b>(39,353)</b>



# Notes to Pension Fund Account

## By authority

LB Hillingdon  
Scheduled Bodies  
Admitted Bodies

31 March 2018 £000's	31 March 2017 £000's
(40,220)	(37,561)
(1,428)	(1,443)
(355)	(349)
<b>(42,003)</b>	<b>(39,353)</b>

## 7. PAYMENTS TO AND ON ACCOUNT OF LEAVERS

Refunds to members leaving service  
Individual transfers out to other schemes

31 March 2018 £000's	31 March 2017 £000's
(62)	(81)
(3,235)	(2,162)
<b>(3,297)</b>	<b>(2,243)</b>

## 8. MANAGEMENT EXPENSES

The administering authority incurred costs in managing the fund for the period ending 31 March 2018 as follows:

Administrative Costs  
Investment Management Expenses  
Oversight and Governance

31 March 2018 £000's	31 March 2017 £000's
(753)	(902)
(6,392)	(6,761)
(187)	(722)
<b>(7,332)</b>	<b>(8,385)</b>

## 8A. INVESTMENT MANAGEMENT EXPENSES BREAKDOWN

Management Fees  
Performance Related Fees  
Custody Fees  
Transaction Costs

31 March 2018 £000's	31 March 2017 £000's
(5,291)	(5,359)
(525)	(917)
(56)	(96)
(520)	(389)
<b>(6,392)</b>	<b>(6,761)</b>

## 8B. TRANSACTION COSTS ANALYSIS BY ASSET CLASS

Equities  
Pooled Investments

31 March 2018 £000's	31 March 2017 £000's
(14)	(72)
(506)	(317)
<b>(520)</b>	<b>(389)</b>

## 8C. EXTERNAL AUDIT COSTS

Payable in Respect of External Audit

31 March 2018 £000's	31 March 2017 £000's
(20)	(21)
<b>(20)</b>	<b>(21)</b>

External Audit costs are included in Oversight and Governance within Management Expenses

# Notes to Pension Fund Account

## 9. INVESTMENT INCOME

	31 March 2018 £000's	31 March 2017 £000's
Income from Equities	5,294	5,071
Income from Bonds	0	37
Private Equity Income	11	4,209
Pooled Property Investments	4,838	4,774
Pooled Investments- Unit trusts and other managed funds	5,496	2,669
Interest on cash deposits	55	63
Other (for example from stock lending or underwriting)	(405)	(819)
	<b>15,289</b>	<b>16,004</b>

## 10. INVESTMENTS

	31 March 2018 £000's	31 March 2017 £000's
<b>Investment Assets</b>		
Bonds		0
Equities	128,306	123,992
Pooled investments	683,922	672,256
Pooled property investments	127,808	114,894
Private equity	19,545	27,128
<b>Other Investment balances</b>		
Cash deposits	53,558	16,276
Investment income due	757	644
<b>Total investment assets</b>	<b>1,013,896</b>	<b>955,190</b>
<b>Investment liabilities</b>		
<b>Derivative contracts:</b>		
Purchase Settlements Outstanding	(326)	0
<b>Total investment liabilities</b>	<b>(326)</b>	<b>0</b>
<b>Net investment assets</b>	<b>1,013,570</b>	<b>955,190</b>

# Notes to Pension Fund Account

## 10A. RECONCILIATION OF MOVEMENTS IN INVESTMENTS AND DERIVATIVES

	Value 1 April 2017 £000's	Purchases at cost £000's	Sales proceeds £000's	Change in market value £000's	Value 31 March 2018 £000's
<b>2017/18</b>					
Bonds	0				0
Equities	123,992	257,437	(254,089)	966	128,306
Pooled Investments	672,256	197,317	(188,869)	3,218	683,922
Pooled Property Investments	114,894	4,006	0	8,908	127,808
Private Equity	27,128	370	(9,669)	1,716	19,545
	<b>938,270</b>	<b>459,130</b>	<b>(452,627)</b>	<b>14,808</b>	<b>959,581</b>
Forward Foreign Exchange	0	12	(19)	7	(0)
	<b>938,270</b>	<b>459,142</b>	<b>(452,646)</b>	<b>14,815</b>	<b>959,581</b>
<b>Other investment balances</b>					
Cash Deposits	16,276			(575)	53,558
Investment Income Due	644				757
Adjustments to Market Value Changes				5,062	
<b>Total Investment Assets</b>	<b>955,190</b>			<b>19,302</b>	<b>1,013,896</b>
	Value 1 April 2016 £000's	Purchases at cost £000's	Sales proceeds £000's	Change in market value £000's	Value 31 March 2017 £000's
<b>2016/17</b>					
Bonds	34,898	4,704	(40,461)	859	0
Equities	123,599	139,652	(167,581)	28,322	123,992
Pooled Investments	495,752	721,833	(645,615)	100,286	672,256
Pooled Property Investments	106,360	11,904	(4,825)	1,455	114,894
Private Equity	30,082	865	(5,287)	1,468	27,128
	<b>790,691</b>	<b>878,958</b>	<b>(863,769)</b>	<b>132,390</b>	<b>938,270</b>
Forward Foreign Exchange	(317)	4,367	(3,152)	(898)	0
	<b>790,374</b>	<b>883,325</b>	<b>(866,921)</b>	<b>131,492</b>	<b>938,270</b>
<b>Other investment balances</b>					
Cash Deposits	17,296			256	16,276
Investment Income Due	980				644
Adjustments to Market Value Changes				5,942	0
<b>Total Investment Assets</b>	<b>808,650</b>			<b>137,690</b>	<b>955,190</b>

Outstanding trade of settlements (liabilities) are not included in the above reconciliation

# Notes to Pension Fund Account

## 10B. ANALYSIS OF INVESTMENTS

	31 March 2018 £000's	31 March 2017 £000's
<b>Equities</b>		
<b>UK</b>		
Quoted	128,306	123,992
	<b>128,306</b>	<b>123,992</b>
<b>Pooled funds - additional analysis</b>		
<b>UK</b>		
Fixed income unit trust	56,312	54,622
Unit trusts	233,063	242,454
Unitised insurance policies	295,839	287,498
Limited liability partnerships	98,708	87,682
	<b>683,922</b>	<b>672,256</b>
Pooled property Investments	127,808	114,894
Private equity	19,545	27,128
Cash deposits	53,558	16,276
Investment income due	757	644
	<b>201,668</b>	<b>158,942</b>
<b>Total investment assets</b>	<b>1,013,896</b>	<b>955,190</b>
<b>Investment liabilities</b>		
Purchase Settlements Outstanding	(326)	0
<b>Total investment liabilities</b>	<b>(326)</b>	<b>0</b>
<b>Net investment assets</b>	<b>1,013,570</b>	<b>955,190</b>

## 10C. INVESTMENTS ANALYSED BY FUND MANAGER

Fund Manager	Market Value 31 March 2018 £000's	%	Market Value 31 March 2017 £000's	%
Adams Street Partners	13,206	1	17,532	2
AEW UK	54,361	5	47,565	5
JP Morgan Asset Management	56,312	6	54,622	6
Legal & General Investment Management	295,839	29	287,498	30
LGT Capital Partners	6,339	1	9,596	1
London CIV - Ruffer	233,020	23	104,440	11
M&G Investments	13,220	1	22,447	2
Macquarie Infrastructure	27,374	3	27,002	3
Newton Asset Management	0	0	137,948	14
Permira Credit Solutions	58,114	6	38,233	4
UBS Global Asset Management (Equities)	133,133	13	130,119	14
UBS Global Asset Management (Property)	75,192	7	68,499	7
Other*	47,460	5	9,689	1
<b>Total</b>	<b>1,013,570</b>	<b>100</b>	<b>955,190</b>	<b>100</b>

\* Other includes pending trades, accrued income and cash held in custody accounts, independent of fund managers not mandated to hold cash.

There are no fund investments which constitute more than 5% of net assets of the scheme.

# Notes to Pension Fund Account

## 10D. STOCK LENDING

The fund's investment strategy sets the parameters for the fund's stock-lending programme. At the year-end, the value of quoted equities on loan was £31,377k (31 March 2017: £21,444k). These equities continue to be recognised in the fund's financial statements.

Counterparty risk is managed through holding collateral at the fund's custodian bank. At the year-end the fund held collateral (via the custodian) at fair value of £34,288k (31 March 2017: £23,412k) representing 109% of stock lent. Collateral consists of acceptable securities and government debt.

Stock-lending commissions are remitted to the fund via the custodian. During the period the stock is on loan, the voting rights of the loaned stock pass to the borrower. There are no liabilities associated with the loaned assets.

## 11. CURRENT ASSETS

	31 March 2018 £000's	31 March 2017 £000's
Debtors		
Employers' contributions due	50	68
Employees' contributions due	16	19
Cash balances	2,414	2,111
	<b>2,480</b>	<b>2,198</b>

## 12. CURRENT LIABILITIES

	31 March 2018 £000's	31 March 2017 £000's
Creditors		
Other local authorities (LB Hillingdon)	(8)	(227)
Other entities	(271)	(454)
	<b>(279)</b>	<b>(681)</b>

Note: Other entities balance is due to the pension fund from bodies external to the government e.g. fund managers.

## 13. ADDITIONAL VOLUNTARY CONTRIBUTIONS

	Market Value 31 March 2018 £000's	Market Value 31 March 2017 £000's
Prudential Assurance Company	5,546	5,975

Additional Voluntary Contributions paid by scheme members are not included in the accounts. The additional voluntary contributions are paid by scheme members directly to Prudential Assurance Company, who manage these monies independently of the fund and, as determined by the fund actuary, do not form part of the fund valuation.

According to information provided by Prudential, £220k was received in additional voluntary contributions by members. Any transfer of additional contributions into the fund during the year are included in the employee contributions value as detailed in note 4.

# Notes to Pension Fund Account

## 14. FAIR VALUE - BASIS OF VALUATION

The basis of the valuation of each class of investment asset is set out below. There has been no change in the valuation techniques used during the year. All assets have been valued using fair value techniques which represent the highest and best price available at the reporting date.

Description of asset	Valuation hierarchy	Basis of valuation	Observable and unobservable inputs	Key sensitivities affecting the valuations provided
Market quoted investments	Level 1	Published bid market price ruling on the final day of accounting period.	Not required	Not required
Quoted bonds	Level 1	Fixed interest securities are valued at market value based on current yields.	Not required	Not required
Pooled investments - overseas unit trusts and property funds	Level 2	Closing bid price where bid and offer prices are published. Closing single price where single price is published.	NAV-based pricing set on a forward pricing basis	Not required
Unquoted equity	Level 3	Comparable valuation of similar companies in accordance with International Private Equity and Venture Capital Valuation Guidelines (2012)	EBITDA multiple Revenue multiple Discount for lack of marketability Control premium	Valuations could be affected by material events occurring between the date of the financial statements provided and the pension fund's own reporting date, by changes to expected cashflows, and by any differences between audited and unaudited accounts.

### Sensitivity of assets valued at level 3

Having analysed historical data and current market trends, and consulted with fund managers, the fund has determined that the valuation methods described above are likely to be accurate to within the following ranges, and has set out below the consequent potential impact on the closing value of investments held at 31 March 2018. It is worth noting the sensitivity analysis below is just one of the possible changes to assets value due to the impact of factors affecting valuation methodology employed by the fund managers. Sensitivity being measured in this note differs from those in note 16 (other price risks).

	Valuation range (+/-)	Market Value 31 March 2018 £000's	Value on Increase £000's	Value on Decrease £000's
Pooled investments - Limited Liability Partnerships (Infrastructure)	10%	27,373	30,111	24,636
Pooled investments - Limited Liability Partnerships (Private Credit)	10%	71,388	78,526	64,248
Private Equity	5%	19,545	20,522	18,568
Venture Capital	5%	41	43	39
<b>Total</b>		<b>118,347</b>	<b>129,202</b>	<b>107,491</b>

# Notes to Pension Fund Account

## 14A. FAIR VALUE HIERARCHY

Asset and liability valuations have been classified into three levels, according to the quality and reliability of information used to determine fair values. Transfers between levels are recognised in the year in which they occur.

### Level 1

Assets and liabilities at level 1 are those where the fair values are derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 comprise quoted equities, quoted fixed securities, quoted index linked securities and unit trusts.

### Level 2

Assets and liabilities at level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value.

### Level 3

Assets and liabilities at level 3 are those where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data.

The following table provides an analysis of the financial assets and liabilities of the pension fund grouped into levels 1 to 3, based on the level at which the fair value is observable.

Values as at 31 March 2018	Quoted Market Price	Using Observable Inputs	With Significant Unobservable Inputs	
	Level 1 £000's	Level 2 £000's	Level 3 £000's	Total £000's
Financial Assets at Fair Value through Profit and Loss	128,307	712,927	118,347	959,581
Loans and Receivables	54,315	0	0	54,315
Financial Liabilities at Fair Value through Profit and Loss	(326)	0	0	(326)
<b>Net investment Assets</b>	<b>182,296</b>	<b>712,927</b>	<b>118,347</b>	<b>1,013,570</b>

Values as at 31 March 2017	Quoted Market Price	Using Observable Inputs	With Significant Unobservable Inputs	
	Level 1 £000's	Level 2 £000's	Level 3 £000's	Total £000's
Financial Assets at Fair Value through Profit and Loss	124,016	699,403	114,851	938,270
Loans and Receivables	16,920	0	0	16,920
Financial Liabilities at Fair Value through Profit and Loss	0	0	0	0
<b>Net investment Assets</b>	<b>140,936</b>	<b>699,403</b>	<b>114,851</b>	<b>955,190</b>

## 14B. RESTATEMENT OF VALUATION HIERARCHIES

There were no restatements of valuations between hierarchies in 2017/18.

# Notes to Pension Fund Account

## 14C.RECONCILIATION OF FAIR VALUE MEASUREMENTS WITHIN LEVEL 3

### Level 3 Assets Reconciliation

	Value 1 April 2017	Purchases at cost	Sales proceeds	Unrealised gains/(losses)	Realised gains/(losses)	Value 31 March 2018
	£000's	£000's	£000's	£000's	£000's	£000's
Private Equity - Adams Street Partners, LGT Capital Partners & UBS	27,128	370	(9,670)	(1,798)	3,514	19,545
Private Finance - M&G	22,447	3	(11,176)	(2,522)	4,521	13,273
Infrastructure - Macquarie	27,002	99	(1,315)	1,396	192	27,373
Venture Capital - UBS	41	0	0	0	0	41
Direct Lending - Permira	38,233	34,725	(16,208)	1,120	245	58,114
	<b>114,851</b>	<b>35,197</b>	<b>(38,368)</b>	<b>(1,805)</b>	<b>8,472</b>	<b>118,347</b>
Other investment balances	0				0	0
<b>Total Investment Assets</b>	<b>114,851</b>				<b>8,472</b>	<b>118,347</b>

There were no transfers in or out of level 3 assets in 2017/18.

## 14D. LEVEL 3 PRICING HIERARCHY DISCLOSURES

### Quantitative Information on Significant unobservable inputs

#### Private Equity: Adams Street & LGT capital

The significant unobservable inputs used in the fair value measurement of privately held securities are: Revenue multiples, EBITDA multiple, net income multiple and discount for lack of marketability and potential bids.

#### Private Finance: M&G

The assets are mostly floating rate notes and held at par value.

#### Infrastructure: Macquarie

The following quantitative information are considered for significant unobservable inputs, in valuation of infrastructure assets.

- The acquisition financial model is used as a base case.
- Update for any material changes in economic, operational and financial assumptions.
- Discount equity cash flows at the sum of the risk free rate and the appropriate risk premium (as determined by the implied risk premium at acquisition unless there is an inherent change in the riskiness of the underlying investments which may necessitate a change in the risk premium).

#### Direct Lending: Permira

The following key terms are confirmed as inputs for each yield analysis calculation:

- Cash / PIK (Payment In Kind) margin
- Frequency of interest payments
- Commitment and settlement date
- Contracted and expected maturity date

### Description of Valuation Process

#### Private Equity

The fair value of financial instruments that are not traded in an active market are determined by using valuation techniques. Private equity investments for which market quotations are not readily available are valued at their fair values by the Board of Directors. Private equity valuations are usually generated by the managers of the underlying portfolio of investments on a quarterly basis and are actually received with a delay of at least one-to-two months after the quarter end date. As a result, the year-end net asset value predominantly consists of portfolio valuations provided by the investment managers of the underlying funds at a specific date, adjusted for subsequent capital calls and distributions. If the Board of Directors comes to the conclusion upon recommendation of the Investment Manager (after applying the above mentioned valuation methods), that the most recent valuation reported by the manager/administrator of a fund investment is materially misstated, it will make the necessary adjustments using the results of its own review and analysis. The valuation adjustments relate to events subsequent to the last capital account valuation statement received but based upon information provided by the investment manager and all other



# Notes to Pension Fund Account

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available unobservable inputs. In estimating the fair value of fund investments, the Investment Manager in its valuation recommendation to the Board of Directors considers all appropriate and applicable factors.

## **Private Finance: M&G**

These assets are floating rate and are held to maturity they are valued at par unless suffering from impairment. Impairments may be applied if an asset's credit rating deteriorates.

## **Direct Lending: Permira**

- In each case, valuations are prepared in accordance with International Private Equity & Venture Capital Valuation ("IPEV") Guidelines
- All direct lending investments are valued on a mark-to-market basis at the date of valuation
- Where an investment is considered illiquid (level 3), a yield analysis is performed to infer a fair market value for that investment.
- Each valuation is reviewed to ensure:
  - Third party evidence to support pricing (such as Market data, broker quotes or Bloomberg pricing, as well as latest financials and capital structure; and any other adjustments to value) was evidenced;
  - That the valuations are prepared in a consistent manner with previous valuations and that any changes in methodology or valuation are clearly explained; and valuations are derived using methodology consistent with the IPEV guidelines.

## **Infrastructure: Macquarie**

Valuations are calculated by the individual asset teams on a quarterly basis. The valuation process follows the British Venture Capital Association (BVCA) guidelines, and is compliant with International Financial Reporting Standards (IFRS). The most generally accepted methodology of valuing infrastructure assets is by way of a discounted cash flow (DCF) analysis.

## **DCF-Based Market Valuation Process**

### **Financial Model**

The acquisition financial models of all of the Fund's underlying investments will be externally audited prior to financial close. They will be used as the initial base financial models for the DCF analysis.

### **Update for Economic, Operational and Financial Assumptions**

The economic assumptions in the financial models are adjusted every three months in order to reflect current market conditions. The main economic variables relate to interest rates, exchange rates and inflation.

The initial operational assumptions in each of the financial models are the acquisition forecasts. Any historical information (e.g. distributions received in an intervening period and year to date performance) will be updated within the model. In relation to forward-looking assumptions, the acquisition assumptions will continue to be used unless there is a material inconsistency between these assumptions and:

- The actual operational results to date
- The revised forecasts provided by management or approved by the board.

The financial assumptions in the model (e.g. cost of debt and capital structure) are also updated to reflect the actual debt put into place, current base rates and any material change in outlook with regards to future leverage.

### **Discount Rate**

Equity cash flows are discounted at the acquisition internal rate of return, which is adjusted for changes in the relevant risk free rate. The acquisition internal rate of return is the return which is forecast under the acquisition case and price, reflecting the risks inherent in each of the investments. The difference between the acquisition internal rate of return and the risk free rate at the date of acquisition equates to the risk premium, which is the risk compensation to equity holders.

Most of the Fund's assets are likely to see some decrease in the risk premium as assets are de-risked following acquisition. Such projects may have a changing risk "life-cycle", whereby the risk changes as the asset matures. In addition, if there is a change in the inherent risk of an investment, then the risk premium may need to be reconsidered.

# Notes to Pension Fund Account

## Narrative and Quantitative description of sensitivity to changes in valuation methods and market conditions:

### Private Equity

Market valuation method applied to investments is sensitive to four main components:

- i) changes in actual market prices;
- ii) interest rate risk;
- iii) foreign currency movements; and
- iv) other price risks

### Private Finance (M&G)

The only possible sensitivity associated with private finance valuations and methodology is credit rating. This may result in an analyst impairing an asset if there is a change in the asset's credit rating.

### Infrastructure: Macquarie

The economic assumptions in the financial models are adjusted every three months in order to reflect current market conditions. The main economic variables relate to interest rates, exchange rates and inflation.

### Direct Lending: Permira

The yield analysis methodology used to value the level 3 assets are sensitive to the following inputs:

- EURIBOR swap rates (up to 7 years)
- LIBOR swap rates (up to 7 years)
- ELLI (3 year discounted spread data)

These inputs are sourced directly from Bloomberg feeds or independently from Duff & Phelps (ELLI data) relevant to each period end date.

These inputs impact on: (1) the implied IRR calculations at the period end valuation date; (2) the forecast cash and/or PIK yields that track LIBOR or EURIBOR; and (3) ultimately the implied asset price calculated from these inputs as the period end to determine the valuation price.

## 15. CLASSIFICATION OF FINANCIAL INSTRUMENTS

The following table analyses the carrying amounts of financial instruments by category and net assets statement heading. No financial instruments were reclassified during the accounting period.

	Designated as fair value through P&L	Loans & receivables	Financial Liabilities At amortised Cost	Total	Designated as fair value through P&L	Loans & receivables	Financial Liabilities At amortised Cost	Total
	31 March 2018 £000's	31 March 2018 £000's	31 March 2018 £000's	31 March 2018 £000's	31 March 2017 £000's	31 March 2017 £000's	31 March 2018 £000's	31 March 2017 £000's
<b>Financial Assets</b>								
Equities	128,306	0	0	128,306	123,992	0	0	123,992
Pooled Investments	683,922	0	0	683,922	672,256	0	0	672,256
Pooled property investments	127,808	0	0	127,808	114,894	0	0	114,894
Private Equity	19,545	0	0	19,545	27,128	0	0	27,128
Cash	0	53,558	0	53,558	0	16,276	0	16,276
Other Investment balances	0	757	0	757	0	644	0	644
	<b>959,581</b>	<b>54,315</b>	<b>0</b>	<b>1,013,896</b>	<b>938,270</b>	<b>16,920</b>	<b>0</b>	<b>955,190</b>
<b>Financial Liabilities</b>								
Purchase Settlements Outstanding	0	0	(326)	(326)	0	0	0	0
	<b>0</b>	<b>0</b>	<b>(326)</b>	<b>(326)</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total</b>	<b>959,581</b>	<b>54,315</b>	<b>(326)</b>	<b>1,013,570</b>	<b>938,270</b>	<b>16,920</b>	<b>0</b>	<b>955,190</b>

# Notes to Pension Fund Account

## 16. NATURE & EXTENT OF EXPOSURE TO 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. Therefore the aim of investment risk management is to minimise the risk of an overall reduction in the value of the fund and to maximise the opportunity for gains across the whole fund portfolio. The fund achieves this through asset diversification to reduce exposure to market risk (price risk, currency and interest rate risks) and credit risk to an acceptable level. In addition, the fund manages its liquidity risk to ensure there is sufficient liquidity to meet the fund's forecast cash flows.

Responsibility for the fund's risk management strategy rests with the Pensions Committee. Risk management policies are established to identify and analyse the risks faced by the Council's pensions operations. Policies are reviewed regularly to reflect changes in activity and in market conditions.

### Market risk

The risk that the fair value of cash flows of a financial instrument will fluctuate due to changes in market prices. Market risk reflects interest rate risk, currency risk and other price risks. To mitigate against market risk the pension fund invests in a diversified pool of assets to ensure a reasonable balance between different categories. The management of the assets are placed with a number of fund managers with different performance targets and investment strategies. Each fund manager is expected to maintain a diversified portfolio in each asset class. Risks associated with the strategy and investment returns are included as part of the quarterly reporting to Pensions Committee where they are monitored and reviewed.

### Other price risk

Other price risk represents the risk that the value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate risk or foreign exchange risk), whether those changes are caused by factors specific to the individual instruments or its issuer, or factors affecting all such instruments in the market. The fund is exposed to share and derivative price risk. This arises from investments held by the fund for which the future price is uncertain. All securities investments present a risk of loss of capital. Except for shares sold short, the maximum risk resulting from financial instruments is determined by the fair value of the financial instruments. The potential losses from shares sold short are unlimited. The fund's investment managers mitigate this price risk through diversification and the selection of securities and other financial instruments is monitored by the Council to ensure it is within limits specified in the fund Investment Strategy Statement.

### Other price risk - Sensitivity Analysis

Following analysis of historical data and expected investment return movement during the financial year, the fund has determined that the following potential change in market price risk are reasonably possible for the relevant reporting periods.

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 as an example, so the overall outcome will depend largely on fund asset allocations. The potential volatilities are consistent with one standard deviation movement of the change in value of assets over the last three years. This can then be applied to period end asset mix.

Had the market price of the fund investments increased or decreased in line with the percentage change below, the change in the net assets available to pay benefits in the market price would have been as follows (the prior year comparator is shown below).

Asset Type	Value as at	Percentage Change	Value on Increase	Value on Decrease
	31 March 2018		£000's	£000's
	£000's	%	£000's	£000's
Global Equity	344,271	8.40%	373,190	315,352
UK Equity	214,794	10.00%	236,273	193,315
Bonds	154,478	4.30%	161,121	147,835
Alternatives	118,253	5.10%	124,284	112,222
Property	127,785	5.40%	134,685	120,885
<b>Total</b>	<b>959,581</b>		<b>1,029,553</b>	<b>889,609</b>

# Notes to Pension Fund Account

Asset Type	Value as at 31 March 2017 (Restated)	Percentage Change	Value on Increase	Value on Decrease
	£000's	%	£000's	£000's
Global Equity	348,733	8.70%	379,073	318,393
UK Equity	210,953	9.60%	231,204	190,702
Bonds	148,817	5.20%	156,555	141,079
Alternatives	114,851	6.20%	121,972	107,730
Property	114,916	3.40%	118,823	111,009
<b>Total</b>	<b>938,270</b>		<b>1,007,628</b>	<b>868,912</b>

Note: changes in asset values as at 31 March 2017 restated by asset type for comparative reason based on the current analysis provided by PIRC, our fund's analytics information provider.

**Interest Rate Risk** - The risk to which the pension fund is exposed to changes in interest rates and relates to its holdings in bonds and cash. Based on interest received on fixed interest securities, cash balances and cash and cash equivalents.

The fund's direct exposure to interest rate movements as at 31 March 2018 and 31 March 2017 is set out below. These disclosures present interest rate risk based on the underlying financial assets at fair value.

## Interest Rate Risk Sensitivity Analysis

The fund recognises that 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 points (1%) movement in interest rates is consistent with the level of sensitivity applied as part of the fund's risk management strategy.

The analysis that follows assumes that all other variables, in particular exchange rates remain constant, and shows the effect in the year on the net assets available to pay benefits of a +/- 1% change in interest rates.

Assets exposed to income rate risks	Value as at 31 March 2018	Potential movement on 1% change in interest rates	Value on increase	Value on decrease
	£000's	£000's	£000's	£000's
Cash balances	53,558	535	54,093	53,023
Bonds - pooled funds	154,478	1,545	156,023	152,934
<b>Total change in assets available</b>	<b>208,036</b>	<b>2,080</b>	<b>210,116</b>	<b>205,957</b>

Assets exposed to income rate risks	Value as at 31 March 2017	Potential movement on 1% change in interest rates	Value on increase	Value on decrease
	£000's	£000's	£000's	£000's
Cash balances	16,276	163	16,439	16,113
Bonds - pooled funds	148,817	1,488	150,305	147,329
<b>Total change in assets available</b>	<b>165,093</b>	<b>1,651</b>	<b>166,744</b>	<b>163,442</b>

**Currency Risk** - The risk to which the pension fund is exposed to fluctuations in foreign currency exchange rates.

The pension fund has the ability to set up a passive currency hedge where these risks are perceived to be adverse. As at 31 March 2018 the Fund had no currency hedge in place for those managers who do not hedge their own portfolios. The following table summarises the fund's currency exposure as at 31 March 2018 and as at the previous period ending 31 March 2017.

# Notes to Pension Fund Account

## Currency risk sensitivity analysis

Following analysis of historical data in consultation with PIRC Ltd, the funds data provider, the fund considers the likely volatility associated with foreign exchange rate movements to be 8.70%, based on the data provided by PIRC. A 8.70% fluctuation in the currency is considered reasonable based on PIRC's analysis of historical movements in month end exchange rates over a rolling twelve month period. This analysis assumes that all variables, in particular interest rates, remain constant. Managers that hedge against currency risk are not included in this sensitivity analysis. An 8.70% strengthening/weakening of the pound against various currencies in which the fund holds investments would increase/decrease the net assets available to pay benefits as follows:

<b>Assets exposed to currency risk</b>	<b>Asset Value 31 March 2018</b>	<b>Potential market movement</b>	<b>Value on increase</b>	<b>Value on decrease</b>
		8.70%		
	<b>£000's</b>	<b>£000's</b>	<b>£000's</b>	<b>£000's</b>
Overseas Managed Funds	111,250	9,679	120,929	101,571
Private Equity/Infrastructure	46,919	4,082	51,001	42,837
	<b>158,169</b>	<b>13,761</b>	<b>171,929</b>	<b>144,408</b>

<b>Assets exposed to currency risk</b>	<b>Asset Value 31 March 2017</b>	<b>Potential market movement</b>	<b>Value on increase</b>	<b>Value on decrease</b>
		7.90%		
	<b>£000's</b>	<b>£000's</b>	<b>£000's</b>	<b>£000's</b>
Overseas Managed Funds	106,344	8,401	114,745	97,943
Private Equity/Infrastructure	54,130	4,276	58,406	49,854
	<b>160,474</b>	<b>12,677</b>	<b>173,151</b>	<b>147,797</b>

**Credit Risk** - Credit risk represents the risk that the counterparty to a transaction or a financial instrument will fail to discharge an obligation and cause the fund to incur a financial loss. The market values 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 pension fund's entire investment portfolio is exposed to some form of credit risk, with the exception of the derivative position, where the risk equates to the net market value of a positive derivative position. Credit risk can be minimised through careful selection of high quality counterparties, brokers and financial institutions. The pension fund is also exposed to credit risk through Securities Lending, Forward Currency Contracts and its daily treasury activities. The Securities Lending programme is run by the fund's custodian Northern Trust who assign four different risk management oversight committees to control counterparty risk, collateral risk and the overall securities lending programme. The minimum level of collateral for securities on loan is 102%, however more collateral may be required depending on the type of transaction. To further mitigate risks, the collateral held on behalf of the pension fund is ring fenced from Northern Trust. Securities lending is capped by investment regulations and statutory limits are in place to ensure no more than 25% of eligible assets can be on loan at any one time.

The prime objective of the pension fund treasury management activity is the security of principal sums invested. As such it will take a prudent approach to organisations employed as the banker and deposit taker. The pension fund will ensure it has adequate but not excessive cash resources in order to meet its objectives. The bank accounts are held with Lloyds Plc, which holds an S&P long-term credit rating of A. Deposits are placed in the AAAf rated Northern Trust Money Market Fund which is ring fenced from the administering company. Credit ratings, market indicators and media coverage are monitored to ensure credit worthiness is maintained. The fund's cash holding under its treasury management arrangements at 31 March 2018 was £55,972k (31 March 2017: £18,387k) and this was held with the following institutions

# Notes to Pension Fund Account

Summary	Rating S&P	Balances as at 31 March 2018 £000's	Rating S&P	Balances as at 31 March 2017 £000's
<b>Money market funds</b>				
Northern Trust Global Sterling Fund A	AAAf S1+	200	AAAf	200
<b>Bank current accounts</b>				
Lloyds	A	2,214	A	1911
<b>Global Custody Cash</b>				
Northern Trust Company	AA-	53,558	AA-	16276
<b>Total</b>		<b>55,972</b>		<b>18,387</b>

**Liquidity Risk** - The risk the pension fund will have difficulties in paying its financial obligations when they fall due.

The pension fund holds a working cash balance in its own bank accounts with Lloyds and Money Market Fund to which it has instant access to cover the payment of benefits and other lump sum payments (£2,414k). At an investment level the fund holds a large proportion of assets in instruments which can be liquidated at short notice, normally three working days. As at the 31 March 2018 these assets totalled £713,477k, with a further £53,558k held in cash in the Custody accounts at Northern Trust.

## Refinancing risk

The key risk is that the fund will be bound to replenish a significant proportion of its financial instruments at a time of unfavourable interest rates. The fund does not have any financial instruments that have a refinancing risk as part of its investment strategy.

## 17. FUNDING ARRANGEMENTS

In line with the Local Government Pension Scheme Regulations 2013, the fund's actuary undertakes a revaluation every three years for the purpose of setting employer contribution rates for the forthcoming triennial period. The last valuation took place as at 31 March 2016 setting rates for the period April 2017 to March 2020. The next triennial valuation will take place as at 31 March 2019.

In line with the triennial valuation the fund updates its Funding Strategy Statement every three years. The key elements of the funding strategy are:

1. to ensure the long-term solvency of the fund, i.e. that sufficient funds are available to meet all pension liabilities as they fall due for payment
2. to ensure that employer contribution rates are as stable as possible
3. to minimise the long-term cost of the scheme by recognising the link between assets and liabilities and adopting an investment strategy that balances risk and return
4. to reflect the different characteristics of employing bodies in determining contribution rates where it is reasonable to do so
5. 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

The funding level is the ratio of assets to liabilities at the valuation date. A funding level of less/more than 100% implies that there is a deficit/surplus in the Fund at the valuation date against the funding target. Funding plans are set to eliminate any deficit (or surplus) over the set time horizon and therefore get back to a funding level of 100%. To do so, additional contributions may be required to be paid into the Fund; these contributions are known as the "secondary rate".

At the 2016 actuarial valuation, the fund was assessed as 75% funded (72% at the March 2013 valuation). This corresponded to a deficit of £269m (2013 valuation: £266m) at that time. The slight improvement in funding position between 2013 and 2016 is mainly due to investment performance over the inter-valuation period. The liabilities have also increased due to a reduction in the future expected investment return, although this has been partially been offset by lower than expected pay and benefit growth (both over the inter-valuation period and forecast to continue into the long term).

# Notes to Pension Fund Account

## Contribution rates

The table below summarises the whole fund Primary and Secondary Contribution rates at this triennial valuation. These rates are the payroll weighted average of the underlying individual employer primary and the total of employer secondary rates expressed as a monetary amount, calculated in accordance with the Regulations and CIPFA guidance.

Primary Rate (%) 1 April 2017 - 31 March 2020	Secondary Rate (£)		
	2017/18	2018/19	2019/20
19.50%	£5,296,000	£5,537,000	£6,938,000

The Primary rate above includes an allowance for administration expenses of 0.7% of pay. The employee average contribution rate is 6.4% of pay.

At the previous formal valuation at 31 March 2016, a different regulatory regime was in force. Therefore a contribution rate that is directly comparable to the rates above is not provided.

The valuation of the fund has been undertaken using a risk based approach and this approach adopted recognises the uncertainties and risks posed to funding and follows the process outlined below.

Step 1: The Fund sets a funding target (or funding basis) which defines the target amount of assets to be held to meet the future cash flows. The assumptions underlying the funding target are discussed further in the next section. A measurement is made at the valuation date to compare the assets held with the funding target.

Step 2: The Fund sets the time horizon over which the funding target is to be reached.

Step 3: The Fund sets contributions that give a sufficiently high likelihood of meeting the funding target over the set time horizon.

## Assumptions

Due to the long term nature of the Fund, assumptions about the future are required to place a value of the benefits earned to date (past service) and the cost of benefits that will be earned in the future (future service). Assumptions fall into two categories when projecting and placing a value on the future benefit payments and accrual – financial and demographic.

### Financial Assumptions

A summary of the financial assumptions underpinning the target funding basis and adopted during the assessment of the liabilities of the Fund as at 31 March 2016 (alongside those adopted at the previous valuation for comparison) are shown below.

Description	31 March 2016	31 March 2013
Funding Basis Discount Rate	4.0%	4.6%
Benefit Increases (CPI)	2.1%	2.5%
Salaries Increases	2.6%	3.3%

### Demographic Assumptions

The main demographic assumption to which the valuation results are most sensitive is that relating to the longevity of the Fund's members. For this valuation, the Fund has adopted assumptions which give the following sample average future life expectancies for members:

Description	31 March 2016	31 March 2013
<b>Male</b>		
Pensioners	22.6 years	22.7 years
Non- Pensioners	24.0 years	24.3 years
<b>Female</b>		
Pensioners	24.6 years	24.7 years
Non- Pensioners	26.5 years	26.9 years

# Notes to Pension Fund Account

## 18. ACTUARIAL PRESENT VALUE OF PROMISED RETIREMENT BENEFITS

In addition to the triennial funding valuation, the fund's actuary also undertakes a valuation of the pension fund liabilities, on an IAS 19 basis, every year using the same base data as the funding valuation rolled forward to the current financial year taking account of changes in membership numbers and updating assumptions to the current year. This valuation is not carried out on the same basis as that used for setting fund contribution rates and the fund accounts do not take account of liabilities to pay pensions and other benefits in the future.

Description	31 March 2018	31 March 2017
	% per annum	% per annum
Inflation /Pensions Increase Rate	2.4%	2.4%
Salary Increase Rate	2.8%	2.8%
Discount Rate	2.6%	2.5%

An IAS 26 valuation was carried out for the fund as at 31 March 2018 by Hymans Robertson with the following results:

Description	31 March 2018	31 March 2017
	£000's	£000's
Present Value of Promised Retirement Benefits	1,548	1,522
Active Members	624	569
Deferred Members	350	355
Pensioners	574	598

These figures are presented for the purposes of IAS 26 only. They are not relevant for the calculations undertaken for funding purposes or other statutory purposes under UK pension legislation. This item is not recognised in the Net Asset Statement, hence is considered not to be in opposition to the assertion included in the Net Asset Statement surrounding future liabilities of the fund.

The promised retirement benefits at 31 March 2018 have been projected using a roll forward approximation from the latest formal funding valuation as at 31 March 2016. The above figures include both vested and non-vested benefits, although the latter is assumed to have a negligible value.

## 19. RELATED PARTY TRANSACTIONS

It is required under IAS 24 "Related Party Disclosures" that material transactions with related parties which are not disclosed elsewhere should be included in a note to the financial statements.

The London Borough of Hillingdon is a related party to the pension fund. The revenue contributions the Council has made into the pension fund are set out in note 4 to the Pension Fund accounts.

No senior officer or Pension Committee member had any interest with any related parties to the pension fund.

### Governance

There are two members of the Pension Fund Committee who are deferred or retired members of the pension fund. Cllr Philip Corthorne (Chairman), a deferred member; and Cllr Tony Eginton, a retired member. Each member is required to declare their interest at each meeting.

### Key Management Personnel

Three employees of the London Borough of Hillingdon hold key positions in the financial management of the London Borough of Hillingdon Pension Fund. These employees are the Section 151 officer, Deputy Director - Strategic Finance (post deleted September 2017) and the Head of Pensions, Treasury & Statutory Accounts. Total remuneration payable to key management personnel is set out below:



# Notes to Pension Fund Account

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	31 March 2018 £000's	31 March 2017 £000's
Short term benefits	82	69
Post employment benefits	84	31
	<b>166</b>	<b>100</b>

This note highlights the funding by the pension fund for key officers and pension benefits of those staff accrued in year.

The Pensions Committee of the London Borough of Hillingdon Pension Fund ("the Fund") has prepared an Investment Strategy Statement (ISS) in accordance with the DCLG Guidance on Preparing and Maintaining an Investment Strategy Statement.

As set out in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, the Pensions Committee will review this Statement from time to time, but at least every three years, and revise it as necessary. Also, in the event of a significant change, changes will be reflected within three months of the change occurring. The current version of the ISS is available on the pension fund pages of the Council's website: [www.hillingdon.gov.uk](http://www.hillingdon.gov.uk) and included in the Annual Report.

## 20. BULK TRANSFER

There was a bulk transfer of £31,049k into the fund from Harrow College as a result of a merger with Uxbridge College during the 2017/18 financial year. There were no bulk transfers in 2016/17.

## 21. CONTINGENT LIABILITIES AND CONTRACTUAL COMMITMENTS

Outstanding capital commitments (investments) as at 31 March 2018 totalled £23,859k (£46,472k at 31 March 2017).

These commitments relate to outstanding call payments due on unquoted limited partnership funds held in the Private Equity, Infrastructure and Credit Solutions (Permira) parts of the portfolio. The amounts called by these funds vary both in size and timing over a period of between four and six years from the date of each original commitment.

There were no contingent liabilities outstanding for the fund at the end of the financial year 2017/18.

## 22. CONTINGENT ASSETS

Three admitted body employers in the London Borough of Hillingdon Pension Fund hold insurance bonds to guard against the possibility of being unable 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.

## 23. POST BALANCE SHEET EVENTS

There are no post balance sheet events.

## **POLICY STATEMENTS**

Details of the following Statements can be found on the London Borough of Hillingdon website, using the links provided below.

### **Investment Strategy Statement**

From 1 April 2017, the Fund is required to publish an Investment Strategy Statement (ISS), which replaces the requirement for a Statement of Investment Principles. The ISS will be kept under review and will be updated whenever there is a change in Fund Manager or mandate. The current ISS is available at:

<http://www.hillingdon.gov.uk/article/6492/Pension-fund>.

### **Funding Strategy Statement**

Since 2004, administering authorities have been required to prepare, publish and maintain a Funding Strategy Statement (FSS). Pensions Committee approved the current FSS in March 2017 following the 2016 valuation. The statement is available at: <http://www.hillingdon.gov.uk/article/6492/Pension-fund>.

### **Communication Strategy**

The London Borough of Hillingdon Pension Fund's Communication Strategy was fully revised in 2016/17 and agreed at Pensions Committee in June 2017, and came into effect from 1 July 2017. It can be accessed at:

<http://www.hillingdon.gov.uk/article/6492/Pension-fund>

### **Governance Policy Statement**

Regulations introduced in December 2005 required Administering Authorities to publish and maintain a Governance Policy Statement. Pensions Committee approved the first statement in March 2008. Later amendment regulations then required that by 1 December 2008 a Governance Compliance Statement should be published which required the addition of a Governance Best Practice Compliance Statement. Governance arrangements of the fund are kept under review, and statements are updated with amendments, Pension Committee approved the latest version September 2017. The documents are available at:

<http://www.hillingdon.gov.uk/article/6492/Pension-fund> .

### **Risk Management Policy**

A risk management policy was introduced during 2016 as part of the work undertaken by the local Pension Board. While Committee regularly review Fund risks through the risk register, it was identified that a formal risk management policy had not been drafted. The policy is available at:

<http://www.hillingdon.gov.uk/article/6492/Pension-fund>

## Administration strategy

During 2016, it was agreed by Committee that best practice was to have an Administration Strategy and this was agreed in September 2016. The aims of the Pension Administration Strategy are to:

- ensure that the parties to which it relates are fully aware of their responsibilities under the Scheme, and
- outline the quality and performance standards expected of the Fund and its scheme employers to ensure the delivery of a high quality, timely and professional administration service. These performance standards are explained further in the employer service level agreement.

The strategy is available at: <http://www.hillingdon.gov.uk/article/6492/Pension-fund>

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## GLOSSARY

### **Active Management**

A style of management where the fund manager aims to outperform a **benchmark** by superior **asset allocation**, market timing or **stock selection** (or a combination of these).

### **Actuary**

An independent consultant who advises the Council on the financial position of the Fund. See **actuarial valuation**.

### **Actuarial Valuation**

This is an assessment done by an **actuary**, usually every three years. The actuary will work out how much money needs to be put into a pension fund to make sure pensions can be paid in the future.

### **Additional Voluntary Contribution (AVC)**

An option available to individuals to secure additional pensions benefits by making regular payments in addition to the 5.5%-12.5% of basic earnings payable.

### **Administering Authority**

In this instance, the 'Administering Authority' is London Borough Hillingdon. An administering authority is responsible, amongst other things, for maintaining member records, dealing with member queries/requests, investment of the fund and paying your LGPS pension.

### **Admitted Bodies**

Employers whose staff can become members of the Fund by virtue of an admission agreement made between the administering authority and the employer.

### **Asset Allocation**

The apportionment of a fund's assets between asset classes and/or world markets. The long-term strategic asset allocation of a fund will reflect the fund's investment objectives. In the short term, the fund manager can aim to add value through **tactical asset allocation** decisions.

### **Asset Liability Modelling**

Models the interaction and the allocation of assets to meet to meet present and future financial liabilities over time

### **Benchmark**

A yardstick against which the investment policy or performance of a fund manager can be compared. Each Fund's benchmark is customised, meaning that it is tailored to the Fund's **liability profile**.

**Bond**

A debt investment with which the investor loans money to an entity (company or government) that borrows the funds for a defined period of time at a specified interest rate.

**Book cost**

The value of an asset as it appears on a balance sheet, equivalent to how much was paid for the asset (less liabilities due). Book cost often differs substantially from **market value**.

**Broker**

An individual or firm that charges a fee or commission for executing buy and sell orders submitted by an investor.

**CARE**

'Career Average Revalued Earnings'. LGPS 2014 is a career average scheme, and is a method used for calculating pensions earned from April 2014.

**Commission**

A service charge assessed by an agent in return for arranging the purchase or sale of a security or real estate. The commission must be fair and reasonable, considering all the relevant factors of the transaction. (Underwriting commission)

**Corporate Bond**

A debt security issued by a corporation, as opposed to those issued by the government.

**Corporate Governance**

The system by which organisations are run, and the means by which they are responsible to their shareholders, employees and other stakeholders.

**Coupon**

The return earned on an investment. E.g. £5 received from a £100 debenture is the coupon.

**Creditors**

Amounts owed by the pension fund.

**Custody**

Safekeeping of securities by a financial institution. The custodian keeps a record of the client's investments and may also collect income; process tax reclaims and provide other services such as performance measurement.

**Debtors**

Amounts owed to the pension fund.

**Defined Benefit**

A type of pension plan in which an employer/sponsor promises a specified monthly benefit on retirement that is predetermined by a formula based on the

employee's earnings history, tenure of service and age, rather than depending directly on individual investment returns.

### **Derivative**

Used to describe a specialist financial instrument such as **options** or **futures contracts**. Financial instruments are agreements to buy or sell something, under terms laid out in a contract.

### **Diversification**

A risk management technique that mixes a wide variety of investments within a portfolio. It is designed to minimize the impact of any one security on overall portfolio performance.

### **Dividend**

Distribution of a portion of a company's earnings, decided by the board of directors, to a class of its shareholders. The amount of a dividend is quoted in the amount each share receives or in other words dividends per share.

### **Dividend Yield**

An indication of the income generated by a share, calculated as Annual Dividend per Share/Price per Share

### **Emerging Markets**

There are about 80 stock markets around the world of which 22 markets are generally considered to be mature. The rest are classified as emerging markets.

### **Equity**

Stock or any other security representing an ownership interest.

### **Ex-dividend**

Purchase of shares without entitlement to current dividends. This entitlement remains with the seller of the shares.

### **Final Salary Scheme**

An employer pension scheme, the benefits of which are linked to length of service and the final salary of the member (also known as defined benefit).

### **Fixed interest**

A loan with an interest rate that will remain at a predetermined rate for the entire term of the loan. See bond.

### **FTSE All-Share**

An arithmetically weighted index of leading UK shares (by market capitalisation) listed on the London Stock Exchange (LSE). The FTSE 100 Index covers only the largest 100 companies.

### **Funding Level**

A comparison of a scheme's assets and liabilities.

### **Futures Contract**

A contract to buy goods at a fixed price and on a particular date in the future. Both the buyer and seller must follow the contract by law.

### **Gilts**

The familiar name given to sterling, marketable securities (or bonds) issued by the British Government.

### **Hedge**

Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such as a **futures contract**.

### **Index Linked**

A **bond** that pays a coupon that varies according to some underlying index, usually the Consumer Price Index.

### **Liability Profile**

The future cash outflows for Scheme Member benefits as they mature.

### **LGPS**

Local Government Pension Scheme

### **LSE**

London Stock Exchange

### **Mandate**

The agreement between a client and investment manager laying down how the portfolio is to be managed, including performance targets.

### **Market Value**

A security's last reported sale price (if on an exchange) i.e. the price as determined dynamically by buyers and sellers in an open market. Also called market price.

### **Option**

The name for a contract where somebody pays a sum of money for the right to buy or sell goods at a fixed price by a particular date in the future. However, the goods do not have to be bought or sold.

### **Passive Management**

A style of fund management that aims to construct a portfolio to provide the same return as that of a chosen index.

### **Pension Fund**

A fund established by an employer to facilitate and organise the investment of employees' retirement funds contributed by the employer and employees. The **pension fund** is meant to generate stable growth over the long term, and provide pensions for employees when they reach the end of their working years and commence retirement.

### **Private Equity**

When equity capital is made available to companies or investors, but not quoted on a stock market. The funds raised through private equity can be used to develop new products and technologies, to expand working capital, to make acquisitions, or to strengthen a company's balance sheet. Also known as **development capital**.

### **Property Unit Trusts**

Pooled investment vehicles that enable investors to hold a stake in a diversified portfolio of properties

### **Quantitative Easing (QE)**

QE is monetary policy in which a central bank purchases government securities or other securities from the market in order to lower interest rates and increase the money supply

### **Resolution Bodies**

Scheme employers with the power to decide if an employee or group of employees can join the scheme

### **Return**

Synonymous with profit, be it income received, capital gain or income and capital gain in combination. Usually expressed as a percentage of the nominal value of the asset.

### **Risk**

The likelihood of performance deviating significantly from the average. The wider the spread of investment in an investment sector or across investment sectors, i.e. the greater the diversification, the lower the risk.

### **Scheme Employers**

Local authorities and other similar bodies whose staff automatically qualify to become members of the pension fund

### **Security**

An investment instrument, other than an insurance policy or fixed annuity, issued by a corporation, government, or other organisation, which offers evidence of debt or equity

### **Socially Responsible Investment (SRI)**

Investments or funds containing stock in companies whose activities are considered ethical.

### **Specialist Manager**

A fund management arrangement whereby a number of different managers each concentrate on a different asset class. A specialist fund manager is concerned primarily with **stock selection** within the specialist asset class. **Asset allocation** decisions are made by the investment committee, their consultant or by a specialist tactical asset allocation manager (or combination of the three).



## **Stock**

A type of security that signifies ownership in a corporation and represents a claim on part of the corporation's assets and earnings. Also known as shares or **equity**.

## **Stock Selection**

The process of deciding which stocks to buy within an asset class.

## **The Fund**

'The Fund' explicitly refers to London Borough of Hillingdon Pension Fund

## **Tracking Error**

An unplanned divergence between the price behaviour of an underlying stock or portfolio and the price behaviour of a benchmark. Reflects how closely the make-up of a portfolio matches the make-up of the index that it is tracking.

## **Transaction Costs**

Those costs associated with managing a portfolio, notably brokerage costs and taxes.

## **Transfer Value**

The amount transferred to/from another pension fund should a member change employment. The amount transferred relates to the current value of past contributions.

## **Transition**

To move from one set of investment managers to another

## **Underwriting**

The process by which investment bankers raise investment capital from investors on behalf of corporations and governments that are issuing securities (both equity and debt)

## **Unit Trust**

A pooled fund in which investors can buy and sell units on an ongoing basis

## **Unlisted Security**

A security that is not traded on an **exchange**

## **Unrealised Gains/ (losses)**

The increase/ (decrease) at year-end in the market value of investments held by the fund since the date of their purchase.

## **Yield**

The rate of income generated from a stock in the form of dividends, or the effective rate of interest paid on a bond, calculated by the coupon rate divided by the bond's market price. Furthermore, for any investment, yield is the annual rate of return expressed as a percentage.