



## **Pension Fund**

# Annual Report and Accounts

For the year ended 31 March 2017

The Durham County Council Pension Fund is registered with the Pension Schemes Registry  
No. 10079166

<b>Durham County Council Pension Fund</b>	<b>Page</b>
Preface.....	1
Contents .....	2
Introduction .....	3
The Local Government Pension Scheme.....	4
Management and Financial Performance Report.....	7
Investment Policy and Performance Report.....	15
Scheme Administration Report.....	24
Governance Compliance Statement.....	29
Pension Fund Accounts.....	38
Notes to Pension Fund Accounts .....	40
Appendix 1: Funding Strategy Statement.....	82
Appendix 2: Investment Strategy Statement .....	105
Appendix 3: Communications Policy Statement.....	118
Appendix 4: Participating Bodies and Contribution Rates.....	121
Appendix 5: Membership Statistics .....	122
Glossary of Terms .....	124
Contacts for Further Information.....	129

## **INTRODUCTION**

Welcome to the Annual Report and Accounts of the Durham County Council Pension Fund for the financial year ended 31 March 2017.

These are the key issues:

- Contributing members increased by 0.54% to 18,630;
- Market value of the Fund's assets increased from £2,321m to £2,692m (by 16.0%).

The report provides further information on these issues and on the activities and management of the Pension Fund during the year.

I hope this report provides useful information about your Pension Fund. However, it is important that we try to improve the quality and suitability of information provided within the report and feedback is welcomed.

For further information on Durham County Council Pension Fund or for providing me with your views on this report, contact details are provided at the end of the report.

**John Hewitt C.P.F.A.**  
**Corporate Director Resources**

29 September 2017

## **THE LOCAL GOVERNMENT PENSION SCHEME**

Durham County Council Pension Fund (the Fund) is part of the Local Government Pension Scheme (LGPS) administered by Durham County Council. It is a statutory scheme governed by regulations made under the Public Service Pensions Act 2013.

The Fund is currently administered in accordance with the following secondary legislation:

- LGPS Regulations 2013 (as amended)
- LGPS (Management and Investment of Funds) Regulations 2016
- LGPS (Transitional Provisions, Savings and Amendments) Regulations 2014 (as amended)

### **HOW THE SCHEME PRESENTLY WORKS**

The LGPS is required to be funded. Scheme funds, currently surplus to immediate pension benefit requirements, are invested in approved securities. The Fund must be sufficient to sustain future pension entitlements of past and present members. The Fund is financed by members and employers' contributions and earnings from investments.

Until 31 March 2014 the LGPS was classified as a final salary scheme whereby the annual pension and any retirement grant were paid based on the period of membership and (usually) the final twelve months pay. Benefits built up in the LGPS up to and including 31 March 2014 will continue to be calculated on a final salary basis.

With effect from 1 April 2014 the LGPS changed from a final salary scheme to a career average scheme. All benefits built up in the LGPS after 31 March 2014 will be calculated under the rules of the new career average scheme.

An independent actuarial valuation of the Fund is carried out every three years to review the assets and liabilities of the Fund and to determine the rate of contributions which the employers must make to the Fund. The most recent valuation applicable to the period covered by the report was undertaken as at 31 March 2016 and a report of the actuary is provided on page 27. The next review will take place during 2019/20 for the valuation as at 31 March 2019.

From 1 April 2014 contributors to the scheme are required to pay between 5.5% and 12.5% of their pensionable salary to the Fund. The rate they pay depends on which of nine different salary bands their pay falls into. Employee contributions qualify for income tax relief. Members may have additional voluntary contributions (AVCs) deducted from pay and paid into a personal fund. AVCs can be invested with any of the following companies: Standard Life, Prudential and Equitable Life (closed to new investors).

Contributors to the scheme can also choose to pay additional pension contributions (APCs) over a number of years or by a one-off payment to buy additional pension on retirement.

Members who leave the scheme may transfer their accrued benefits to other approved schemes. Members who leave with less than two years membership can choose to receive a refund of their contributions (less income tax) provided they have no other LGPS benefits and, in most circumstances, have not transferred other pension benefits. New

members may transfer benefits accrued with other schemes into the Fund (usually within a deadline of twelve months).

The scheme includes a 50/50 option which allows a member to contribute half of their normal contribution rate into the scheme in return for half of their normal pension. Under this option full life assurance and ill health cover is retained.

## **PENSION BENEFITS**

Membership builds up an annual pension at a rate of  $1/49^{\text{th}}$  of the amount of pensionable pay received for each year of membership (or half that rate under the 50/50 option). This annual pension amount is added to an individual's pension account and revalued at the end of each year in line with inflation.

Pension is determined at a rate of  $1/60^{\text{th}}$  of final pay for each year of membership between 1 April 2008 and 31 March 2014 and  $1/80^{\text{th}}$  of final pay for each year of membership before 1 April 2008.

Retirement grants are based on  $3/80^{\text{th}}$  of final pay for each year of membership before 1 April 2008. Although an automatic lump sum is not a feature of the retirement benefits after that date, retirees have the option to take a lump sum from the scheme up to certain limits, getting £12 of tax free lump sum for every £1 of annual (taxable) pension given up.

Where a member dies in service, a lump sum in the form of a death grant would be paid. This death grant is equal to three years' pay. Survivor's pensions are payable on the death of a scheme member to the scheme member's husband, wife, civil partner or eligible co-habiting partner at an accrual rate of  $1/160^{\text{th}}$ . The survivor pension for an eligible co-habiting partner only takes account of the member's pensionable service after 5 April 1988. Children's pensions are also payable to eligible children of deceased scheme members.

In the main, benefits can be paid upon leaving to a member with at least 2 years qualifying membership in the following circumstances:

- on reaching State Pension Age, without any early retirement reductions applied;
- between the age of 55 and State Pension Age, however early retirement reductions will normally apply where someone draws their pension benefits before State Pension Age. The amount of reduction that applies depends on the individual's age, sex, length of pensionable service and the date they joined the scheme;
- at any age, if the member retires on the grounds of permanent ill-health. Three different levels of ill-health benefit are payable, depending on how soon it is judged that an individual will be able to obtain gainful employment again in future. In the case of death in service, dependants' benefits are paid even if the membership is less than 3 months.
- at the age of 55 and, if the member retires by reason of redundancy or business efficiency.

If a member leaves with at least 2 years membership and is not entitled to immediate payment of benefits, and does not choose to transfer out their accrued benefits, deferred benefits are awarded. Deferred benefits are benefits which remain in the Fund and are paid when the member reaches retirement age. Such benefits are subject to inflationary increases between the date of leaving and the date of payment.

## **PENSION INCREASES**

Mandatory increases in pensions and deferred benefits are made in accordance with annual statutory Pension Increase (Review) Orders to help protect pensions against inflation. The pension increase is currently linked to the Consumer Price Index (CPI).

The following table shows the pension increases over the last 5 years:

<b><i>Effective Date</i></b>	<b><i>% Increase</i></b>
8 April 2013	2.2
7 April 2014	2.7
6 April 2015	1.2
11 April 2016	0.0
10 April 2017	1.0

Pensioners must be over the age of fifty five or have retired on ill-health grounds to receive the increase. Those in receipt of a widow's, widower's or dependant's benefit receive the increase regardless of age.

## MANAGEMENT AND FINANCIAL PERFORMANCE REPORT

### PENSION FUND COMMITTEE MEMBERS, MANAGERS AND ADVISERS

The Constitution of Durham County Council, as administering authority to the Fund, has delegated to the Pension Fund Committee powers and duties arising from the Public Service Pensions Act 2013 and Regulations made thereunder, regarding the administration and investment of funds.

In order to effectively carry out their role, the Committee obtains professional advice, as and when required, from suitably qualified persons, including external advisers, investment managers and officers of the Council. The members of the Pension Fund Committee and contact details of managers and advisers as at 31 March 2017 were as follows:

<b>PENSION FUND COMMITTEE:</b>	Durham County Council	Councillor Andrew Turner (Chairman)
	Members:	Councillor Watts Stelling (Vice Chairman)
		Councillor Jimmy Alvey
		Councillor Colin Carr
		Councillor Mark Davinson
		Councillor Bill Kellett
		Councillor John Lethbridge
		Councillor John Lindsay
		Councillor Joyce Maitland
		Councillor Nigel Martin
		Councillor John Shuttleworth
	Darlington Borough Council	Councillor I G Haszeldine
	Members:	Councillor S Harker
	Scheduled Body Representative	( Vacancy )
	Admission Body Representative	Mr J Norton
	Pensioner Representative	Mr D Ford
	Active Members Representative	( Vacancy )
	Further Education Colleges Representative	( Vacancy )
<b>STAFF OBSERVERS:</b>	UNISON	N Hancock
	GMB	D Clegg

<b>PENSION BOARD MEMBERS:</b>	Scheme Member Representatives	Mr N Hancock Mr G Sykes Mr I Densham
	Scheme Employer Representatives	Councillor Amanda Hopgood (Chair) Councillor Fraser Tinsley Vacant
<b>ADMINISTERING AUTHORITY OFFICERS:</b>	T Collins	Chief Executive
	C Longbottom, LLB	Head of Legal and Democratic Services
	J Hewitt (w.e.f. 18/10/16) } D McLure (retired 31/5/16) } P Darby (1/6/16 to 17/10/16)	Corporate Director Resources Interim Corporate Director Resources
<b>GLOBAL CUSTODIAN</b>	J P Morgan Europe Ltd	1 Chaseside, Bournemouth, BH7 7DA
<b>ACTUARY:</b>	AonHewitt	40 Queen Square, Bristol. BS1 4QP
<b>INVESTMENT MANAGERS:</b>	Aberdeen Asset Management	Bow Bells House, 1 Bread Street, London. EC4M 9HH
	AB Ltd	50 Berkeley Street, London. W1J 8HA
	Bank of New York Mellon	160 Queen Victoria Street, London. EC4V 4LA
	BlackRock Investment Management (UK) Ltd	12 Throgmorton Avenue, London. EC2N 2DL
	CB Richard Ellis Collective Investors Ltd	3 <sup>rd</sup> Floor, One New Change, London. EC4M 9AF
	Mondrian	10 Gresham Street, London. EC2V 7JD
	Royal London Asset Management Ltd	55 Gracechurch Street, London. EC3V 0UF
<b>INVESTMENT ADVISERS:</b>	Mercer Ltd	1 Tower Place West, Tower Place, London, EC3R 5BU



<b>AVC PROVIDERS:</b>	Equitable Life Assurance Society	PO Box 177, Walton Street, Aylesbury, Bucks. HP21 7YH
	Prudential	Local Government AVC Department, Stirling. FK9 4UE
	Standard Life	Standard Life House, 30 Lothian Road, Edinburgh. EH1 2DH
<b>AUDITOR:</b>	Mazars LLP	Tower Bridge House, St Katharine's Way, London. E1W 1DD
<b>BANKER:</b>	Lloyds Bank plc	PO Box 1000, Andover. BX1 1LT

## **RISK MANAGEMENT**

The Statement of Investment Principles was superseded by the Investment Strategy Statement (ISS) with effect from 1 April 2017, a copy of which is included as Appendix 2. This document sets out the roles of the Fund's investment managers and custodian, who have a responsibility for the management and safekeeping of the Pension Fund's assets. The Funding Strategy Statement (FSS), at Appendix 1, identifies the Fund's key risks and counter measures taken by the administering authority to mitigate those risks. The administering authority takes professional advice from the actuary, custodian and advisers before taking appropriate action.

The Fund's primary long-term risk is that the Fund's assets fall short of its liabilities (i.e. promised benefits payable to members). The Fund's assets are diversified to reduce exposure to market (price, currency and interest rate) risk and credit risk. The assets are divided between seven investment managers to further control risk. Asset allocation benchmarks have been set and performance is monitored relative to these benchmarks to ensure compliance with the Fund's investment strategy.

Liquidity risk is the risk that the Fund will not be able to meet its financial obligations as they fall due. The administering authority manages the Fund's liquidity position through a comprehensive cashflow management system to ensure cash is available when needed.

Note 16 of the Pension Fund's Accounts provides more detail on the nature and extent of risks arising from financial instruments and how the administering authority manages those risks.

The Pensions Administration team manages the risk of late payment of contributions by monitoring contribution payments, identifying cases of late payment and contacting employing bodies as appropriate.

Responsibility for the Fund's risk management rests with the Pension Fund Committee. The objective of the risk management strategy is to identify, manage and control the risks faced by the Fund whilst achieving a good return on investment. Risk is measured, in part, by the administering authority's risk management team as part of its assessment of the County Council's risks, and is reviewed as part of the independent governance review undertaken by the Pension Fund.

Performance of investment managers is reported monthly; reviews are carried out by officers on a monthly basis and by the Pension Fund Committee quarterly. A detailed summary of all internal audit reports and all external audit reports are reviewed by the Pension Fund Committee.

The investment managers and custodian are audited by companies outside of the administering authority's control. Their auditors produce Reporting Accountants Reports, which are made available and utilised to provide some level of assurance to the Pension Fund that the managers and custodian have effective internal controls in operation within their organisations.

**KEY FINANCIAL INFORMATION**

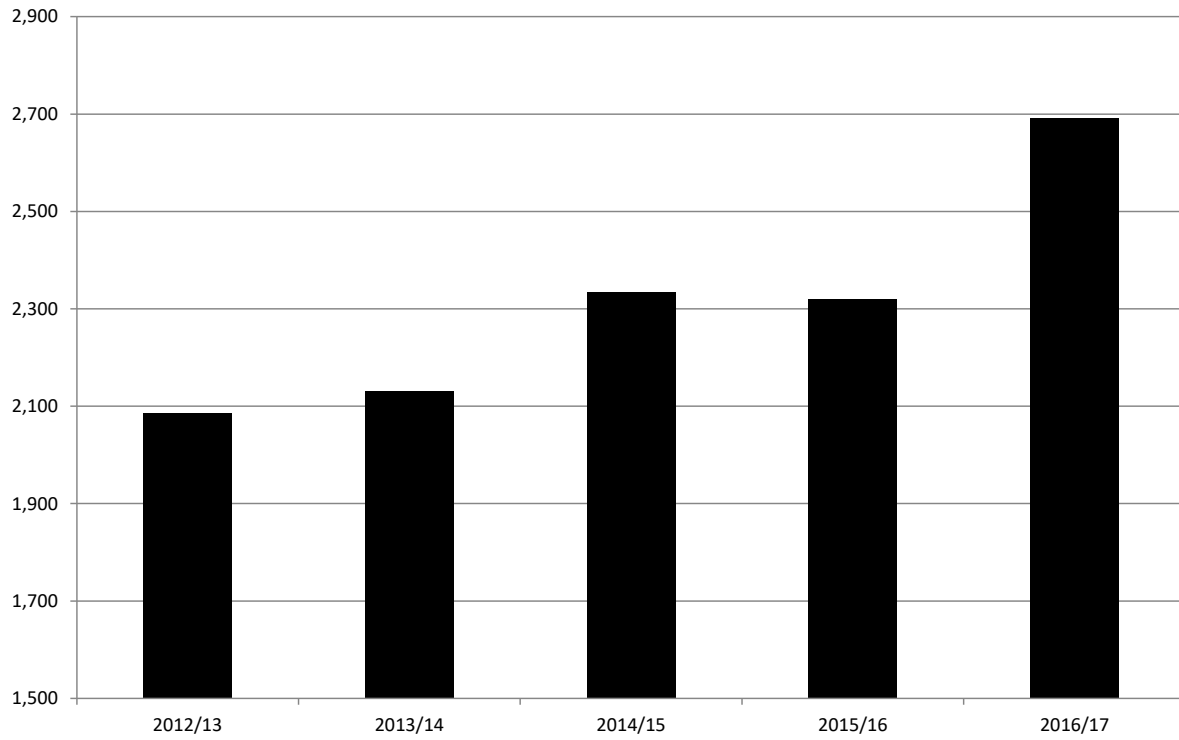
The following table and bar chart provide an overview of the Fund’s financial position as at the last five year ends. The key financial information over this time period is summarised below:

- Over the last 4 years the market value of the net assets has increased by 29.1% to £2,692.455m;
- Income from contributions has been gradually increasing; contributions received in 2015/16 were higher in comparison to other years due to the premature payment of deficit contributions by one employer;
- Pension benefit payments have been steadily rising over the 4 year period;
- Other expenses in 2013/14 were significantly higher due to a one-off payment relating to the bulk transfer of Durham Probation staff transferring out of the Fund;
- The increase in the market value of investments in 2016/17 was £366.723m, mainly due to favourable market conditions.

	<b>2012/13</b> <b>£000</b>	<b>2013/14</b> <b>£000</b>	<b>2014/15</b> <b>£000</b>	<b>2015/16</b> <b>£000</b>	<b>2016/17</b> <b>£000</b>
<b>Income</b>					
Contributions	93,884	96,800	98,848	112,035	106,715
Investment and other income	38,939	32,957	31,863	26,342	31,096
<b>Total Income</b>	<b>132,823</b>	<b>129,757</b>	<b>130,711</b>	<b>138,377</b>	<b>137,811</b>
<b>Expenditure</b>					
Benefits	95,978	96,669	101,419	110,422	114,152
Other expenses	15,849	38,683	15,432	16,758	19,144
<b>Net income</b>	<b>20,996</b>	<b>-5,595</b>	<b>13,860</b>	<b>11,197</b>	<b>4,515</b>
Increase (-Decrease) in market value of investments	175,578	50,990	190,260	-24,955	366,723
<b>Increase (-Decrease) in Fund during the year</b>	<b>196,574</b>	<b>45,395</b>	<b>204,120</b>	<b>-13,758</b>	<b>371,238</b>
<b>Net assets at 31 March</b>	<b>2,085,460</b>	<b>2,130,855</b>	<b>2,334,975</b>	<b>2,321,217</b>	<b>2,692,455</b>

## NET ASSETS OF THE FUND

The following graph shows how the net assets of the Fund have changed over the last five years:



**MEMBERSHIP**

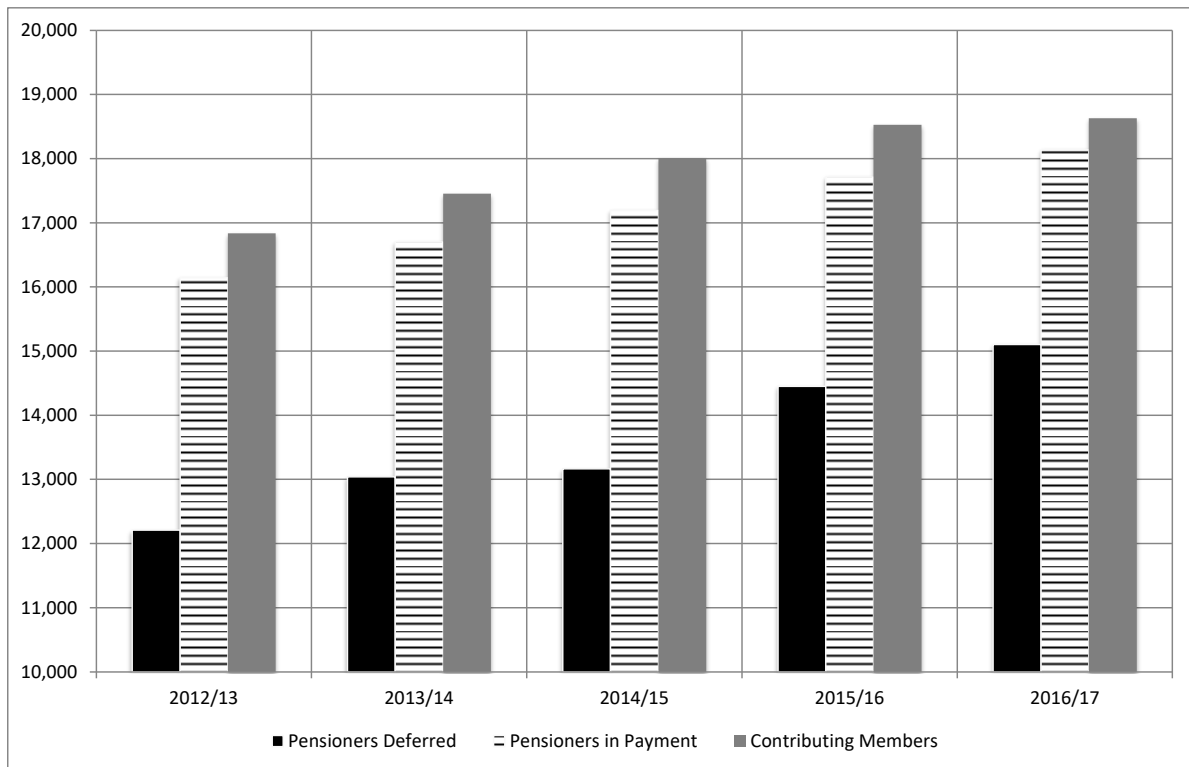
The Fund was established in 1974 to cover the future pension entitlement of all eligible employees of the County Council and former District Councils. The Fund excludes provision for teachers, police officers and fire-fighters, for whom separate arrangements exist. A number of other bodies also participate in the Scheme. These include Parish and Town Councils, Further Education Colleges, Academy Schools, Police and Fire Authorities (non-uniformed staff only) and Admission Bodies. Admission Bodies are those which are able to apply for membership of the Scheme under the Regulations. If the Pension Fund Committee agrees to the application, an Admission Agreement is drawn up admitting the body into the Scheme.

Appendix 4 provides a list of all organisations currently contributing to the Fund. It includes their contribution rates as set by the actuary, expressed as a percentage of employees’ pensionable pay, and additional annual payments for those participating bodies which would otherwise have a shortfall in contributions by the end of the recovery period. During 2016/17 the number of contributing members within the Pension Fund increased by 0.54% from 18,530 to 18,630.

The number of pensioners in receipt of payments from the Fund increased by 2.39% from 17,715 to 18,139.

The following table and bar chart provide a summary of contributing members, pensioners in payment and deferred pensioners over the last five years.

	2012/13	2013/14	2014/15	2015/16	2016/17
Contributing Members	16,837	17,454	18,011	18,530	18,630
Pensioners in Payment	16,386	16,700	17,193	17,715	18,139
Pensioners Deferred	12,211	13,040	13,165	14,451	15,104



Appendix 5 provides a detailed analysis of the numbers of pensionable employees and pensioners of the scheme at 31 March 2016 and 31 March 2017.

## **INVESTMENT POLICY AND PERFORMANCE REPORT**

### **INVESTMENT POWERS AND DUTIES**

Durham County Council, as administering authority, has delegated responsibility for the investment arrangements of the Fund to the Pension Fund Committee who decide on the investment policy most suited to the meet the liabilities of the Fund. The principal powers to invest are contained within the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 which permit a wide range of investments in the UK and overseas markets.

Income to the Fund is primarily from the contributions of the Fund members and their employers and from the interest and dividends received from investments. Income to the Fund, which is not required to pay pension and other benefits, must be invested having regard to the need for a suitably diversified portfolio of investments and the advice of appropriately qualified advisers.

### **FUNDING STRATEGY STATEMENT**

The Local Government Pension Regulations 2013 provide the statutory framework from which administering authorities are required to prepare a Funding Strategy Statement. A copy of the Funding Strategy Statement, which was revised during 2016/17 and is line with the fund's Investment Strategy Statement, is included at Appendix 1.

The purpose of the Funding Strategy Statement is to establish a clear and transparent fund specific strategy which will identify how employers' pension liabilities are best met going forward and to provide a means of supporting the requirement to maintain employer contribution rates at a level which is as constant as possible. The Statement raises the level of transparency and accountability, and provides a helpful context for adopting higher levels of communication with scheme employers.

### **INVESTMENT STRATEGY STATEMENT**

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 required administering authorities to prepare and maintain a written statement recording the investment policy of the Pension Fund, this was known as the Statement of Investment Principles.

These regulations were replaced by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 which were effective from 1 November 2016. In accordance with these 2016 regulations administering authorities, after taking proper advice, are required to formulate and publish a statement of its investment strategy, namely the Investment Strategy Statement. This document replaces the Pension Fund's former Statement of Investment Principles and is included as Appendix 2.

## ASSET ALLOCATION

The long-term strategic target asset allocations have been determined in line with the Fund's Investment Strategy Statement and following the advice of the Fund's investment adviser. The target asset allocations and actual asset allocations at 31 March 2016 and 31 March 2017, split between investment managers, are detailed in the table below.

Investment Manager	Asset Class	Investment Style	% Asset Allocation			
			at 31 March 2016		at 31 March 2017	
			Target	Actual	Target	Actual
Aberdeen	Global Equities	Active	15.00	14.79	15.00	16.45
AB	Global Bonds	Active	15.00	14.91	15.00	13.38
BNYM	Global Equities	Active	15.00	15.91	15.00	16.63
Barings	Dynamic Asset Allocation - all major asset classes	Active	0.00	0.01	0.00	0.00
BlackRock	Dynamic Asset Allocation - all major asset classes	Active	20.00	19.10	20.00	18.30
CBRE	Global Property	Active	8.00	8.18	8.00	8.09
Mondrian	Emerging Market Equities	Active	7.00	6.66	7.00	7.37
RLAM	Investment grade sterling bonds	Active	20.00	20.44	20.00	19.78
Totals			<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>

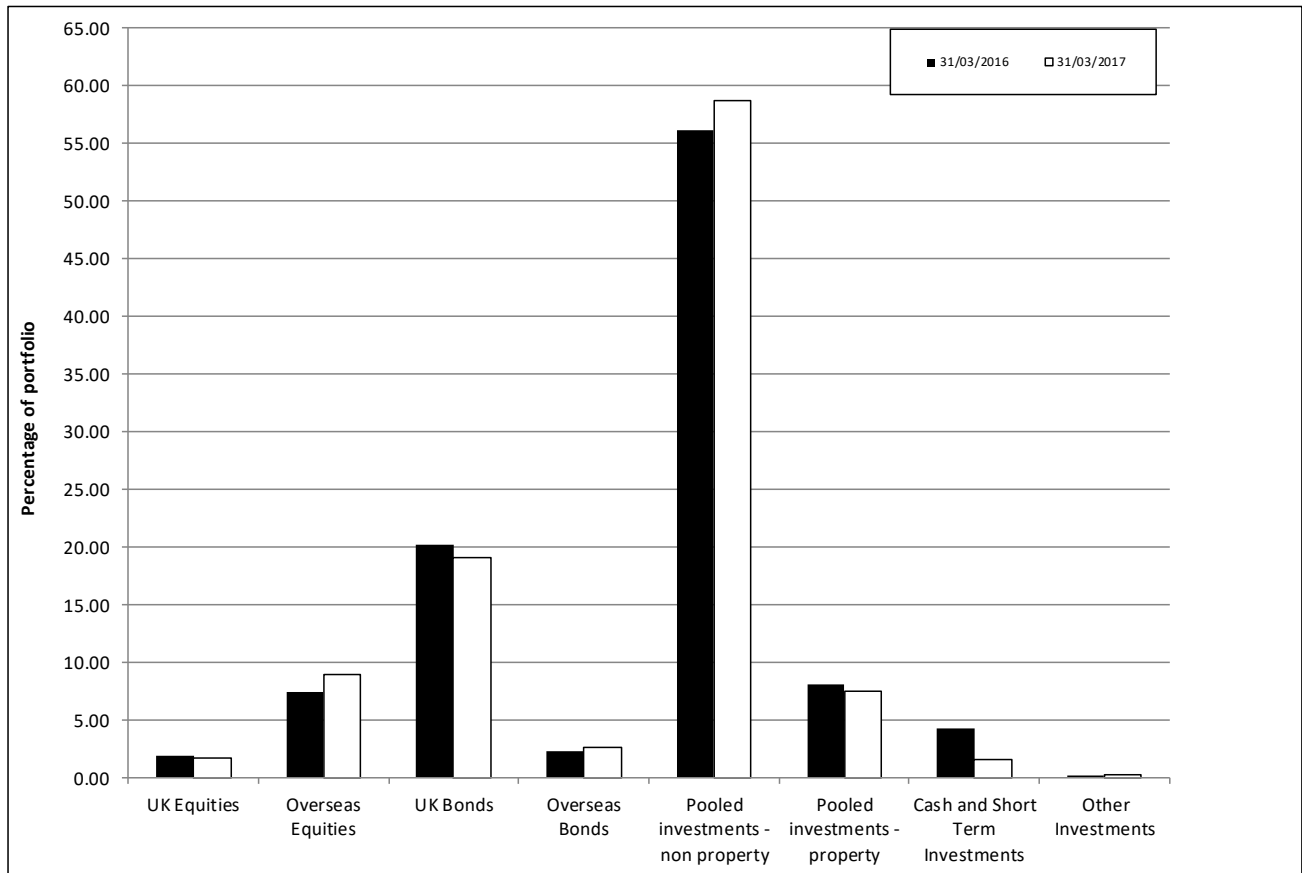
The small variances between the actual asset allocation and the target asset allocation are due to market movements.

An asset allocation rebalancing exercise is undertaken by the administering authority on a quarterly basis to bring the actual allocation of assets as close as possible to the target for each investment manager.



## DISTRIBUTION OF INVESTMENTS

The following graph shows the distribution of Fund investments (by market value) as at 31 March 2016 and 31 March 2017. Further details of the distribution are shown in Note 14 to the Pension Fund Accounts.



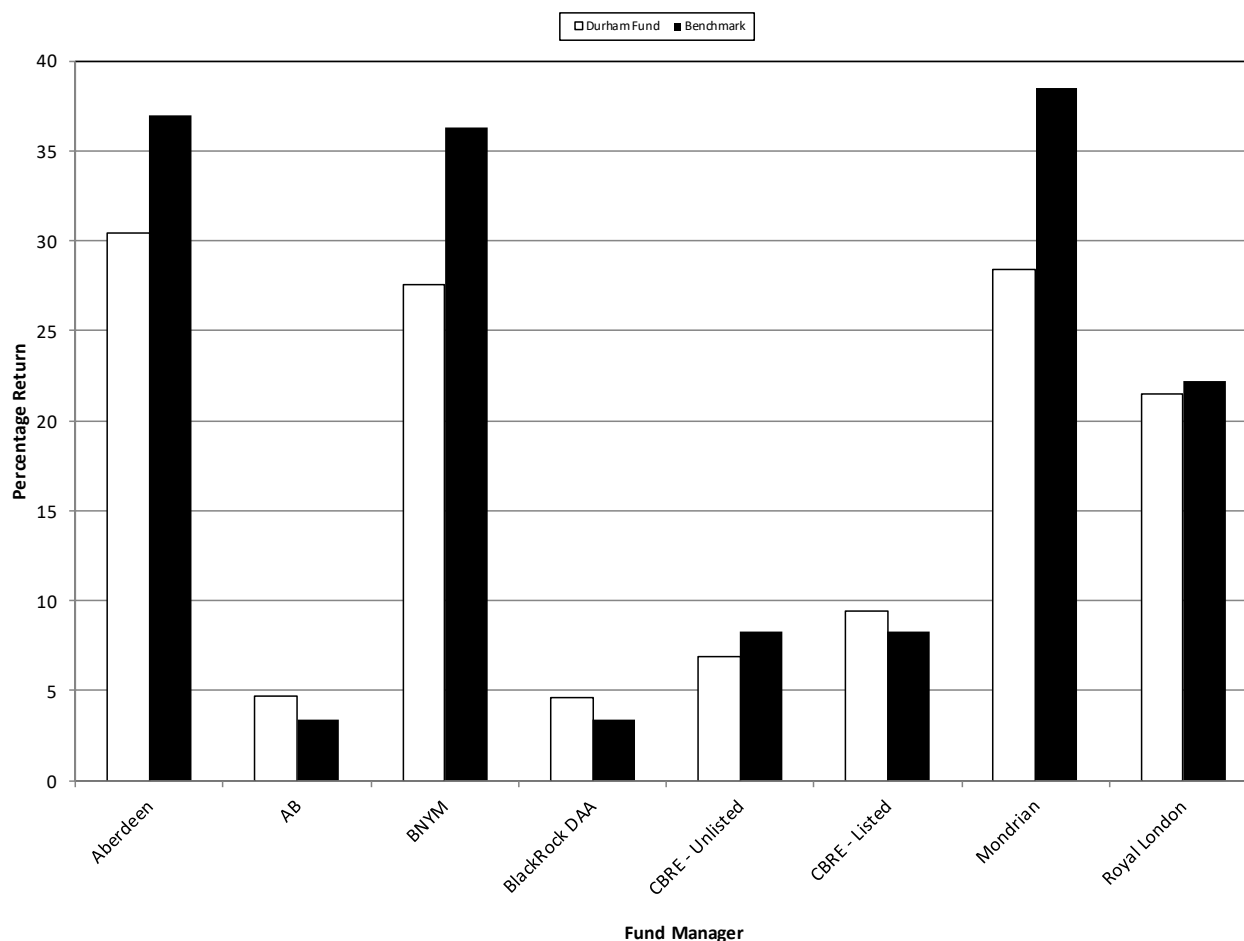
## INVESTMENT MONITORING AND PERFORMANCE STATISTICS

The performance of the investment managers is monitored and reported to the Pension Fund Committee on a quarterly basis, with an annual meeting to consider the full year's performance. At the quarterly meetings of the committee, the investments are reviewed and advice is given by independent advisers. The investment managers submit reports to the meetings giving detailed information on transactions, views on the economy and investment strategy, including any proposed changes in asset allocation and a valuation of the investments and cash under management as at the end of the quarter.

Performance measurement is undertaken by JP Morgan, the Pension Fund's Global Custodian. Performance reports are produced on a quarterly basis, and the results are considered by the Fund's independent investment advisers and reported to the Pension Fund Committee.

## TOTAL FUND PERFORMANCE

The following chart illustrates the performance of the Fund by Investment Manager in comparison to their benchmark for the 12 months to 31 March 2017.



The following table shows the actual performance of the total fund compared to the fund's benchmark and target as at 31 March 2017 for the last 1, 3 and 5 year periods.

	Performance (%) to 31 March 2017		
	1 year	3 years	5 years
<b>Total Fund</b>	<b>17.3</b>	<b>8.9</b>	<b>8.4</b>
Total Fund Benchmark	19.9	10.9	9.8
<b>Relative to Benchmark</b>	<b>-2.6</b>	<b>-2.0</b>	<b>-1.4</b>
Target	4.5	5.1	5.5
<b>Relative to Target</b>	<b>12.8</b>	<b>3.8</b>	<b>2.9</b>

The table shows that overall the Fund has underperformed its benchmark over the last 1, 3 and 5 years.

However, whilst the Fund has underperformed against its benchmark, a more important comparison for funding purposes is the comparison against the target return. The target of 4.5% is the required long-term annual rate of return assumed in the latest actuarial valuation as at 31 March 2016. The Fund produced a return well above the target during 2016/17 - outperforming by 12.8%.

## INVESTMENT MANAGERS' PERFORMANCE

The following tables show performance for each of the Pension Fund's investment managers in turn. In all cases the manager's benchmark and performance target are shown and the benchmark figures quoted include the out-performance objective.

### ABERDEEN

Aberdeen manages one half of the Fund's global equity portfolio. Their performance has been well below target since inception. Market conditions have not been favourable to the manager's style however improvements are expected if benchmark returns are less buoyant in future.

Currency GBP	Performance (%)	
	2016/17	Since inception in November 2014
<b>Aberdeen</b>	30.43	11.23
MSCI AC World index +3%	36.96	20.30
<i>Relative Performance</i>	-6.53	-9.07

### AB

AB manages the global bonds portfolio. It is important to note that the objective for this portfolio, and therefore its composition, is quite different from the matching bonds portfolio and this is reflected in the benchmark index. Their performance has been higher than target during the year but marginally below target since inception.

Currency GBP	Performance (%)	
	2016/17	Since inception in February 2008
<b>AB</b>	4.71	4.02
GBP Libor +3% pa	3.36	4.15
<i>Relative Performance</i>	1.35	-0.13

**BANK OF NEW YORK MELLON (BNYM)**

BNYM manages one half of the Fund's global equity portfolio. Their performance has been below target since inception and during the year.

Currency GBP	Performance (%)	
	2016/17	Since inception in November 2014
<b>BNYM</b>	27.59	17.11
MSCI AC World index +2.5%	36.29	19.91
<i>Relative Performance</i>	-8.70	-2.80

**BLACKROCK**

BlackRock manages the Dynamic Asset Allocation (DAA) portfolio. This is a very broad mandate, giving the manager freedom to seek value across asset categories, currencies and commodities. Their performance has been slightly higher than target during the year, but significantly below target since inception.

Currency GBP	Performance (%)	
	2016/17	Since inception in January 2015
<b>BlackRock</b>	4.59	1.57
3 month GBP Libor +3% pa	3.36	3.98
<i>Relative Performance</i>	1.24	-2.41

**CB RICHARD ELLIS INVESTORS (CBRE)**

CBRE manages the global real estate portfolio. The mandate is subdivided into listed and unlisted holdings.

The listed holdings returns, which tend to be highly correlated with those from equity markets in general, have outperformed the target during the year, whereas the unlisted holdings have underperformed against the target over the last 12 months and since inception.

Currency GBP	Performance (%)	
	2016/17	Since inception in February 2008
<b>CBRE - Unlisted</b>	6.89	3.60
Headline RPI +5% pa	8.28	7.83
<i>Relative Performance</i>	-1.39	-4.22
<b>CBRE - Listed</b>	9.44	6.32
Headline RPI +5% pa	8.28	7.83
<i>Relative Performance</i>	1.15	-1.51

**MONDRIAN**

Mondrian manages the emerging market equity portfolio.

Their performance has been well below target during the year and since inception. Market conditions have not been favourable to the manager's style however improvements are expected if benchmark returns are less buoyant in future.

Currency GBP	Performance (%)	
	2016/17	Since inception in November 2014
<b>Mondrian</b>	28.45	6.58
MSCI EM +2.5%	38.53	13.64
<i>Relative Performance</i>	-10.08	-7.07

**ROYAL LONDON ASSET MANAGEMENT (RLAM)**

RLAM manages the liability matching bonds portfolio. This is the lowest risk element of the Fund's strategy, relative to liabilities. Performance has been slightly above target during 2016/17.

Currency GBP	Performance (%)	
	2016/17	Since inception in February 2008
<b>Royal London</b>	21.47	9.90
FTSE index Linked >5 years +0.5% pa	22.25	9.98
<i>Relative Performance</i>	0.78	-0.08

## LGPS ASSET POOLING

On 1 November 2016 the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 came into force. These Regulations require all of the 88 Local Government Pension Scheme Funds (LGPS) in England and Wales to combine their assets into a small number of investment pools.

Under the regulations each LGPS administering authority must formulate, having taken proper advice, an investment strategy and publish a statement of that strategy no later than 1 April 2017 (as provided in Appendix 2). That investment strategy must include the administering authority's approach to pooling investments including the use of collective investment vehicles, and must be in accordance with guidance issued by the Secretary of State.

The Guidance states that each LGPS administering authority must commit to a suitable pool to achieve benefits of scale and must confirm their chosen investment pool meets the Investment Reform and Criteria issued in November 2015. The Secretary of State has direction and intervention powers if he is not satisfied that an administering authority is complying with its obligations in relation to the Regulations.

The Secretary of State approved the Border to Coast Pensions Partnership as meeting the requirements of the Investment Reform and Criteria document by letter dated 12 December 2016. At its meeting on 22 February 2017, the County Council agreed to become a member of the BCPP and adopt its arrangements.

### **BORDER TO COAST PENSIONS PARTNERSHIP (BCPP)**

The BCPP will be formed of the following 12 LGPS Funds with combined assets of over £40 billion as at 30 September 2016:

Bedfordshire Pension Fund	Northumberland Pension Fund
Cumbria Pension Fund	South Yorkshire Pension Fund
Durham Pension Fund	Surrey Pension Fund
East Riding Pension Fund	Teesside Pension Fund
Lincolnshire Pension Fund	Tyne and Wear Pension Fund
North Yorkshire Pension Fund	Warwickshire Pension Fund

In developing the BCPP proposal, both the independent specialist legal and financial advisers concluded that the most appropriate approach was to establish a separate vehicle in the form of a wholly owned company, i.e. BCPP Limited, which will be fully regulated by the Financial Conduct Authority (FCA).

Durham Pension Fund will be represented by the Chair of the Pensions Committee or any other person nominated from time to time on the Joint Committee, which will focus on investor issues of the partner funds, and in exercising voting rights at shareholder meetings.

The aim of the BCPP pooling proposal is to:

- i) meet the regulatory requirements of pooling assets by collectively investing;
- ii) deliver savings to the partner funds;

- iii) improve governance by moving the asset management into a financially regulated entity;
- iv) build capability and capacity to invest in infrastructure and other asset classes to improve the risk adjusted returns of partner Funds;
- v) through collaboration and consolidation of resource improve technical specialisms and resilience across Partner Funds;
- vi) use the scale of the pool to more effectively utilise shareholder voting rights to drive corporate governance change in the companies the Funds invest in.

BCPP Limited will be responsible for managing investments in line with the investment strategy and asset allocation requirements as instructed by the Durham County Council Pension Fund and the other partner funds. While there will be some changes required from the current processes, much will remain as is, for example instead of overseeing a range of external managers, the Pension Fund Committee will oversee a range of sub-funds managed by BCPP Limited. The Pension Fund Committee will therefore retain responsibility for setting the investment strategy and asset allocation of the Fund.

The key change is that responsibility for the appointment, monitoring and termination of investment managers will pass from the Pension Fund Committee to BCPP Limited. It is generally accepted that over 80% of investment performance is driven by determining the investment strategy and asset allocation, rather than selecting investment managers to implement that strategy.

Administering authorities are making progress in setting up the regulated asset management company, ensuring it is FCA regulated, appointing staff (including through transferring employment from funds within BCPP where appropriate), finding the most suitable location from which to operate and implementing all other necessary arrangements to facilitate pooling including the appointments of a depositary and custodian.

It is anticipated that assets will start to be transferred by partner funds into BCPP Limited with effect from June 2018.

## SCHEME ADMINISTRATION REPORT

Durham County Council is the administering authority for the Durham County Council Pension Fund and the scheme administration is the responsibility of the Corporate Director Resources. The costs of administering the scheme are charged to the Pension Fund.

Resources staff assist the Corporate Director Resources in his statutory duty to ensure that the Pension Scheme remains solvent and is administered effectively, adhering to the Local Government Pension Scheme Regulations in order to meet any current and future liabilities.

The Pensions Administration Team comprises 17 full time equivalent staff who provide a wide range of services including:

- administration of the affairs of Durham County Council Pension Scheme and also provision of services in connection with the pensions of teachers and uniformed fire officers;
- calculation of pensions and lump sums for retiring members of the LGPS and provision of early retirement estimates;
- administration of new starters in the Scheme;
- calculation of service credit calculations, outgoing transfer value calculations and divorce estimates for the Local Government and Fire Brigade Schemes;
- collection of employee and employer contributions to be invested into the LGPS;
- maintenance of the database of pension scheme members and provision of annual benefit statements and deferred benefit statements;
- production of newsletters for active and retired members;
- calculation of deferred pensions and refunds for early leavers;
- preparation of Pensions Fund Committee reports relating to benefits related issues;
- undertaking the annual pension increase exercise;
- calculation of widows and dependants benefits for retired and active members;
- dealing with the administration of in-house AVCs and APCs;
- working with Pension Fund employers to assist them in understanding and managing the cost of participation in the LGPS;
- liaison with the Actuary to provide information for the triennial valuation, annual accountancy disclosures and ad hoc costings for employers and prospective employers.

A team of 3.3 full time equivalent staff in Strategic Finance provide support to the Corporate Director Resources in his statutory role in relation to accounting and investment related activities for the Pension Fund, including:

- preparation of the Pension Fund Accounts for inclusion in Durham County Council's Statement of Accounts;
- preparation of the Annual Report and Accounts of the Pension Fund;
- liaison with External and Internal Audit;
- day-to-day accounting for the Pension Fund;
- completion of statistical and financial returns for Government and other bodies ;
- co-ordination of the production of FRS102/ IAS19 information for employers;



- preparation of Pension Fund Committee reports relating to investments and accounting issues;
- co-ordination of reports for Quarterly Pension Fund Committee meetings and the Pension Fund's Annual Meeting;
- liaison with Investment Managers, Advisers and Actuary;
- appointment of Investment Managers, Advisers and Actuary;
- monitoring and review of Investment Managers, Advisers and Actuary;
- preparation of the Investment Strategy Statement and Funding Strategy Statement;
- allocation of cash to Investment Managers;
- rebalancing of Investment Managers's portfolios to their target asset allocations;
- investment of the Fund's surplus cash balances;
- reconciliation of all Managers' purchases, sales and dividends received.

### Internal Dispute Resolution Procedure

The Pensions Advisory Services offer a free service to all members of the Pension Fund who have problems with their pensions. There are set procedures in the Local Government Pension Scheme Regulations for dealing with disputes about the pension scheme, namely the Internal Dispute Resolution Procedure. Under this procedure initial queries should be referred to the Employing Body or the Administering Authority's Pension Administration Team, who should be able to explain the reasons behind any decision made.

Following this, if a complainant has a dispute, the first stage of appeal is to refer it to the Adjudicator (currently an independent Pensions Officer from another Local Authority Pension Fund). If still not satisfied after that, the complaint must be referred to the Administering Authority in writing as a second stage appeal. A further referral is available to the Pensions Ombudsman.

The following table summarises the number of disputes made through the Fund's Internal Dispute Resolution Procedure at each stage of appeal.

	<b>2015-16</b>	<b>2016-17</b>
First Stage Appeals	<b>16</b>	<b>15</b>
Upheld	<b>5</b>	<b>3</b>
Declined	<b>11</b>	<b>12</b>
Ongoing	<b>0</b>	<b>0</b>
Second Stage Appeals	<b>2</b>	<b>1</b>
Upheld	<b>0</b>	<b>0</b>
Declined	<b>2</b>	<b>0</b>
Ongoing	<b>0</b>	<b>1</b>

## STATEMENT OF THE ACTUARY FOR THE YEAR ENDED 31 MARCH 2017

### INTRODUCTION

The accounts summarise the transactions and net assets of the Fund. They do not take account of liabilities to pay pensions and other benefits in the future. Actuarial valuations, which do take account of such liabilities, are carried out every three years.

The Scheme Regulations require that a full actuarial valuation is carried out every third year. The purpose of this is to establish that the Durham County Council Pension Fund (the Fund) is able to meet its liabilities to past and present contributors and to review employer contribution rates. The last full actuarial investigation into the financial position of the Fund was completed as at 31 March 2016 by Aon Hewitt Limited, in accordance with Regulation 62 of the Local Government Pension Scheme Regulations 2013.

### ACTUARIAL POSITION

1. The valuation as at 31 March 2016 showed that the funding ratio of the Fund had decreased since the previous valuation with the market value of the Fund's assets as at 31 March 2016 (of £2,321.2M) covering 81% of the liabilities allowing, in the case of pre- 1 April 2014 membership for current contributors to the Fund, for future increases in pensionable pay.
2. The valuation also showed that the aggregate level of contributions required to be paid by participating employers with effect from 1 April 2017 is:
  - 16.7% of pensionable pay. This is the rate calculated as being sufficient, together with contributions paid by members, to meet the liabilities arising in respect of service after the valuation date, (the primary rate)

**Plus**

  - Monetary amounts to restore the assets to 100% of the liabilities in respect of service prior to the valuation date over a recovery period of 21 years from 1 April 2017 (the secondary rate), equivalent to 7.9% of pensionable pay (or £28.6M in 2017/18, and increasing by 3.5% p.a. thereafter).
3. In practice, each individual Employer's or group of Employers' position is assessed separately and contributions are set out in Aon Hewitt Limited's report dated 31 March 2017 (the "actuarial valuation report"). In addition to the contributions shown above, payments to cover additional liabilities arising from early retirements (other than ill-health retirements) will be made to the Fund by the Employers.
4. The funding plan adopted in assessing the contributions for each individual Employer or group is in accordance with the Funding Strategy Statement. Different approaches adopted in implementing contribution increases and individual Employers' recovery periods were agreed with the Administering Authority reflecting the Employers' circumstances.

5. The valuation was carried out using the projected unit actuarial method for most employers and the main financial actuarial assumptions used for assessing the funding target and the contribution rates were as follows:

Discount rate for periods in service	
Scheduled bodies (1)	4.5% p.a.
Orphan bodies (2)	4.5% p.a.
Discount rate for periods after leaving service	
Scheduled bodies (1)	4.5% p.a.
Orphan bodies (2)	2.5% p.a.
Rate of pay increases	3.5% p.a.
Rate of increase to pension accounts	2.0% p.a.
Rate of increases in pensions in payment (in excess of Guaranteed Minimum Pension)	2.0% p.a.

- (1) *The scheduled body discount rate was also used for employers whose liabilities will be subsumed after exit by a scheduled body.*
- (2) *In addition the discount rate for already orphaned liabilities (i.e. where there is no scheme employer responsible for funding those liabilities) was 2.1% p.a. in service and left service.*

The assets were valued at market value.

Further details of the assumptions adopted for the valuation, including the demographic assumptions, are set out in the actuarial valuation report.

6. The valuation results summarised above are based on the financial position and market levels at the valuation date, 31 March 2016. As such the results do not make allowance for changes which have occurred subsequent to the valuation date.
7. The formal actuarial valuation report and the Rates and Adjustments Certificate setting out the Employer contribution rates for the period from 1 April 2017 to 31 March 2020 were signed on 31 March 2017. Contribution rates will be reviewed at the next actuarial valuation of the Fund as at 31 March 2019 in accordance with Regulation 62 of the Local Government Pension Scheme Regulations 2013.
8. This Statement has been prepared by the current Actuary to the Fund, Aon Hewitt Limited, for inclusion in the accounts of the Fund. It provides a summary of the results of their actuarial valuation which was carried out as at 31 March 2016. The valuation provides a snapshot of the funding position at the valuation date and is used to assess the future level of contributions required.

This Statement must not be considered without reference to the formal actuarial valuation report which details fully the context and limitations of the actuarial valuation.

Aon Hewitt Limited does not accept any responsibility or liability to any party other than our client, Durham County Council, the Administering Authority of the Fund, in respect of this Statement.

9. The actuarial valuation report is available on Durham County Council's website.

Aon Hewitt Limited

**May 2017**

## GOVERNANCE COMPLIANCE STATEMENT

Durham County Council is the Administering Authority for the Durham County Council Pension Fund.

The Council has delegated to the Pension Fund Committee various powers and duties in respect of its administration of the Fund.

This statement sets out the Fund’s scheme of delegation and the terms of reference, structure and operational procedures of the delegation, and the extent of its compliance with guidance issued by the Secretary of State (CLG) under the provisions of regulation 31 of the Local Government Pension Scheme Regulations 2008.

The following sections set out the principles of governance as prescribed in the CLG guidance and describe the Fund’s current arrangements for compliance.

Principle A – Structure	Fully compliant
<p>a) The management of the administration of benefits and strategic management of fund assets clearly rests with the main committee established by the appointing council.</p> <p>b) That representatives of participating LGPS employers, admitted bodies and scheme members (including pensioner and deferred members) are members of either the main or secondary committee established to underpin the work of the main committee.</p> <p>c) That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.</p> <p>d) That where a secondary committee or panel has been established, at least one seat on the main committee is allocated for a member from the secondary committee or panel.</p>	

The constitution of the Council delegates to the **Pension Fund Committee** “powers and duties arising from Section 7 of the Superannuation Act 1972 and Regulations made thereunder” regarding the administration of the Scheme and investment of funds, including:

- Approval of applications from bodies seeking admission to the Local Government Pension Scheme;
- Appointment of external investment managers and advisers.

The following function is delegated to the **Corporate Director of Resources** by the Council:

“To take all necessary actions of a routine nature to properly administer the financial affairs of the Council including ... the Council’s functions as a pension fund administering authority under the Superannuation Act 1972 and associated regulations.”

The structure of the Pension Fund Committee was reviewed in December 2008 and revised with effect from 1 April 2009 to reflect the composition of Durham County Council as a unitary authority from that date. The structure of the Pension Fund Committee is as follows:

<b>Body / category of bodies represented</b>	<b>Number of Committee Members</b>
Durham County Council	11
Darlington Borough Council	2
Colleges	1
Scheduled Bodies	1
Admitted Bodies	1
Active Members	1
Pensioners	1
<b>Total</b>	<b>18</b>
<i>(plus 2 non-voting union observers)</i>	

A secondary committee or panel has not been established due to the full extent of representation on the Committee.

<b>Principle B - Representation</b>	<b>Fully compliant</b>
<p>a) That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include:</p> <ul style="list-style-type: none"> <li>i) employing authorities (including non-scheme employers e.g. admitted bodies);</li> <li>ii) scheme members (including deferred and pensioner scheme members),</li> <li>iii) where appropriate, independent professional observers,</li> <li>iv) expert advisers (on an ad-hoc basis).</li> </ul> <p>b) That where lay members sit on a main or secondary committee they are treated equally in terms of access to papers and meetings, training and are given full opportunity to contribute to the decision making process, with or without voting rights.</p>	

The allocation of members to the Committee broadly reflects the number of active members, pensioners and deferred pensioners each of the larger employers has within the Fund.

The two Trade Union representatives are invited as observers.

The Committee does not consider it appropriate to appoint an independent professional observer to the Committee but these governance arrangements have been independently audited by AllenbridgeEPIC Investment Advisers on behalf of the Committee.

The Committee has appointed Philip Williams and PSolve Asset Solutions to provide independent investment advice.

All members of the Committee, union observers and independent advisers are given full access to papers and are allowed to participate in meetings.

<b>Principle C - Selection and role of lay members</b>	<b>Fully compliant</b>
<p>a) That committee or panel members are made fully aware of the status, role and function they are required to perform on either a main or secondary committee.</p> <p>b) That at the start of any meeting, committee members are invited to declare any financial or pecuniary interest related to specific matters on the agenda.</p>	

The representatives from Durham County Council and Darlington Borough Council are appointed by decisions of the respective councils.

The representatives of the Colleges, other Statutory Bodies, and Admitted Bodies are selected by the Committee from nominations made by the employers and appointed for a period of 4 years.

The two scheme member representatives are selected by the Committee from applications received from the membership following advertisement in the newsletter - one from active scheme members and one from pensioner members.

All Committee members are made fully aware of their role and functions as set out in the terms of reference for the Committee and other documentation.

Applicants from the scheme membership are provided with an information pack setting out the duties and responsibilities of a Pension Fund Committee Member together with a description of the type of individual qualities and experience seen as essential or desirable for the role.

All members are also made aware that as well as having legal responsibilities for the prudent and effective stewardship of the Fund, in more general terms they have a clear fiduciary duty to participating employers, local tax payers and scheme beneficiaries in the performance of their responsibilities.

There is a standing agenda item at the start of each meeting inviting members to declare any financial or pecuniary interest related to specific matters on the agenda.

<b>Principle D - Voting</b>	<b>Fully compliant</b>
a) The policy of individual administering authorities on voting rights is clear and transparent, including the justification for not extending voting rights to each body or group represented on main LGPS committees.	

All members appointed to the Committee have voting rights.

Union observers and advisers do not have voting rights as they do not act as formal members of the Committee.



<b>Principle E - Training/Facility Time/Expenses</b>	<b>Fully compliant</b>
<p>a) That in relation to the way in which statutory and related decisions are taken by the administering authority, there is a clear policy on training, facility time and reimbursement of expenses in respect of members involved in the decision-making process.</p> <p>b) That where such a policy exists, it applies equally to all members of committees, sub-committees, advisory panels or any other form of secondary forum.</p> <p>c) That the administering authority considers the adoption of annual training plans for committee members and maintains a log of all such training undertaken.</p>	

The Committee has established a policy on training, facility time and reimbursement of expenses which applies to all members of the Committee.

Consideration has been given to the adoption of annual training plans and the maintenance of a log of all such training undertaken.

<b>Principle F – Meetings (frequency/ quorum)</b>	<b>Fully compliant</b>
<p>a) That an administering authority’s main committee or committees meet at least quarterly.</p> <p>b) That an administering authority’s secondary committee or panel meet at least twice a year and is synchronised with the dates when the main committee sits.</p> <p>c) That an administering authority which does not include lay members in their formal governance arrangements, must provide a forum outside of those arrangements by which the interests of key stakeholders can be represented.</p>	

The Pension Fund Committee meets four times a year and occasionally holds special meetings when required. The Pension Fund Committee also holds an Annual General Meeting each year to which all employers are invited.

The quorum for each regular meeting of the Committee is 5.

<b>Principle G - Access</b>	<b>Fully compliant</b>
<p>a) That subject to any rules in the council’s constitution all members of main and secondary committees or panels have equal access to committee papers, documents and advice that falls to be considered at meetings of the main committee.</p>	

All members of the Committee have equal access to committee papers, documents and advice to be considered at each meeting. Public documents are posted on the website.

<b>Principle H - Scope</b>	<b>Fully compliant</b>
<p>a) That administering authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.</p>	

As set out in the terms of reference, the Committee regularly considers “wider issues” and not just matters relating to the investment of the Fund.

<b>Principle I - Publicity</b>	<b>Fully compliant</b>
<p>a) That administering authorities have published details of their governance arrangements in such a way that stakeholders with an interest in the way in which the scheme is governed, can express an interest in wanting to be part of those arrangements.</p>	

The Governance Compliance Statement is distributed to all employers, is reproduced in the Annual Report, and is published on the Council’s website. The appointment of member representatives was advertised to all members for them to express an interest.

Approved by the Pension Fund Committee  
29 November 2010



## **INDEPENDENT REVIEW OF GOVERNANCE ARRANGEMENTS**

I have undertaken an independent review of the Governance Compliance Statement and other statutory statements relating to the investment and administration of the Durham County Council Pension Fund.

In my opinion, the Pension Fund is compliant with the statutory requirements for the publication and review of a Governance Compliance Statement and, overall, the Pension Fund Committee demonstrates a high standard of governance in the operation of its responsibilities.

I am also satisfied that the Pension Fund complies with the statutory requirements relating to the Funding Strategy Statement, the Statement of Investment Principles (subject to updating in respect of compliance with Myners Principles), and the Communications Policy Statement.

In my review I have identified a number of recommendations for the Pension Fund Committee to consider to enhance governance compliance, bringing documentation up to date with industry-wide practice, and to improve transparency.

The current regulatory framework and good practice relating to governance continues to develop, and proposals are under consideration by the Department for Communities and Local Government (CLG). These developments will need to be considered and implemented as requirements change.

My conclusion is that the arrangements now in place for independent advice and review provide a robust basis for the Committee to maintain its governance standards in an efficient and effective manner.

Peter Scales  
Senior Adviser  
AllenbridgeEPIC Investment Advisers

16 November 2010

## **INDEPENDENT AUDITOR'S STATEMENT TO THE MEMBERS OF DURHAM COUNTY COUNCIL ON THE PENSION FUND FINANCIAL STATEMENTS**

We have examined the Pension Fund financial statements for the year ended 31 March 2017, which comprise the Fund Account, the Net Assets Statement and the related notes. This report is made solely to the members of Durham County Council, as a body, in accordance with Part 5 paragraph 20(5) of the Local Audit and Accountability Act 2014 and as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our work has been undertaken so that we might state to the members of Durham County Council those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Members of Durham County Council as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective responsibilities of the Corporate Director of Resources and the auditor**

As explained more fully in the Statement of the Corporate Director of Resources' Responsibilities, the Corporate Director of Resources is responsible for the preparation of the Pension Fund's financial statements in accordance with applicable United Kingdom law.

Our responsibility is to report to the Members of Durham County Council as a body, our opinion on the consistency of the Pension Fund financial statements within the Pension Fund Annual Report with the Pension Fund financial statements in the Statement of Accounts of Durham County Council, and its compliance with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.

We also read the other information contained in the Pension Fund annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Pension Fund financial statements. The other information consists only the Introduction, Management and Financial Performance Report, Investment Policy and Performance Report, Statement of the Actuary, Governance Compliance Statement, Funding Strategy Statement, Investment Strategy Statement, Communications Policy Statement, Participating Bodies and Contribution Rates, and Membership Statistics.

We conducted our work in accordance with Auditor Guidance Note 07 – Auditor Reporting, issued by the National Audit Office. Our report on the administering authority's full annual statement of accounts describes the basis of our opinion[s] on those financial statements.

## Opinion

In our opinion, the Pension Fund financial statements are consistent with the full annual Statement of Accounts of Durham County Council for the year ended 31 March 2017 and comply with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.



Mark Kirkham  
For and on behalf of Mazars LLP



Salvus House,  
Aykley Heads

**Fund Account**

2015-16			Notes	2016-17	
£000	£000			£000	£000
<b>DEALINGS WITH MEMBERS, EMPLOYERS AND OTHERS DIRECTLY INVOLVED IN THE FUND</b>					
-112,035		Contributions receivable	7	-106,715	
-3,680		Transfers in from other pension funds	8	-4,974	
-5		Other income		-3	
	-115,720				-111,692
110,422		Benefits payable	9	114,152	
5,273		Payments to and on account of leavers	10	7,270	
	115,695				121,422
	<b>-25</b>	<b>Net withdrawals/ -additions from dealings with members, employers and others</b>			<b>9,730</b>
	11,490	<b>Management expenses</b>	11		11,877
<b>RETURN ON INVESTMENTS</b>					
-22,662		Investment income	12	-26,122	
24,955		Profit and losses on disposal of investments and change in market value of investments	14	-366,723	
	<b>2,293</b>	<b>Net returns on investments</b>			<b>-392,845</b>
	<b>13,758</b>	<b>NET -INCREASE/ DECREASE IN THE NET ASSETS AVAILABLE FOR BENEFITS DURING THE YEAR</b>			<b>-371,238</b>

## Net Assets Statement

2015-16			2016-17		
£000	£000	Notes	£000	£000	
<b>INVESTMENT ASSETS</b>					
211,866		Equities	14	282,942	
519,293		Bonds	14	580,729	
<u>1,487,500</u>	2,218,659	Pooled investment vehicles	14	<u>1,778,540</u>	2,642,211
349		Loans	14	327	
Other cash deposits:					
79,484		Fund Managers	14	31,491	
17,217		Short term investments	14	8,431	
<u>12,880</u>	<u>109,930</u>	Derivative contracts	14	<u>4,524</u>	<u>44,773</u>
	2,328,589				2,686,984
<b>Other Investment Assets</b>					
1,925		Dividend accruals	14,17	1,766	
368		Tax recovery	14,17	480	
<u>13,388</u>	<u>15,681</u>	Other investment balances	14,17	<u>3,230</u>	<u>5,476</u>
	<b>2,344,270</b>	<b>Total Investment Assets</b>			<b>2,692,460</b>
<b>INVESTMENT LIABILITIES</b>					
-17,785		Derivative contracts	14	-2,989	
<u>-9,734</u>		Other investment balances	18	-1,981	
	<u>-27,519</u>	<b>Total Investment Liabilities</b>			<u>-4,970</u>
	<b>2,316,751</b>	<b>NET INVESTMENT ASSETS</b>			<b>2,687,490</b>
	833	<b>Long Term Assets</b>	17		625
<b>Current assets</b>					
8,563		Contributions due from employers	17	9,091	
<u>1,185</u>		Other current assets	17	<u>1,716</u>	
	9,748				10,807
<b>Current liabilities</b>					
<u>-6,115</u>		Current liabilities	18	<u>-6,467</u>	
	-6,115				-6,467
	<u><b>2,321,217</b></u>	<b>NET ASSETS OF THE FUND AVAILABLE TO PAY BENEFITS AT 31 MARCH</b>			<u><b>2,692,455</b></u>

The Pension Fund's accounts do not take account of obligations to pay pensions and benefits which fall due after the end of the reported accounting period. The actuarial present value of promised retirement benefits, which does take account of such obligations, is disclosed in Note 23.

These accounts should therefore be read in conjunction with the information contained within this note.

## 1. Fund Operation and Membership

Durham County Council Pension Fund (the Fund) is part of the Local Government Pension Scheme (LGPS) which is administered by Durham County Council. The Council is the reporting entity for the Fund. The LGPS is a statutory scheme governed by the following legislation:

- Public Services Pensions Act 2013
- LGPS Regulations 2013 (as amended)
- LGPS (Transitional Provisions, Savings and Amendments) Regulations 2014 (as amended)
- LGPS (Management and Investment of Funds) Regulations 2016

The Pension Fund Committee has responsibility delegated from Durham County Council to discharge the powers and duties arising from Section 7 of the Superannuation Act 1972 and Regulations made thereunder to ensure the effective stewardship of the Pension Fund's affairs. The delegation is wide ranging and covers the management of all of the Fund's activities, including the administration and investment of funds. The Committee meets at least quarterly to assess performance and annually to consider wider matters.

The Corporate Director Resources is responsible for the administration of the Pension Fund. He is assisted by the Pensions Administration and Pension Fund Accounting teams in his statutory duty to ensure the Pension Fund is administered effectively and remains solvent.

The Fund was established in 1974 to cover the future pension entitlement of all eligible employees of the County Council and former District Councils. The Fund excludes provision for teachers, police officers and firefighters for whom separate pension arrangements exist. A number of other scheduled and admitted bodies also participate in the Scheme.

The LGPS is a defined benefit occupational pension scheme to provide pensions benefits for pensionable employees of participating bodies. On retirement contributors receive annual pensions and where applicable lump sum payments. Entitlement to these benefits arises mainly on the grounds of reaching retirement age and retirement through early retirement schemes or being made redundant. Contributors who leave and who are not immediately entitled to these benefits may have their pension rights transferred or preserved until reaching retirement age.



The following table provides a summary of contributing members, pensioners in payment and deferred pensioners over the last five years.

	2012/13	2013/14	2014/15	2015/16	2016/17
Contributing Members	16,837	17,454	18,011	18,530	18,630
Pensioners in Payment	16,386	16,700	17,193	17,715	18,139
Pensioners Deferred	12,211	13,040	13,165	14,451	15,104

In comparison to the figures reported at 31 March 2016, the number of pensionable employees in the Fund at 31 March 2017 has increased by 100, the number of pensioners has increased by 424 and deferred pensioners have increased by 653.

Contributions represent the total amounts receivable from:

- employing authorities (of which there were 115 at 31 March 2017), at a rate determined by the Fund's Actuary, and
- pensionable employees, at a rate set by statute.

The Fund's total benefits and contributions are summarised in the following table:

2015-16			2016-17	
Benefits	Contributions		Benefits	Contributions
£000	£000		£000	£000
83,286	-70,340	Administering Authority	86,173	-71,078
20,567	-34,000	Scheduled Bodies	22,158	-28,273
6,569	-7,695	Admission Bodies	5,821	-7,364
<b>110,422</b>	<b>-112,035</b>		<b>114,152</b>	<b>-106,715</b>

## 2. Basis of Preparation

The Pension Fund accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the Code) issued by the Chartered Institute of Public Finance and Accountancy (CIPFA), which is based upon International Financial Reporting Standards (IFRS) as amended for the UK public sector.

The accounts have been prepared on an accruals and going concern basis.

The financial statements summarise the transactions and the net assets of the Pension Fund available to pay pension benefits. They do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial

valuations of the Fund, which do take account of such obligations, are carried out every three years. The Actuary completed a valuation during 2016/17, the results of which determined the contribution rates effective from 1 April 2017 to 31 March 2020. Details of the latest valuation are included in Note 22.

### **3. Statement of Accounting Policies**

#### **Significant accounting policies**

The accounting policies set out below have been applied consistently to all periods presented in these accounts. The accounts have been prepared on the accruals basis of accounting (except individual transfer values to and from the scheme, which are accounted for on a cash basis).

#### ***Fund Account***

##### **Contributions receivable**

Contribution income is categorised and recognised as follows:

- Normal contributions, from both members and employers, are accounted for on an accruals basis;
- Employers' augmentation contributions are accounted for in the year in which they become due;
- Employers' deficit funding contributions are accounted for in the year in which they become due in accordance with the Rates and Adjustment Certificate set by the actuary or on receipt, if earlier than the due date.

##### **Transfers to and from other schemes**

Transfer values represent amounts paid to or received from other local and public authorities, private, occupational or personal pension schemes in respect of pension rights already accumulated by employees transferring from or to the participating authorities. Individual transfer values paid and received are accounted for on a cash basis as the amount payable or receivable is not determined until payment is made and accepted by the recipient. Bulk (Group) transfers out and in are accounted for in full in the year in which the transfer value is agreed by Durham County Council Pension Fund.

##### **Pension benefits payable**

Pension benefits are recognised and recorded in the accounting records and reported in the financial statements as an expense in the period to which the benefit relates. Any amounts due, but yet to be paid, are disclosed in the Net Assets Statement as current liabilities.

##### **Management expenses**

All management expenses, which include administrative expenses, investment management expenses and oversight and governance costs, are accounted for on an accruals basis.

All staffing and overhead costs of the pensions administration team are allocated to the Pension Fund as administrative expenses.

Fees of the external Investment Managers and Custodian are agreed in the respective mandates governing their appointments. Note 11 provides further information regarding the basis of Investment Managers' Fees. Where an Investment Manager's fee note has not been received by the balance sheet date, an estimate based upon the market value of their mandate as at the end of the financial year is used for inclusion in the Fund Account.

Oversight and governance costs include costs relating to the pension fund accounting team, which are apportioned on the basis of staff time spent on the Fund and include all associated overheads, plus legal, actuarial and investments advisory services.

### **Investment income**

Investment income is accounted for as follows:

- income from equities is recognised in the fund account on the date stocks are quoted ex-dividend;
- income from fixed interest and index-linked securities, cash and short-term deposits is accounted for on an accruals basis;
- interest income is recognised in the fund account as it accrues;
- income from other investments is accounted for on an accruals basis;
- income from overseas investments is recorded net of any withholding tax where this cannot be recovered;
- foreign income has been translated into sterling at the date of the transactions, when received during the year, or at the exchange rates applicable on the last working day in March, where amounts were still outstanding at the year end;
- changes in the net market value of investments are recognised as income and comprise all realised and unrealised profits/ losses during the year.

### **Taxation**

The Fund is a registered public service scheme under Section 1(1) of Schedule 36 of the Finance Act 2004 and as such is exempt from UK income tax on interest received and from capital gains tax on the proceeds of investments sold. Income from overseas investments suffers withholding tax in the country of origin, unless exemption is permitted. Irrecoverable tax would normally be accounted for as a fund expense as it arises, however when Investment Managers are not able to supply the necessary information, no taxation is separately disclosed in the Fund Account.

### ***Net Assets Statement***

#### **Valuation of Investments**

Investments are included in the accounts at their fair value as at the reporting date. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

All prices in foreign currency are translated into sterling at the prevailing rate on the last working day of March.

An investment asset is recognised in the Net Assets Statement on the date the Fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes to the fair value of the asset are recognised by the Fund. The values of investments as shown in the Net Assets Statement have been determined as follows:

- Quoted equity securities traded on an exchange are accounted for on a bid market price basis, where Investment Managers provide valuations in this manner;
- Fixed interest securities traded on an exchange are accounted for at bid market price where Investment Managers provide valuations in this manner;
- Index linked securities are valued at bid market value where Investment Managers provide valuations in this manner;
- Unitised managed funds are valued at the closing bid price if bid and offer prices are reported by the relevant exchange and in the Investment Manager's valuation report. Single priced unitised managed funds are valued at the reported price;
- Unitised, unquoted managed property funds are valued at the net asset value adjusted for cash flows or a single price advised by the fund manager.
- Unquoted equity investments are included based on an estimated price of the investments held. Investment Managers use valuation techniques to establish a price at the year-end date based on an arm's length exchange given normal business considerations;
- Derivative contracts outstanding at the year-end are included in the Net Assets Statement at fair value (as provided by Investment Managers) and gains and losses arising are recognised in the Fund Account as at 31 March. The value of foreign currency contracts is based on market forward exchange rates at the reporting date. The value of all other derivative contracts is determined using exchange prices at the reporting date.

Where Investment Managers are unable to supply investment valuations in line with the above policies, valuations will be included as supplied by the Investment Manager, usually at mid-market price.

### **Cash and Cash Equivalents**

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with insignificant risk of change in value.

### **Contingent Assets**

A contingent asset arises where an event has taken place that gives a possible asset which will only be confirmed by the occurrence of uncertain future events not wholly within the control of the Pension Fund. Contingent assets are not recognised in the Net Assets Statement however details are disclosed in Note 21.

**Investment transactions**

Investment transactions arising up to 31 March but not settled until later are accrued in the accounts. All purchases and sales of investments in foreign currency are accounted for in sterling at the prevailing rate on the transaction date.

**Acquisition costs of investments**

Acquisition costs of investments are added to book cost at the time of purchase.

**Financial liabilities**

The Fund recognises financial liabilities at fair value as at the reporting date. A financial liability is recognised in the Net Assets Statement on the date the Fund becomes party to the liability. From this date any gains or losses arising from changes in the fair value of the liability are recognised by the Fund.

**Actuarial present value of promised retirement benefits**

The actuarial present value of promised retirement benefits is assessed on a triennial basis by the scheme actuary in accordance with the requirements of IAS 19 and relevant actuarial standards. As permitted under IAS 26 the Pension Fund has opted to disclose the actuarial present value of promised retirement benefits by way of a note to the accounts (Note 23).

**Additional Voluntary Contributions (AVCs)**

The Fund provides an additional voluntary contribution (AVC) scheme for its members, the assets of which are invested separately from those of the Fund. In accordance with LGPS Regulations, AVCs are not recognised as income or assets in the Pension Fund Accounts, however a summary of the scheme and transactions are disclosed in Note 19 to these accounts.

If, however, AVCs are used to purchase extra years' service from the Pension Fund, this is recognised as contribution income in the Fund's accounts on an accruals basis. Amounts received in this way can be found in Note 7 as additional contributions from members.

**Prior Period Adjustments**

Prior period adjustments may arise as a result of a change in accounting policies or to correct a material error. Material errors discovered in prior period figures are corrected retrospectively by amending opening balances and comparative amounts for the prior period. Disclosure notes have been provided within the notes to the accounts for all prior period restatements. There has been no impact on the Fund Account or value of the net assets of the Fund available to available to pay benefits.

**Events After the Reporting Period**

Events after the Balance Sheet date are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the Statement of Accounts is authorised for issue. Two types of events can be identified:

- Those that provide evidence of conditions that existed at the end of the reporting period - the Statement of Accounts is adjusted to reflect such events.
- Those that are indicative of conditions that arose after the reporting period - the Statement of Accounts is not adjusted to reflect such events, but where a category of events would have a material effect, disclosure is made in the notes of the nature of the events and their estimated financial effect.

Events taking place after the date of authorisation for issue are not reflected in the Statement of Accounts.

#### **4. Critical judgements in applying accounting policies**

The preparation of the statements in accordance with the Code of Practice on Local Authority Accounting requires management to make judgements, estimates and assumptions which affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. In applying the policies, the Pension Fund has to make certain judgements about complex transactions, or those involving uncertainty. Those with most significant effect are:

- the fair value of unquoted investments is highly subjective and based upon forward looking estimates and judgements involving many factors. The valuations of unquoted investments disclosed in the Net Assets Statement are based on the latest investor reports and financial statements provided by the fund managers of the underlying funds.
- the pension fund liability is calculated every three years by the appointed actuary. Assumptions underpinning the valuations are agreed with the actuary; the estimate is subject to significant variances based on changes to the underlying assumptions.

#### **5. Assumptions made about the future and other major sources of estimation uncertainty**

The Pension Fund Accounts contain estimated figures that are based upon assumptions made about the future or that are otherwise uncertain. Estimates are made taking into account historical experience, current trends and other relevant factors. However, the nature of estimation means that actual results may differ from the estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

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

Item	Uncertainties	Effect if actual differs from assumptions
Actuarial Valuation	Estimation of the net liability to pay pensions depends on a number of complex judgements including the discount rate used, the salary increase projections, expected changes in retirement ages, mortality rates and returns on pension fund assets. A firm of actuaries is engaged to provide the Fund with expert advice about the assumptions to be applied. Note 22 summarises the results of the actuarial valuation.	The Actuary calculated the funding ratio to be 81% as at 31 March 2016 (the last triennial valuation). If the following figures were to differ from the assumptions used in the calculation, there would be a reduction in the funding ratio to: <ul style="list-style-type: none"> <li>- 75% if life expectancy increases by 3 years</li> <li>- 67% if discount rate falls by 1%</li> <li>- 67% if inflation increases by 1%</li> <li>- 68% if equities fall by 25%</li> <li>- 78% if pensionable pay increases by 1%</li> </ul>
Fair Value of Investments	The Accounts are as at 31 March 2017 and all the investments held by the fund are valued as at that date using the best estimate possible of 'fair value', as detailed in 'Significant Accounting Policies - Valuation of Investments'.	The use of estimates for investment values is greatest for those assets classified at Level 3 which means there is a risk that these investments may be over/ under-stated in the accounts. The total value of Level 3 investments (explained in Note 15) is £165.4m at 31/3/17 (£154.1m at 31/3/16). In line with the market risk section within Note 16, there is a risk that the value of the Fund may be over/ under stated in the accounts by £23.99m (£21.73m at 31/3/16).

## 6. Post Net Assets Statement (Balance Sheet) Event

There have been no events after 31 March 2017 which require any adjustments to be made to these accounts.

## 7. Contributions Receivable

2015-16 £000		2016-17 £000
	<b>Employer contributions:</b>	
-49,770	Normal	-49,580
-6,400	Augmentation	-5,797
-32,827	Deficit funding	-28,059
	<b>Member contributions:</b>	
-22,929	Normal	-23,191
-109	Additional contributions	-88
<b>-112,035</b>		<b>-106,715</b>
-70,340	Administering Authority	-71,078
-34,000	Scheduled Bodies	-28,273
-7,695	Admission Bodies	-7,364
<b>-112,035</b>		<b>-106,715</b>

**8. Transfers in from other pension funds**

2015-16		2016-17
£000		£000
-3,680	Individual Transfers	-4,974
<u><u>-3,680</u></u>		<u><u>-4,974</u></u>

**9. Benefits Payable**

2015-16		2016-17
£000		£000
90,708	Pensions	93,285
22,514	Commutations and lump sum retirement benefits	23,344
2,035	Lump sum death benefits	2,167
-4,835	Recharged benefits	-4,644
<u><u>110,422</u></u>		<u><u>114,152</u></u>
83,286	Administering Authority	86,173
20,567	Scheduled Bodies	22,158
6,569	Admission Bodies	5,821
<u><u>110,422</u></u>		<u><u>114,152</u></u>

**10. Payments To And On Account Of Leavers**

2015-16		2016-17
£000		£000
153	Refunds to members leaving service	297
61	Payments for members joining state scheme	75
5,059	Individual transfers to other schemes	6,329
-	Group transfers to other schemes	569
<u><u>5,273</u></u>		<u><u>7,270</u></u>

**11. Management Expenses**

Administration expenses include the cost of the administering authority in supporting the Fund.

Investment management expenses include any expenses in relation to the management of the pension fund assets. Investment manager fees are based on the value of assets under management. A performance related fee, derived from a base fee plus a percentage of out-performance, is paid to three of the Fund's investment managers; an ad-valorem fee is payable to the other managers.



Oversight and governance costs include costs relating to the pension fund accounting team, plus legal, actuarial and investments advisory services.

2015-16 £000		2016-17 £000
854	Administration expenses	905
9,962	Investment Management expenses	10,330
674	Oversight and Governance costs	642
<u>11,490</u>		<u>11,877</u>

Included within oversight and governance costs is the external audit fee payable to Mazars LLP in 2016/17 of £0.026m (£0.026m in 2015/16). No fees have been paid to Mazars in 2016-17 in respect of non-audit work.

## 12. Investment Income

2015-16 £000		2016-17 £000
-5,089	Interest from bonds	-5,620
-6,860	Dividends from equities	-7,071
-102	Interest on cash deposits	-48
-10,611	Income from pooled investment vehicles	-13,383
<u>-22,662</u>		<u>-26,122</u>

## 13. Taxation

The Code requires that any withholding tax that is irrecoverable should be disclosed in the Fund Account as a tax charge, however as Investment Managers have not been able to supply information for the full year, no amount of irrecoverable withholding tax has been disclosed.

- **United Kingdom Income Tax**

The Fund is an exempt approved Fund under Section 1(1) Schedule 36 of the Finance Act 2004, and is therefore not liable to UK income tax on interest, dividends and property income, or to capital gains tax.

- **Value Added Tax**

As Durham County Council is the administering authority for the Fund, VAT input tax is recoverable on most fund activities.

- **Foreign Withholding Tax**

Income earned from investments in stocks and securities in the United States, Australia and Belgium is exempt from tax. In all other countries dividends are taxed at source and, where the tax paid at source is greater than the rate of tax under the 'Double Taxation Agreement', the excess tax is reclaimable except in the case of Malaysia.

## 14. Investments

### Analysis by Investment Manager

The following Investment Managers were employed during 2016/17 to manage the Pension Fund's assets:

- Aberdeen Asset Management Limited (Aberdeen)
- AB (Formerly AllianceBernstein Limited)
- Bank of New York Mellon Investment Management EMEA Limited (BNYM)
- BlackRock Investment Management UK Limited (BlackRock)
- CB Richard Ellis Collective Investors Limited (CBRE)
- Mondrian Investment Partners Limited (Mondrian)
- Royal London Asset Management (RLAM)

The long-term strategic allocation as at 31 March was as follows:

31 March 2016 %	Investment Manager	Asset Class	31 March 2017 %
15	Aberdeen	Global equities	15
15	AB	Global Bonds	15
15	BNYM	Global equities	15
20	BlackRock	Dynamic Asset Allocation	20
8	CBRE	Global property	8
7	Mondrian	Emerging Market Equities	7
20	RLAM	Investment grade sterling bonds	20
<b>100</b>			<b>100</b>

The actual allocations vary slightly from the long-term strategic allocations due to market movements. The actual market values of investments held by each Investment Manager as at 31 March were as follows :

31-Mar-16		Investment Manager	31-Mar-17	
£000	%		£000	%
339,124	14.79	Aberdeen	440,069	16.45
341,874	14.91	AB	357,972	13.38
364,837	15.91	BNYM	444,824	16.63
198	0.01	Barings	-	-
437,984	19.10	BlackRock	489,644	18.30
187,755	8.18	CBRE	216,266	8.09
152,726	6.66	Mondrian	197,224	7.37
28	-	Other - NEL	-	-
468,712	20.44	RLAM	529,238	19.78
<b>2,293,238</b>	<b>100.00</b>		<b>2,675,237</b>	<b>100.00</b>

The totals in the above table include all assets held by Investment Managers on behalf of the Fund, including cash and derivatives. The total as at 31 March 2017 excludes loans of £0.327m, cash invested by the administering authority of £8.431m, other investment assets of £5.476m and other investment liabilities of £1.981m (£0.349m, £17.217m, £15.681m and £9.734m respectively as at 31 March 2016).

Of the total value of net investment assets reported in the Net Assets Statement as at 31 March 2017, £2.675m (99.54%) is invested through Investment Managers (£2.293m or 98.99% at 31 March 2016).

### Reconciliation of Movements in Investments 2016/17

Investment category	Value at 31 March 2016	Purchases at cost	Sales proceeds	Change in market value	Value at 31 March 2017
	£000	£000	£000	£000	£000
Equities	211,866	124,863	-107,999	54,212	282,942
Bonds	519,293	2,714,495	-2,756,492	103,433	580,729
Pooled investment vehicles	1,487,500	233,241	-203,684	261,483	1,778,540
	<u>2,218,659</u>	<u>3,072,599</u>	<u>-3,068,175</u>	<u>419,128</u>	<u>2,642,211</u>
Derivative contracts:					
Futures, margins & options	-691	28,754	-20,561	-6,768	734
Forward foreign currency	-4,214	139,497	-90,544	-43,938	801
	<u>2,213,754</u>	<u>3,240,850</u>	<u>-3,179,280</u>	<u>368,422</u>	<u>2,643,746</u>
Other investment balances:					
Loans	349				327
Other cash deposits	96,701			-1,699	39,922
Dividend accruals	1,925				1,766
Tax recovery	368				480
Other investment balances	3,654				1,249
<b>Net Investment Assets</b>	<u><b>2,316,751</b></u>			<u><b>366,723</b></u>	<u><b>2,687,490</b></u>

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

**Reconciliation of Movements in Investments 2015/16 (Restated)**

Investment category	Value at 31 March 2015	Purchases at cost	Sales proceeds	Change in market value	Value at 31 March 2016
	£000	£000	£000	£000	£000
Equities	234,213	103,326	-105,533	-20,140	211,866
Bonds	564,765	2,025,849	-2,077,720	6,399	519,293
Pooled investment vehicles	1,392,430	228,960	-142,369	8,479	1,487,500
	<b>2,191,408</b>	<b>2,358,135</b>	<b>-2,325,622</b>	<b>-5,262</b>	<b>2,218,659</b>
Derivative contracts:					
Futures, margins & options	3,102	41,841	-38,621	-7,013	-691
Forward foreign currency	-3,877	70,728	-56,678	-14,387	-4,214
	<b>2,190,633</b>	<b>2,470,704</b>	<b>-2,420,921</b>	<b>-26,662</b>	<b>2,213,754</b>
Other investment balances:					
Loans	375				349
Other cash deposits	165,402			1,707	96,701
Dividend accruals	1,815				1,925
Tax recovery	276				368
Other investment balances	-25,294				3,654
<b>Net Investment Assets</b>	<b>2,333,207</b>			<b>-24,955</b>	<b>2,316,751</b>

The 2015/16 note has been restated to include omitted Forward Foreign Currency transactions. The total Change in Market Value remains unchanged

Purchases and sales of derivatives are recognised in the Reconciliation of Movements in Investments tables as follows:

- Futures – on close out or expiry of the futures contract the variation margin balances held in respect of unrealised gains or losses are recognised as cash receipts or payments, depending on whether there is a gain or loss.
- Options – premiums paid and received are reported as payments or receipts together with any close out costs or proceeds arising from early termination.
- Forward currency contracts – forward foreign exchange contracts settled during the period are reported on a net basis as net receipts and payments.

## Analysis of Investments

2015-16 (Restated)			2016-17	
£000	£000		£000	£000
<b>ASSETS INVESTED THROUGH FUND MANAGERS</b>				
<b>Bonds</b>				
466,549		UK - Public sector - quoted	511,012	
33,455		Overseas - Public sector - quoted	69,717	
19,289		Overseas - Corporate - quoted	-	
	519,293			580,729
<b>Equities</b>				
41,520		UK quoted	45,087	
28		UK unquoted	-	
170,318		Overseas quoted	237,855	
	211,866			282,942
<b>Pooled Investment Vehicles</b>				
80,400		Managed funds - non property - UK quoted	113,196	
1,221,371		Managed funds - non property - overseas quoted	1,465,519	
1,815		Unit Trusts - property - UK quoted	2,086	
32,729		Unit Trusts - property - UK unquoted	23,510	
29,804		Unit Trusts - property - Overseas quoted	32,289	
121,381		Unit Trusts - property - Overseas unquoted	141,940	
	1,487,500			1,778,540
<b>Derivative Contracts</b>				
12,880		Assets	4,524	
-17,785		Liabilities	-2,989	
	-4,905			1,535
79,484	79,484	<b>Fund Managers' cash</b>	31,491	31,491
<b>2,293,238</b>		<b>NET ASSETS INVESTED THROUGH FUND MANAGERS</b>		<b>2,675,237</b>
<b>OTHER INVESTMENT BALANCES</b>				
17,217		Short term investments (via DCC Treasury Management)		8,431
349		Loans		327
15,681		Other investment assets		5,476
-9,734		Other investment liabilities		-1,981
<b><u>2,316,751</u></b>		<b>NET INVESTMENT ASSETS</b>		<b><u>2,687,490</u></b>

The 2015-16 Pooled Investment Vehicles figures have been restated to show the reclassification of £341.874m from Managed funds - non property - overseas unquoted to Managed funds - non property - overseas quoted following additional information received from our Fund Managers. The total remains unchanged.

## Analysis of Derivatives

### Objectives and policies for holding derivatives

Derivatives are financial instruments that derive their value from the price or rate of some underlying item. Underlying items include equities, bonds, commodities, interest rates, exchange rates and stock market indices.

The Fund uses derivatives to manage its exposure to specific risks arising from its investment activities. Derivatives may be used to gain exposure to an asset more efficiently than holding the underlying asset or hedge against the risk of adverse currency movement on the Fund's investments. The use of derivatives is managed in line with the investment management agreement agreed between the Pension Fund and its Investment Managers.

A summary of the derivative contracts held by the Pension Fund is provided in the following table:

2015-16		Derivative Contracts	2016-17	
£000	£000		£000	£000
8,399		<b>Forward foreign currency</b>		
<u>-12,613</u>		Assets	2,671	
	-4,214	Liabilities	<u>-1,870</u>	
		<b>Net Forward foreign currency</b>		801
		<b>Futures</b>		
1,232		Assets	585	
<u>-1,388</u>		Liabilities	<u>-155</u>	
	-156	<b>Net Futures</b>		430
		<b>Options</b>		
3,249		Assets	1,268	
<u>-3,784</u>		Liabilities	<u>-964</u>	
	-535	<b>Net Options</b>		304
	<u><b>-4,905</b></u>	<b>Net market value of derivative contracts</b>		<u><b>1,535</b></u>

The Pension Fund invests in the following types of derivatives:

#### i. Forward foreign currency contracts

Currency is bought and sold by investment managers for future settlement at a predetermined exchange rate. Such contracts are used to hedge against the risk of adverse currency movements on the Fund's investments.

The following tables list all of the forward foreign currency contracts held by the investment managers (BlackRock, CBRE and Royal London) on 31 March 2017 and 31 March 2016.

Settlement	Currency bought	Local Value	Currency sold	Local Value	Asset Value £000	Liability Value £000
1 to 3 mths	USD	1,470,000	AUD	-1,914,703	9	
1 to 3 mths	USD	1,210,000	BRL	-3,802,062	25	
1 to 3 mths	USD	10,850,000	CAD	-14,150,896	184	
1 to 3 mths	USD	8,120,000	CHF	-8,058,126	31	
1 to 3 mths	USD	6,200,000	CLP	-3,990,940,000	152	
1 to 3 mths	GBP	49,018,213	EUR	-57,120,000	88	
1 to 3 mths	EUR	2,200,000	GBP	-1,915,903		-31
1 to 3 mths	SEK	27,573,779	EUR	-2,920,000		-28
1 to 3 mths	EUR	41,860,000	USD	-44,711,085	157	
1 to 3 mths	GBP	3,358,132	JPY	-470,000,000		-18
1 to 3 mths	GBP	5,150,000	PLN	-26,102,260		-107
1 to 3 mths	GBP	2,200,966	TRY	-10,380,000		-32
1 to 3 mths	GBP	1,585,000	USD	-1,973,404	9	
1 to 3 mths	GBP	40,444,159	USD	-50,355,000	236	
1 to 3 mths	GBP	1,585,000	USD	-1,973,420	9	
1 to 3 mths	GBP	40,443,834	USD	-50,355,000	236	
1 to 3 mths	GBP	1,590,000	USD	-1,980,459	9	
1 to 3 mths	GBP	40,423,195	USD	-50,350,000	219	
1 to 3 mths	USD	13,000,000	GBP	-10,619,874		-240
1 to 3 mths	USD	1,000,000	GBP	-801,852		-3
1 to 3 mths	USD	2,200,000	HKD	-17,052,792	2	
1 to 3 mths	IDR	21,845,700,000	USD	-1,620,000	9	
1 to 3 mths	INR	122,491,750	USD	-1,810,000	55	
1 to 3 mths	USD	1,200,000	KRW	-1,365,468,000		-18
1 to 3 mths	KRW	1,370,820,000	USD	-1,200,000	22	
1 to 3 mths	USD	10,210,000	MXN	-210,977,092		-703
1 to 3 mths	MYR	10,822,105	USD	-2,410,000	16	
1 to 3 mths	PHP	283,052,150	USD	-5,615,000		-3
1 to 3 mths	USD	1,660,000	SGD	-2,352,094		-19
1 to 3 mths	SGD	850,726	USD	-600,000	7	
1 to 3 mths	USD	3,880,000	THB	-135,889,240		-65
1 to 3 mths	USD	6,630,000	TRY	-24,967,917		-77
1 to 3 mths	USD	11,370,000	TWD	-347,626,380		-78
1 to 3 mths	AUD	11,299,503	GBP	-6,862,949		-3
1 to 3 mths	EUR	34,743,034	GBP	-30,033,616	263	
1 to 3 mths	USD	87,011,920	GBP	-69,340,495		-97
1 to 3 mths	JPY	1,889,517,790	GBP	-13,570,223		-6
1 to 3 mths	AUD	5,355,688	GBP	-3,252,870		-1
1 to 3 mths	USD	895,848	GBP	-713,908		-1
1 to 3 mths	JPY	164,020,249	GBP	-1,177,968		-1
1 to 3 mths	EUR	3,787,663	GBP	-3,274,245	28	
1 to 3 mths	USD	177,005	GBP	-141,057	-	
1 to 3 mths	DKK	16,843,346	GBP	-1,954,211	13	
1 to 3 mths	SEK	12,750,547	GBP	-1,157,457	13	
1 to 3 mths	JPY	972,939,089	GBP	-6,987,497		-3
1 to 3 mths	USD	2,510,935	GBP	-2,000,984		-3
1 to 3 mths	GBP	6,518,048	AUD	-10,486,913	139	
1 to 3 mths	GBP	2,897,543	CAD	-4,740,597	57	
1 to 3 mths	GBP	1,813,142	EUR	-2,086,806	25	
1 to 3 mths	GBP	2,221,207	USD	-2,711,838	56	
1 to 3 mths	GBP	8,875,167	USD	-10,812,261	244	
1 to 3 mths	GBP	837,978	EUR	-962,538	13	
1 to 3 mths	GBP	3,208,536	USD	-3,907,054	90	
1 to 3 mths	GBP	2,128,388	USD	-2,597,235	55	
1 to 3 mths	GBP	1,187,053	CAD	-1,951,331	18	
1 to 3 mths	GBP	1,200,107	USD	-1,469,644	27	
1 to 3 mths	GBP	1,921,738	USD	-2,352,067	44	
1 to 3 mths	USD	1,584,001	GBP	-1,293,520		-29
1 to 3 mths	USD	9,553,117	GBP	-7,714,928		-88
1 to 3 mths	USD	2,020,893	GBP	-1,630,774		-17

Notes to Pension Fund Accounts

1 to 3 mths	USD	3,397,540	GBP	-2,738,373		-26
1 to 3 mths	CAD	3,404,106	GBP	-2,055,502		-16
1 to 3 mths	USD	5,756,705	GBP	-4,601,767		-6
1 to 3 mths	AUD	6,214,777	GBP	-3,804,205		-24
1 to 3 mths	USD	1,292,779	GBP	-1,034,930		-3
1 to 3 mths	GBP	9,094,175	EUR	-10,514,712	86	
1 to 3 mths	GBP	1,047,287	EUR	-1,209,613	11	
1 to 3 mths	GBP	7,377,220	USD	-9,232,590	6	
1 to 3 mths	USD	1,943,815	GBP	-1,543,862	8	
1 to 3 mths	AUD	4,515,187	GBP	-2,769,556		-23
1 to 3 mths	EUR	4,941,538	GBP	-4,285,455		-52
1 to 3 mths	EUR	4,654,606	GBP	-4,036,618		-49

**2,671      -1,870**

**Net forward foreign currency contracts at 31 March 2017**

**801**



Settlement	Currency bought	Local Value	Currency sold	Local Value	Asset Value £000	Liability Value £000
0 to 1 mth	USD	6,570,000	BRL	-27,597,285		-842
0 to 1 mth	USD	1,625,000	BRL	-6,082,375		-62
0 to 1 mth	USD	1,625,000	BRL	-6,113,250		-68
0 to 1 mth	USD	1,565,000	BRL	-5,874,228		-63
0 to 1 mth	USD	1,435,000	BRL	-5,419,995		-65
0 to 1 mth	USD	3,410,000	BRL	-12,484,010		-76
0 to 1 mth	USD	800,000	BRL	-2,935,920		-19
0 to 1 mth	USD	800,000	BRL	-2,938,000		-20
0 to 1 mth	USD	1,190,000	BRL	-4,366,705		-29
0 to 1 mth	GBP	11,514,280	CAD	-23,200,000		-965
0 to 1 mth	CAD	19,007,137	USD	-13,480,000	845	
0 to 1 mth	GBP	2,208,084	CHF	-3,200,000		-117
0 to 1 mth	USD	12,960,000	CHF	-13,082,291		-489
0 to 1 mth	USD	6,400,000	CNH	-42,732,800		-151
1 to 3 mths	USD	3,690,000	CNH	-24,261,750		-37
1 to 3 mths	USD	2,460,000	CNH	-16,188,030		-26
1 to 3 mths	USD	2,460,000	CNH	-16,195,410		-27
1 to 3 mths	USD	1,230,000	CNH	-8,086,020		-12
1 to 3 mths	USD	2,460,000	CNH	-16,164,660		-24
1 to 3 mths	USD	6,200,000	CNH	-40,771,200		-63
0 to 1 mth	CZK	2,738,908	EUR	-101,354		-
0 to 1 mth	CZK	3,652,185	EUR	-135,139		-
0 to 1 mth	CZK	19,322,232	EUR	-715,000		-1
0 to 1 mth	CZK	19,454,429	EUR	-720,000		-1
0 to 1 mth	CZK	23,781,208	EUR	-880,000		-1
0 to 1 mth	CZK	34,317,940	EUR	-1,270,000		-1
0 to 1 mth	CZK	37,155,250	EUR	-1,375,000		-1
0 to 1 mth	CZK	14,956,854	EUR	-553,507		-
0 to 1 mth	GBP	35,896,878	EUR	-47,110,000		-1,457
0 to 1 mth	EUR	1,263,686	GBP	-983,375	19	
0 to 1 mth	EUR	718,330	GBP	-558,678	11	
0 to 1 mth	EUR	3,447,984	GBP	-2,678,287	56	
0 to 1 mth	PLN	1,283,346	EUR	-284,341	14	
0 to 1 mth	PLN	10,243,901	EUR	-2,271,318	114	
0 to 1 mth	PLN	1,283,203	EUR	-284,341	14	
0 to 1 mth	EUR	444,157	PLN	-1,995,053		-21
0 to 1 mth	EUR	465,803	PLN	-2,087,475		-21
0 to 1 mth	EUR	310,535	PLN	-1,392,207		-14
0 to 1 mth	EUR	660,000	PLN	-2,952,774		-29
0 to 1 mth	EUR	959,505	PLN	-4,295,190		-42
0 to 1 mth	EUR	405,368	PLN	-1,790,838		-13
0 to 1 mth	EUR	1,621,472	PLN	-7,165,448		-54
0 to 1 mth	EUR	1,690,349	PLN	-7,467,660		-56
0 to 1 mth	EUR	1,782,810	PLN	-7,874,719		-58
0 to 1 mth	USD	7,780,766	EUR	-7,118,116		-231
0 to 1 mth	USD	4,462,079	EUR	-4,081,884		-132
0 to 1 mth	EUR	12,680,000	USD	-13,866,975	406	
0 to 1 mth	EUR	11,539,165	USD	-12,610,000	376	
0 to 1 mth	USD	1,773,157	EUR	-1,614,764		-47
0 to 1 mth	USD	3,545,863	EUR	-3,229,527		-94
0 to 1 mth	USD	829,829	EUR	-755,709		-22
0 to 1 mth	JPY	7,232,000,000	GBP	-42,614,750	2,158	
0 to 1 mth	GBP	123,931,734	USD	-177,890,000	166	
0 to 1 mth	USD	10,500,000	GBP	-7,229,025	76	
0 to 1 mth	GBP	4,192,931	USD	-6,000,000	18	
0 to 1 mth	USD	5,227,126	GBP	-3,654,996		-18
0 to 1 mth	USD	7,019,027	GBP	-4,905,004		-22
0 to 1 mth	GBP	900,000	ZAR	-21,420,270		-113
0 to 1 mth	GBP	4,300,000	ZAR	-102,276,317		-535
0 to 1 mth	ZAR	39,954,031	GBP	-1,785,157	104	

Notes to Pension Fund Accounts

Settlement	Currency bought	Local Value	Currency sold	Local Value	Asset Value £000	Liability Value £000
0 to 1 mth	ZAR	39,353,824	GBP	-1,759,095	101	
0 to 1 mth	ZAR	20,855,035	GBP	-931,404	55	
0 to 1 mth	ZAR	16,097,274	GBP	-724,344	37	
0 to 1 mth	INR	207,552,500	USD	-3,050,000	58	
0 to 1 mth	INR	83,057,600	USD	-1,220,000	24	
0 to 1 mth	INR	83,057,600	USD	-1,220,000	24	
0 to 1 mth	INR	16,053,953	USD	-235,983	4	
0 to 1 mth	INR	21,364,431	USD	-314,017	6	
0 to 1 mth	INR	128,707,431	USD	-1,890,000	37	
0 to 1 mth	INR	41,482,440	USD	-610,000	11	
0 to 1 mth	INR	124,513,200	USD	-1,830,000	35	
0 to 1 mth	INR	41,443,400	USD	-610,000	11	
0 to 1 mth	INR	20,730,850	USD	-305,000	6	
0 to 1 mth	INR	62,172,420	USD	-915,000	17	
0 to 1 mth	USD	55,640,000	JPY	-6,596,711,784		-2,128
0 to 1 mth	USD	6,843,881	JPY	-769,362,681		-1
0 to 1 mth	USD	4,856,119	JPY	-546,064,119		-2
0 to 1 mth	USD	4,090,000	JPY	-462,979,820		-21
0 to 1 mth	USD	8,310,000	JPY	-940,440,190		-41
0 to 1 mth	USD	6,200,000	JPY	-703,700,000		-43
0 to 1 mth	USD	10,035,779	KRW	-12,036,411,784		-357
0 to 1 mth	USD	3,330,000	KRW	-3,981,847,500		-111
0 to 1 mth	USD	1,150,000	KRW	-1,375,630,000		-39
0 to 1 mth	USD	1,150,000	KRW	-1,378,562,500		-41
0 to 1 mth	USD	770,000	KRW	-926,002,000		-29
0 to 1 mth	KRW	5,182,160,000	USD	-4,220,000	224	
0 to 1 mth	KRW	5,173,604,234	USD	-4,215,779	222	
0 to 1 mth	USD	7,800,000	KRW	-9,406,800,000		-309
0 to 1 mth	MXN	122,315,661	USD	-6,570,000	393	
0 to 1 mth	MXN	29,237,608	USD	-1,550,000	108	
0 to 1 mth	MXN	17,550,681	USD	-930,000	65	
0 to 1 mth	MXN	12,820,205	USD	-676,640	50	
0 to 1 mth	MXN	6,401,019	USD	-338,320	24	
0 to 1 mth	MXN	6,412,860	USD	-338,320	25	
0 to 1 mth	MXN	6,024,034	USD	-320,000	22	
0 to 1 mth	MXN	38,566,328	USD	-2,046,719	141	
0 to 1 mth	USD	1,550,000	MXN	-27,764,375		-48
0 to 1 mth	USD	1,550,000	MXN	-27,786,385		-49
0 to 1 mth	USD	166,177	MXN	-2,985,357		-6
0 to 1 mth	USD	2,185,585	MXN	-39,203,448		-70
0 to 1 mth	USD	336,244	MXN	-6,023,506		-10
0 to 1 mth	USD	411,994	MXN	-7,373,570		-13
0 to 1 mth	USD	1,550,000	MYR	-6,491,400		-83
0 to 1 mth	USD	930,000	MYR	-3,908,790		-52
0 to 1 mth	USD	1,240,000	MYR	-5,246,440		-76
0 to 1 mth	USD	310,000	MYR	-1,311,610		-19
0 to 1 mth	USD	310,000	MYR	-1,308,200		-18
0 to 1 mth	USD	1,860,000	MYR	-7,863,150		-113
0 to 1 mth	MYR	10,423,440	USD	-2,480,000	139	
0 to 1 mth	MYR	9,109,660	USD	-2,170,000	120	
0 to 1 mth	MYR	6,513,875	USD	-1,550,000	87	
0 to 1 mth	PHP	627,393,600	USD	-12,960,000	484	
0 to 1 mth	USD	3,293,288	PHP	-153,697,751		-36
0 to 1 mth	USD	3,186,712	PHP	-149,201,856		-42
0 to 1 mth	USD	3,240,000	PHP	-151,729,200		-43
0 to 1 mth	USD	3,240,000	PHP	-151,777,800		-44
0 to 1 mth	USD	2,800,000	SGD	-4,005,120		-121
0 to 1 mth	USD	6,900,000	SGD	-9,879,627		-304
0 to 1 mth	USD	1,500,000	TRY	-4,612,346		-94
0 to 1 mth	USD	1,500,000	TRY	-4,607,025		-93
0 to 1 mth	USD	6,600,000	TRY	-20,239,560		-400
0 to 1 mth	USD	6,200,000	TRY	-17,919,308		-106

Settlement	Currency bought	Local Value	Currency sold	Local Value	Asset Value £000	Liability Value £000
0 to 1 mth	USD	1,680,000	TWD	-56,280,000		-48
0 to 1 mth	USD	13,520,000	TWD	-454,069,200		-413
0 to 1 mth	USD	3,390,000	TWD	-112,209,000		-68
0 to 1 mth	USD	1,345,000	TWD	-44,707,800		-31
0 to 1 mth	USD	1,665,000	TWD	-55,394,550		-39
0 to 1 mth	TWD	179,722,800	USD	-5,400,000	130	
0 to 1 mth	TWD	179,604,000	USD	-5,400,000	127	
0 to 1 mth	USD	3,410,000	TWD	-111,728,650		-44
0 to 1 mth	USD	1,650,000	TWD	-54,095,250		-22
0 to 1 mth	USD	2,090,000	TWD	-68,572,900		-29
0 to 1 mth	USD	3,850,000	TWD	-126,434,000		-55
0 to 1 mth	TWD	350,217,000	USD	-10,900,000		-10
0 to 1 mth	TWD	351,198,000	USD	-10,900,000	11	
1 to 3 mths	USD	10,900,000	TWD	-349,879,100		-
1 to 3 mths	USD	10,900,000	TWD	-351,034,500		-25
1 to 3 mths	AUD	10,869,651	GBP	-5,717,559		-75
1 to 3 mths	EUR	40,824,558	GBP	-32,071,773		-373
1 to 3 mths	USD	91,045,309	GBP	-64,420,370	1,095	
1 to 3 mths	JPY	1,325,912,724	GBP	-8,281,778	55	
1 to 3 mths	MYR	18,690,782	GBP	-3,179,245		-177
1 to 3 mths	AUD	4,408,489	GBP	-2,318,915		-30
1 to 3 mths	USD	572,793	GBP	-405,288	7	
1 to 3 mths	JPY	604,551,839	GBP	-3,776,089	25	
1 to 3 mths	CNY	11,948,588	GBP	-1,287,772	7	
1 to 3 mths	EUR	6,423,145	GBP	-5,046,023		-59
1 to 3 mths	GBP	2,924,865	AUD	-5,478,896	4	
1 to 3 mths	GBP	3,169,203	SEK	-36,991,710		-14
1 to 3 mths	SEK	36,190,874	GBP	-3,084,980	29	
1 to 3 mths	AUD	2,194,000	GBP	-1,167,386	2	
					<b>8,399</b>	<b>-12,613</b>
<b>Net forward foreign currency contracts at 31 March 2016</b>						<b>-4,214</b>

**ii. Futures**

When there is a requirement to hold cash assets, but the Investment Manager does not want this cash to be out of the market, index based futures contracts are bought which have an underlying economic value broadly equivalent to the cash held in anticipation of cash outflow required. Outstanding exchange traded futures contracts, held by BlackRock are as follows:

	Expires	Product Description	Currency	Market Value at 31 March 17	
				£000	£000
<b>Assets</b>					
Overseas equity	1 to 3 mths	S&P500 EMINI JUN 17	EUR	539	
Overseas equity	1 to 3 mths	EURO STOXX 50 JUN 17	USD	46	
<b>Total assets</b>					585
<b>Liabilities</b>					
UK equity	1 to 3 mths	FTSE 100 INDEX JUN 17	GBP	-34	
Overseas equity	1 to 3 mths	EURO STOXX BANK JUN 17	EUR	-58	
Overseas equity	1 to 3 mths	STOXX 600 HEALTH JUN 17	EUR	-63	
<b>Total liabilities</b>					-155
<b>Net Futures Contracts at 31 March 2017</b>					<u>430</u>

	Expires	Product Description	Currency	Market Value at 31 March 16	
				£000	£000
<b>Assets</b>					
Overseas fixed interest	1 to 3 mths	AUST 10YR BOND JUN 16 15/6/2016	AUD	858	
Overseas equity	1 to 3 mths	E-MINI CONSUMER STAPLES JUN 16	USD	170	
Overseas equity	1 to 3 mths	S&P500 EMINI JUN 16	USD	204	
<b>Total assets</b>					1,232
<b>Liabilities</b>					
Overseas equity	1 to 3 mths	E-MINI UTILITIES SELECT SECTOR JUN	USD	-403	
Overseas equity	1 to 3 mths	STOXX 600 INDUS JUN 16	EUR	-742	
Overseas fixed interest	1 to 3 mths	US ULTRA T-BOND JUN 16 21/6/2016	USD	-243	
<b>Total liabilities</b>					-1,388
<b>Net Futures Contracts at 31 March 2016</b>					<u>-156</u>

### iii. Options

In order to benefit from potentially greater returns available from investing in equities whilst minimising the risk of loss of value through adverse equity price movements, the Fund, via Blackrock, has bought a number of equity option contracts. These option contracts are to protect it from falls in value in the main markets in which it is invested.

Type	Expires	Product Description	Currency	Market Value at 31 March 17 £000
<b>Assets</b>				
Overseas equity	1 to 3 mths	S&P 500 INDEX 19/05/2017 P @ 2300.000	USD	419
Overseas fixed interest	Less than 1 year	USD C CNH P @7.000000 EO	USD	188
UK equity	1 to 3 mths	FTSE 100 INDEX 16/06/2017 P @ 6900.000	GBP	179
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 16/06/2017 P @ 3150.000	EUR	168
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 16/06/2017 C @ 3725.000	EUR	98
Overseas equity	Less than 1 year	EURO STOXX 50 INDEX 15/12/2017 C @ 4000.000	EUR	96
Overseas equity	Less than 1 year	S&P 500 INDEX 15/12/2017 P @ 2000.000	USD	87
Overseas fixed interest	Less than 1 year	USD P CNH C @6.600000 EO	USD	17
UK fixed interest	1 to 3 mths	GBP C USD P @1.300000 EO	GBP	8
UK fixed interest	1 to 3 mths	GBP C USD P @1.300000 EO	GBP	4
UK fixed interest	1 to 3 mths	GBP C USD P @1.300000 EO	GBP	4
<b>Total assets</b>				<b>1,268</b>
<b>Liabilities</b>				
Overseas fixed interest	Less than 1 year	USD P CNH C @6.600000 EO	USD	-17
Overseas equity	Less than 1 year	S&P 500 INDEX 15/12/2017 P @ 1875.000	USD	-55
Overseas equity	1 to 3 mths	EURO STOXX BANKS 16/06/2017 C @ 140.000	EUR	-81
UK equity	1 to 3 mths	FTSE 100 INDEX 16/06/2017 P @ 6600.000	GBP	-82
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 16/06/2017 P @ 3000.000	EUR	-87
Overseas fixed interest	Less than 1 year	USD C CNH P @7.000000 EO	USD	-188
UK equity	1 to 3 mths	FTSE 100 INDEX 16/06/2017 C @ 7300.000	GBP	-454
<b>Total liabilities</b>				<b>-964</b>
<b>Net Options at 31 March 2017</b>				<b>304</b>

Type	Expires	Product Description	Currency	Market Value at 31 March 16 £000
<b>Assets</b>				
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 01-JAN-2050 17/6/2016 C @ 2925.000	EUR	930
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 01-JAN-2050 17/6/2016 P @ 2925.000	EUR	518
Overseas equity	1 to 5 years	S&P 500 INDEX 15/12/2017 P @ 2000.000	USD	491
Overseas equity	1 to 3 mths	S&P 500 INDEX 17/6/2016 C @ 2075.000	USD	450
Overseas equity	1 to 3 mths	MSCI EMERGING MARKETS INDEX 23/5/2016 C @ 875.000	USD	351
UK equity	1 to 3 mths	FTSE 100 INDEX 20/5/2016 P @ 6000.000	GBP	204
Overseas equity	1 to 3 mths	SPX VOLATILITY INDEX UX 01-JAN-2050 18/5/2016 C @ 23.000	USD	183
Overseas equity	1 to 5 years	EURO STOXX 50 INDEX 01-JAN-2050 15/12/2017 C @ 4000.000	EUR	90
Overseas fixed interest	0 to 1 mth	APR16 EDM7 P @ 98.75	USD	13
Overseas fixed interest	1 to 3 mths	USD C SGD P @1.420000 EO	USD	9
Overseas fixed interest	3 to 6 months	EUR P CZK C @25.75000 EO	EUR	8
Overseas fixed interest	3 to 6 months	EUR P CZK C @25.75000 EO	EUR	2
<b>Total assets</b>				<b>3,249</b>
<b>Liabilities</b>				
Overseas fixed interest	1 to 3 mths	USD C SGD P @1.450000 EO	USD	-1
Overseas equity	0 to 1 mth	EURO STOXX 50 INDEX 01-JAN-2050 15/4/2016 C @ 3100.000	EUR	-35
UK equity	1 to 3 mths	FTSE 100 INDEX 20/5/2016 P @ 5750.000	GBP	-60
Overseas equity	1 to 3 mths	MSCI EMERGING MARKETS INDEX 23/5/2016 C @ 925.000	USD	-111
Overseas equity	1 to 3 mths	EURO STOXX UTILITIES (PRICE) INDEX 17/6/2016 P @ 235.000	EUR	-143
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 01-JAN-2050 17/6/2016 C @ 3200.000	EUR	-153
Overseas equity	1 to 3 mths	SPX VOLATILITY INDEX UX 01-JAN-2050 18/5/2016 C @ 30.000	USD	-155
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 01-JAN-2050 17/6/2016 P @ 2975.000	EUR	-207
Overseas equity	1 to 3 mths	EURO STOXX 50 INDEX 01-JAN-2050 17/6/2016 P @ 2800.000	EUR	-325
Overseas equity	1 to 5 years	S&P 500 INDEX 15/12/2017 P @ 1875.000	USD	-372
Overseas equity	1 to 3 mths	S&P 500 INDEX 17/6/2016 C @ 1875.000	USD	-2,222
<b>Total liabilities</b>				<b>-3,784</b>
<b>Net Options at 31 March 2016</b>				<b>-535</b>

## Investments Exceeding 5% of the Market Value of the Fund

The investments in the following table individually represented more than 5% of the Pension Fund's total net assets available for benefits at 31 March:

Name of Fund	Investment Manager	At 31 March 2017		At 31 March 2016	
		£m	%	£m	%
BNYM Long Term Global Equity	BNY Mellon	444.82	16.52	364.84	15.72
AAM L and P World Equity	Aberdeen	440.07	16.34	339.12	14.61
Diversified Yield Plus	AB	357.97	13.30	341.87	14.73

Single investments with a market value exceeding 5% of their type of asset as at 31 March are listed as follows:

### At 31 March 2017

Holding	Investment Manager	£000	%
<b>Bonds</b>			
UK Treasury 0.75% IL Gilt 22/11/47	Royal London	50,729	8.74
UK Treasury 2% IL 26/01/2035	Royal London	35,718	6.15
UK Treasury 1.25% IL Gilt 22/11/2055	Royal London	35,048	6.04
UK Treasury 0.125% IL 22/03/2068	Royal London	34,946	6.02
UK Treasury 0.375% IL 22/03/2062	Royal London	29,470	5.07
UK Treasury Gilt 0.125% IL 22/11/2036	Royal London	29,201	5.03

### Pooled Investment Vehicles

BNYM Long Term Global Equity	BNY Mellon	444,824	25.01
AAM L and P World Equity	Aberdeen	440,069	24.74
Diversified Yield Plus	AB	357,972	20.13
ICS INS GBP LIQ AGENCY DIS	BlackRock	110,616	6.22
BGF GLOBAL CORP BND X4RF GBP HDG	BlackRock	96,251	5.41

### At 31 March 2016

Holding	Investment Manager	£000	%
<b>Bonds</b>			
UK Treasury 0.625% IL 22/11/2042	Royal London	37,989	7.32
UK Treasury 1.25% IL 22/11/2032	Royal London	35,829	6.90
UK Treasury 0.5% IL Gilt 22/03/2050	Royal London	35,727	6.88
UK Treasury 2.5% IL 17/07/24	Royal London	32,874	6.33
UK Treasury 0.625% IL 22/03/2040	Royal London	30,223	5.82

### Equities

ISHARES GOLD TRUST	BlackRock	17,363	8.20
--------------------	-----------	--------	------

### Pooled Investment Vehicles

BNYM Long Term Global Equity	BNYM	364,837	24.53
Diversified Yield Plus	AB	341,874	22.98
AAM L and P World Equity	Aberdeen	339,124	22.80
BGF GLOBAL CORP BND X4RF GBP HDG	BlackRock	108,805	7.31
ICS INS GBP LIQ AGENCY DIS	BlackRock	77,739	5.23

## 15. Financial Instruments

### Classification of Financial Instruments

Accounting policies describe how different asset classes of financial instruments are measured and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the carrying amounts of financial assets and liabilities by category and Net Assets Statement heading:

2015-16 (Restated)			2016-17		
Fair value through profit and loss	Loans and receivables	Financial liabilities at amortised cost	Fair value through profit and loss	Loans and receivables	Financial liabilities at amortised cost
£000	£000	£000	£000	£000	£000
<b>Financial assets</b>					
211,866			282,942		
519,293			580,729		
1,487,500			1,778,540		
12,880			4,524		
	349			327	
	79,484			31,491	
	17,217			8,431	
	15,681			5,476	
	10,581			11,432	
2,231,539	123,312	-	2,646,735	57,157	-
<b>Financial liabilities</b>					
-17,785			-2,989		
		-15,849			-8,448
-17,785	-	-15,849	-2,989	-	-8,448
<b>2,213,754</b>	<b>123,312</b>	<b>-15,849</b>	<b>2,643,746</b>	<b>57,157</b>	<b>-8,448</b>
	<b>2,321,217</b>			<b>2,692,455</b>	
		<b>Net Assets at 31 March</b>			

The 2015-16 figures have been restated to re-categorise Other investment Assets as Loans and Receivables and Creditors as Financial Liabilities at Amortised Cost in accordance with the FRS39. The Net Assets total remains unchanged.

### Net gains and losses on financial instruments

31 March 2016 £000 (Restated)		31 March 2017 £000
<b>Financial Assets</b>		
-26,662	Fair Value through profit and loss	368,422
1,707	Loans and receivables	-1,699
<b>Financial Liabilities</b>		
-	Fair Value through profit and loss	-
-	Loans and receivables	-
-	Financial liabilities measured at amortised cost	-
<b>-24,955</b>	<b>Total</b>	<b>366,723</b>



The 31 March 2016 figures have been restated to reflect the restatement to the Reconciliation of Movements in Investments 2015/16 table. The total remains unchanged.

### **Valuation of financial instruments carried at fair value**

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

#### **LEVEL 1**

Financial instruments 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, exchange traded derivatives and unit trusts. Listed investments are shown at bid prices. The bid value of the investment is based on the bid market quotation of the relevant stock exchange.

#### **LEVEL 2**

Financial instruments 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 and where these techniques use inputs that are based significantly on observable market data.

#### **LEVEL 3**

Financial instruments 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. Such instruments would include unquoted property funds, unquoted equity investments and hedge fund of funds, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions. The values of the investment in private equity are based upon valuations provided by the general partners to the private equity in which the Fund has invested. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which follow the valuation principles of IFRS and US GAAP. Valuations are usually undertaken annually.

The following tables provide analyses of the financial assets and liabilities of the Fund as at 31 March 2017 and 31 March 2016, grouped into Levels 1, 2 and 3, based on the level at which the fair value is observable.

	Quoted market price	Using observable inputs	With significant unobservable inputs	
Values at 31 March 2017	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
<b>Financial Assets</b>				
Financial Assets at fair value through profit and loss	2,478,392	2,893	165,450	2,646,735
Loans and receivables	57,157	-	-	57,157
<b>Total Financial Assets</b>	<b>2,535,549</b>	<b>2,893</b>	<b>165,450</b>	<b>2,703,892</b>
<b>Financial Liabilities</b>				
Financial Liabilities at fair value through profit and loss	-913	-2,076	-	-2,989
Financial Liabilities at amortised cost	-8,448	-	-	-8,448
<b>Total Financial Liabilities</b>	<b>-9,361</b>	<b>2,076</b>	<b>-</b>	<b>-11,437</b>
<b>Net Financial Assets</b>	<b>2,526,188</b>	<b>817</b>	<b>165,450</b>	<b>2,692,455</b>
	Quoted market price	Using observable inputs	With significant unobservable inputs	
Values at 31 March 2016 (Restated)	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
<b>Financial Assets</b>				
Financial Assets at fair value through profit and loss	2,068,983	8,446	154,110	2,231,539
Loans and receivables	123,312	-	-	123,312
<b>Total Financial Assets</b>	<b>2,192,295</b>	<b>8,446</b>	<b>154,110</b>	<b>2,354,851</b>
<b>Financial Liabilities</b>				
Financial Liabilities at fair value through profit and loss	-5,171	12,614	-	-17,785
Financial Liabilities at amortised cost	-15,849	-	-	-15,849
<b>Total Financial Liabilities</b>	<b>-21,020</b>	<b>12,614</b>	<b>-</b>	<b>-33,634</b>
<b>Net Financial Assets</b>	<b>2,171,275</b>	<b>-4,168</b>	<b>154,110</b>	<b>2,321,217</b>

The values at 31 March 2016 table has been restated to show :-

The reclassification of the AB Diversified Yield Fund valued at £341.87m from Level 2 to Level 1

The reclassification of BlackRock Futures assets and Exchange Traded Options assets valued at £4.46m from Level 2 to Level 1

The reclassification of Financial Assets valued at £15.68m from Financial Assets at fair value through profit and loss to Loans and Receivables

The reclassification of BlackRock Futures liabilities and Exchange Traded Options liabilities valued at £5.17m from Level 2 to Level 1

The reclassification of Financial Liabilities valued at £9.73m from Financial Liabilities at fair value through profit and loss to Financial Liabilities at amortised cost.

The total remains unchanged.

## 16. Nature and Extent of Risk Arising From Financial Instruments

### Risk and risk management

The Pension Fund's activities expose it to a variety of financial risks. The key risks are:

- i. **MARKET RISK** - the possibility that financial loss may arise for the Fund as a result of changes in, for example, interest rates movements;
- ii. **CREDIT RISK** - the possibility that other parties may fail to pay amounts due to the Fund;
- iii. **LIQUIDITY RISK** - the possibility that the Fund might not have funds available to meet its commitments to make payments.

The Fund's primary long-term risk is that its assets will fall short of its liabilities (i.e. promised benefits payable to members). The aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and maximise the opportunity for gains across the whole fund portfolio. This is achieved through asset diversification to reduce exposure to market risk (price risk, currency risk and interest rate risk) 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. The administering body manages these investment risks as part of its overall Pension Fund risk management programme.

The Fund's assets are managed by a number of Investment Managers, as disclosed in Note 14. By dividing the management of the assets between a number of managers risk is further controlled. Asset allocation benchmarks have been set and performance is monitored relative to the benchmarks. This is to ensure the Investment Manager does not deviate from the Pension Fund Committee's investment strategy.

The Fund has appointed a Global Custodian that performs a range of services including collection of dividends and interest from the Investment Managers, administering corporate actions that the Pension Fund may join, dealing with taxation issues and proxy voting when requested. It also ensures that the settlement of purchases and sales of the Fund assets are completed. The Custodian has stringent risk management processes and controls. Client accounts are strictly segregated to ensure that the Fund assets are separately identifiable. Conservative investment practices are ensured by the Custodian where they invest cash collateral.

The Fund also employs a specialised service as an independent check to ensure that all dividends receivable are compared against those collected by the Custodian and that they were received on the due date; any discrepancies are investigated. In line with its Treasury Management Policy, Durham County Council as administering authority, invests the short term cash balances on behalf of the Pension Fund. Interest is paid over to the Fund on a quarterly basis.

Durham County Council's overall risk management procedures focus on the unpredictability of financial markets and are structured to implement suitable controls to

minimise these risks. The procedures for risk management are set out through a legal framework based on the Local Government Act 2003 and associated regulations. These require the Council to comply with the CIPFA Prudential Code, the CIPFA Code of Practice on Treasury Management in the Public Services and investment guidance issued through the Act.

#### **i. MARKET RISK**

Market risk is the risk of loss from fluctuations in market prices, interest and foreign exchange rates. The Fund is exposed to market risk from its investment activities, particularly through its equity holdings. The level of risk exposure depends on market conditions, expectations of future price and yield movements and the asset mix. The objective of the Fund's risk management strategy is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on risk.

In general, excessive volatility in market risk is managed through the diversification of the portfolio in terms of geographical and industry sectors and individual securities. To mitigate market risk, the Fund and its investment advisers undertake appropriate monitoring of market conditions. Risk exposure is limited by applying maximum exposure restrictions on individual investments to each Investment Manager's portfolio.

#### **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 instrument 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. The maximum risk resulting from financial instruments is determined by the fair value of the financial instruments.

The Fund's Investment Managers mitigate this price risk through diversification and the selection of securities and other financial instruments is monitored by the Fund to ensure it is within limits specified in the Fund Investment Strategy.

#### **Other Price Risk – Sensitivity Analysis**

In consultation with the Fund's investment advisers, an analysis of historical volatility and implied market volatility has been completed. From this, it has been determined that the potential market movements in market price risk, as shown in the following table, are reasonably possible for the 2016/17 reporting period. The analysis assumed that all other variables remain the same.

If the market price of the Fund investments were to increase/ decrease in line with these potential market movements, the value of assets available to pay benefits would vary as illustrated in the following table (the prior year comparator is also provided):

Manager	Asset type	Asset value	Potential	Value on	Value on
		at 31 March 2017 £000	market movements %	increase £000	decrease £000
Aberdeen	Global equity	440,069	18.7%	522,362	357,776
AB	Broad Bonds	357,972	8.0%	386,610	329,334
BNYM	Global equity	444,824	18.7%	528,006	361,642
BlackRock	DAA	480,622	9.4%	525,800	435,444
CBRE	Unlisted property	165,450	14.5%	189,440	141,460
CBRE	Listed property	34,375	21.7%	41,834	26,916
Mondrian	Emerging market equity	195,330	29.0%	251,976	138,684
RLAM	UK Index Linked Gilts	523,569	8.8%	569,643	477,495
	Loans	327	0.0%	327	327
	Cash	39,922	0.0%	39,922	39,922
	Net derivative assets	1,535	0.0%	1,535	1,535
	Net investment balances	3,495	0.0%	3,495	3,495
<b>Total change in net investment assets available</b>		<b>2,687,490</b>		<b>3,060,950</b>	<b>2,314,030</b>

Manager	Asset type	Asset value	Potential	Value on	Value on
		at 31 March 2016 £000	market movements %	increase £000	decrease £000
Aberdeen	Global equity	339,124	18.8%	402,879	275,369
AB	Broad Bonds	341,874	8.0%	369,224	314,524
BNYM	Global equity	364,837	18.8%	433,426	296,248
BlackRock	DAA	371,476	8.6%	403,423	339,529
CBRE	Unlisted property	154,110	14.1%	175,840	132,380
CBRE	Listed property	31,619	20.0%	37,943	25,295
Mondrian	Emerging market equity	147,296	29.9%	191,338	103,254
RLAM	UK Index Linked Gilts	468,295	8.8%	509,505	427,085
Other	UK Equity	28	17.1%	33	23
	Loans	349	0.0%	349	349
	Cash	96,701	0.0%	96,701	96,701
	Net derivative assets	-4,905	0.0%	-4,905	-4,905
	Net investment balances	5,947	0.0%	5,947	5,947
<b>Total change in net investment assets available</b>		<b>2,316,751</b>		<b>2,621,703</b>	<b>2,011,799</b>

## Interest Rate Risk

The Fund invests in financial assets for the primary purpose of obtaining a return on investments. These investments are subject to interest rate risks, which represent the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Fund's interest rate risk is routinely monitored by the administering authority (as part of its Treasury Management Service for investment of surplus cash), its managers,

custodian and investment advisers in accordance with the Fund's risk management strategy. This includes monitoring the exposure to interest rates and assessment of actual interest rates against the relevant benchmarks. During periods of falling interest rates and where economic circumstances make it favourable, fixed rate investments may be taken for longer periods to secure better long term returns.

### Interest Rate Risk - Sensitivity Analysis

The Fund recognises that interest rates can vary and can affect income to the fund and the value of the net assets available to pay benefits. The following table shows the fund's asset values having direct exposure to interest rate movements as at 31 March 2017 and the effect of a +/- 25 BPS change in interest rates on the net assets available to pay benefits (assuming that all other variables, in particular exchange rates, remain constant). The prior year comparator is also provided:

Asset type	Asset Values at 31 March 2017	Change in year in the net assets available to pay benefits	
		+25 BPS	-25 BPS
	£000	£000	£000
Cash and cash equivalents	39,922	100	-100
Fixed interest securities	57,283	143	-143
<b>Total change in net investment assets available</b>	<b>97,205</b>	<b>243</b>	<b>-243</b>

Asset type	Asset Values at 31 March 2016	Change in year in the net assets available to pay benefits	
		+25 BPS	-25 BPS
	£000	£000	£000
Cash and cash equivalents	96,701	242	-242
Fixed interest securities	50,997	127	-127
<b>Total change in net investment assets available</b>	<b>147,698</b>	<b>369</b>	<b>-369</b>

### Currency Risk

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than GBP (the functional currency of the Fund). The Fund's currency rate risk is routinely monitored by the Fund and its investment advisers in accordance with the fund's risk management strategy, including monitoring the range of exposure to currency fluctuations.

## Currency Risk - Sensitivity Analysis

Having consulted with the Fund's independent investment advisers, the likely fluctuation associated with foreign exchange rate movements is expected to be 10% for developed market currencies and 15% in emerging market currencies. This is based upon the adviser's analysis of long-term historical movements in the month end exchange rates of a broad basket of currencies against the pound. This analysis assumes that all other variables, in particular interest rates, remain constant.

The following table exemplifies, by Investment Manager, to what extent a 10% (or 15% for emerging markets) strengthening/ weakening of the pound, against the various currencies in which the fund holds investments, would increase/ decrease the net assets available to pay benefits (the prior year comparator is also provided):

Manager	Currency exposure by asset type	Level of unhedged exposure	Total Volatility	Asset value at	Value on	Value on
				31 March 17	increase	decrease
				£000	£000	£000
Aberdeen	Global Equity	86%	15%	440,069	496,838	383,300
AB	Broad Bonds	0%	0%	357,972	357,972	357,972
BlackRock	DAA	5%	10%	480,622	483,025	478,219
BNYM	Global Equity	95%	15%	444,824	508,211	381,437
CBRE	Global Property	16%	10%	199,825	203,022	196,628
Mondrian	Emerging market equity	99%	15%	195,330	224,337	166,323
RLAM	UK Index Linked Gilts	0%	0%	523,569	523,569	523,569
	Loans	0%	0%	327	327	327
	Cash	12%	10%	39,922	40,401	39,443
	Net derivative assets	0%	0%	1,535	1,535	1,535
	Net investment balances	0%	0%	3,495	3,495	3,495
<b>Total change in net investment assets available</b>				<b>2,687,490</b>	<b>2,842,732</b>	<b>2,532,248</b>

Manager	Currency exposure by asset type	Level of unhedged exposure	Total Volatility	Asset value at	Value on	Value on
				31 March 16	increase (restated)	decrease (restated)
				£000	£000	£000
Aberdeen	Global Equity	87%	15%	339,124	383,380	294,868
AB	Broad Bonds	0%	0%	341,874	341,874	341,874
BlackRock	DAA	5%	10%	364,837	366,661	363,013
BNYM	Global Equity	96%	15%	371,476	424,969	317,983
CBRE	Global Property	16%	10%	185,729	188,701	182,757
Mondrian	Emerging market equity	96%	15%	147,296	168,507	126,085
RLAM	UK Index Linked Gilts	0%	0%	468,295	468,295	468,295
Other	UK Equity	0%	0%	28	28	28
	Loans	0%	0%	349	349	349
	Cash	20%	10%	96,701	98,635	94,767
	Net derivative assets	0%	0%	-4,905	-4,905	-4,905
	Net investment balances	0%	0%	5,947	5,947	5,947
<b>Total change in net investment assets available</b>				<b>2,316,751</b>	<b>2,442,441</b>	<b>2,191,061</b>

The 31 March 2016 Table has been restated to show the actual level of unhedged exposure to currency fluctuations.

**ii. 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 Fund's entire investment portfolio is exposed to some form of credit risk with the exception of the derivatives positions, where the risk equates to the net market value of a positive derivative position. The Fund minimises credit risk by undertaking transactions with a large number of high quality counterparties, brokers and institutions.

Investment Managers adopt procedures to reduce credit risk related to its dealings with counterparties on behalf of its clients. Before transacting with any counterparty, the Investment Manager evaluates both credit worthiness and reputation by conducting a credit analysis of the party, their business and reputation. The credit risk of approved counterparties is then monitored on an ongoing basis, including periodic reviews of financial statements and interim financial reports as required.

The Fund has sole responsibility for the initial and ongoing appointment of custodians. Uninvested cash held with the Custodian is a direct exposure to the balance sheet of the Custodian. Arrangements for investments held by the Custodian vary from market to market but the assets of the Fund are held in a segregated client account. As at 31 March 2017, this level of exposure to the Custodian is only 1.2% of the total value of the portfolio (3.5% as at 31 March 2016).

Surplus cash is invested by Durham County Council only with financial institutions which meet identified minimum credit criteria, in accordance with the Fitch, Moody's and Standard & Poors' Credit Ratings Services. The Council's Investment Strategy sets out the maximum amounts and time limits in respect of deposits placed with each financial institution; deposits are not made unless they meet the minimum requirements of the investment criteria.

The Fund believes it has managed its exposure to credit risk. No credit limits were exceeded during the reporting period and the Fund does not expect any losses from non-performance by any of its counterparties in relation to deposits.

The cash holding under its treasury management arrangements was £8.431m as at 31 March 2017 (£17.217m at 31 March 2016). This was held with the following institutions:



	Rating as at 31 March 2017	Balances £000	Rating as at 31 March 2016	Balances £000
<b>Bank Deposit Accounts</b>				
Handelsbanken	F1+	259	F1+	62
Barclays		-	F1	1,209
Santander UK Plc	F1	458	F1	94
<b>Fixed Term Deposits</b>				
Leeds Building Society	F1	687		-
Royal Bank of Scotland		-	F1	1,612
Barclays		-	F1	1,612
Bank of Scotland	F1	1,603	F1	4,836
Nationwide Building Society	F1	458	F1	2,014
Goldman Sachs	F1	1,145	F1	2,820
UK Local Authorities	N/A	2,861	N/A	898
<b>Income Bond</b>				
National Savings & Investments	N/A	46	N/A	81
Other				
Money Market Funds	N/A	914	N/A	1,979
<b>Total</b>		<b>8,431</b>		<b>17,217</b>

### iii. LIQUIDITY RISK

Liquidity risk represents the risk that the Fund will not be able to meet its financial obligations as they fall due. Steps are taken to ensure that the Fund has adequate cash resources to meet its commitments. Management prepares quarterly cash flow forecasts to understand and manage the timing of the Fund's cash flows. The appropriate strategic level of cash balances to be held forms part of the Fund Investment Strategy and rebalancing policy.

The vast majority of the Fund's investments are readily marketable and may be easily realised if required. Some investments may be less easy to realise in a timely manner but the total value of these types of investments is not considered to have any adverse consequences for the Fund.

Durham County Council invests the cash balances of the Fund in line with its Treasury Management Policy and as agreed by the Pension Fund Committee. The Council manages its liquidity position to ensure that cash is available when needed, through the risk management procedures set out in the prudential indicators and treasury and investment strategy reports, and through a comprehensive cash flow management system. Regulation 5 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, gives Durham County Council a limited power to borrow on behalf of the Pension Fund for up to 90 days. The Council has ready access to borrowings from the money markets to cover any day to day cash flow need. This facility is only used to meet timing differences on pension payments and as they are of a short-term nature, exposure to credit risk is considered negligible.

## 17. Analysis of Debtors

2015-16 £000		2016-17 £000
1,292	Central government bodies	1,073
6,930	Other local authorities	8,347
18,040	Other entities and individuals	7,488
<u>26,262</u>	<b>Total debtors</b>	<u>16,908</u>
	<b>Included in the Net Assets Statement as:</b>	
833	Long Term Assets	625
15,681	Other Investment Assets	5,476
9,748	Current Assets	10,807
<u>26,262</u>		<u>16,908</u>

The long term assets relate to the portion of the transfer value in from the Ministry of Justice for Magistrates' Courts staff which are repayable more than 12 months after the year end.

## 18. Analysis of Creditors

2015-16 £000		2016-17 £000
-815	Central government bodies	-828
-1,388	Other local authorities	-1,417
-13,646	Other entities and individuals	-6,203
<u>-15,849</u>	<b>Total creditors</b>	<u>-8,448</u>
	<b>Included in the Net Assets Statement as:</b>	
-9,734	Investment Liabilities - Other balances	-1,981
-6,115	Current Liabilities	-6,467
<u>-15,849</u>		<u>-8,448</u>

All of the £8.448m is expected to be paid by the Pension Fund within 12 months after the year end.

## 19. Additional Voluntary Contributions (AVCs)

AVCs are paid to the AVC provider by employers and are specifically for providing additional benefits for individual contributors. The Pension Fund offers two types of AVC arrangement:

- Purchase of additional pension, which is invested as an integral part of the Fund's assets;
- Money purchase scheme, managed separately by Equitable Life, Standard Life and Prudential. AVCs may be invested in a range of different funds.

The following table refers only to the money purchase AVCs:

	Value at 31 March 2016 £000	* Purchases £000	Sales £000	Change in Market Value £000	Value at 31 March 2017 £000
Equitable Life	2,103	76	263	173	2,089
Prudential	4,609	1,165	1,015	350	5,109
Standard Life	1,766	298	512	224	1,776
<b>Total</b>	<b>8,478</b>	<b>1,539</b>	<b>1,790</b>	<b>747</b>	<b>8,974</b>

\* Purchases represent the amounts paid to AVC providers in 2016/17

The financial information relating to money purchase AVCs, as set out above, is not included in the Fund's Net Asset Statement or Fund Account in accordance with Regulation 4 (1) (b) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

## 20. Related Party Transactions

Related parties are bodies or individuals that have the potential to control or influence the Pension Fund or to be controlled or influenced by the Pension Fund. Influence in this context is expressed in terms of a party:

- being potentially inhibited from pursuing at all times its own separate interests by virtue of the influence over its financial and operating policies; or
- actually subordinating its separate interests in relation to a particular transaction.

Related parties of the Pension Fund fall into three categories:

- a) Employer related
- b) Member related
- c) Key management personnel

### a) EMPLOYER RELATED

There is a close relationship between an employer and the Pension Fund set up for its employees and therefore each participating employer is considered a related party. The following table details the nature of related party relationships.

Transaction	Description of the Financial Effect	Amount	
		2015/16	2016/17
Contributions receivable	Amounts receivable from employers in respect of contributions to the Pension Fund	£112.035m	£106.715m
Debtors	Amounts due in respect of employers and employee contributions	£8.146m	£8.674m
Creditors	Amounts due to the Administering Authority in respect of administration and investment management expenses	£1.388m	£1.417m
Administration & Investment Management Expenses	The administration, and a small proportion of the investment management, of the Pension Fund is undertaken by officers of the County Council. The Council incurred the following costs, including staff time, which have been subsequently reimbursed by the Fund	£1.388m	£1.417m
Long term loans	The Pension Fund made loans to Durham County Council prior to January 1974 which earn interest of between 5.75% and 9.875% pa of the outstanding balance, in addition to capital repayments	Loans outstanding £0.239m	Loans outstanding £0.233m
Investment Income	Part of the Pension Fund's cash holding is invested in money markets by Durham County Council. The average surplus cash balance during the year and interest earned were:	Balance = £51.289m Interest = £0.233m	Balance = £21.368m Interest = £0.069m

## b) MEMBER RELATED

Member related parties include:

- Members and their close families or households;
- companies and businesses controlled by the Members and their close families which have a financial contractual relationship with any of the organisations that contract with the Pension Fund.

Durham County Council and Darlington Borough Council have a number of Members who are on the Pension Fund Committee. These Members are subjected to a declaration of interest circulation on an annual basis. Each Member of the Pension Fund Committee is also required to declare their interests at the start of each meeting. There were no material related party transactions between any Members or their families and the Pension Fund.

As at 31 March 2017 there were four Members of the Pension Fund Committee in receipt of pension benefits from Durham County Council Pension Fund; a further three Members were active members of the Pension Fund.

Under the LGPS (Transitional Provisions, Savings and Amendment) Regulations 2014, elected Members are no longer allowed to be active members of the Pension Fund with effect from the fourth day after the end of their term in office, in this case 8 May 2017.

---

**c) KEY MANAGEMENT PERSONNEL**

Related parties in this category include:

- key management i.e. senior officers and their close families;
- companies and businesses controlled by the key management of the Pension Fund or their close families.

There were no material related party transactions between any officers or their families and the Pension Fund.

The key management personnel of the Fund are the Members of the Pension Fund Committee and the Corporate Director Resources.

Disclosure requirements for officer remuneration and members allowances can be found in the main accounts of Durham County Council.

**21. Contingent Assets****a) PENSION CONTRIBUTIONS ON EQUAL PAY PAYMENTS**

Originally equal pay settlements were not deemed to be pensionable however, an element of choice has since been introduced. Individuals can choose to have their settlements considered to be pensionable. This provision has now been added to the agreements that individuals with pending equal pay settlements sign.

There is no certainty that an individual will pay pension contributions on their Equal Pay settlement. The agreements signed by individuals are 'open-ended' in that an individual's ability to determine their settlement as 'pensionable' is not time limited, so the timing of any liability to pay contributions are not certain. The level of contributions likely to be received by the Pension Fund, are unlikely to have a material effect on the Pension Fund Accounts.

**b) FOREIGN INCOME DIVIDENDS (FIDs)**

The Pension Fund is involved in claims for tax reclaims due to EC Legislation. The outcome of the Court cases will determine the reclaim of taxes, neither the amount of income nor the timing of the income is certain.

Up until 1 July 1997 UK Pension Funds were entitled, under UK tax law, to reclaim tax credits attaching to dividends received from UK resident companies. However, Pension Funds which received dividends designated by UK companies as FIDs, or dividends received from overseas companies, were not entitled to a refundable tax credit. Since UK sourced dividends came with a 20 percent tax credit, the net investment income return from UK companies paying such dividends was significantly higher than UK companies

paying FIDs or dividends from overseas companies, for which no credit was available. As a result there was a disincentive for Pension Funds to invest in such companies.

The UK tax law which gave rise to these consequences was arguably contrary to EU law, notably Article 56EC, in that it treated UK Pension Funds investing directly into overseas companies, or UK companies paying FIDs, less favourably than UK companies paying ordinary dividends.

The legal arguments to support the strongest element of the FID and Manninen type claims (for EU sourced dividends and FIDs) are considered to be very good. The points in issue are currently being considered at the High Court via a Group Litigation Order containing over 65 UK Pension Funds, including Durham County Council Pension Fund.

### **c) WITHHOLDING TAX (WHT) CLAIMS**

Pension funds, investment funds and other tax exempt bodies across Europe have in recent years been pursuing claims against a number of EU Member States for the recovery of withholding taxes suffered on EU sourced dividend income. These claims were made in the light of the Fokus Bank (Case E-1/04) ruling in December 2004 on the grounds that the WHT rules of those Member States are in breach of the free movement of capital principle of the EC Treaty. The legal arguments used to support Fokus claims are strong and rely on existing case law. The EU Commission announced that it is taking action against a number of member states which operate discriminatory rules regarding the taxation of outbound dividends.

A test case in the Netherlands on behalf of a number of UK pension funds was successful and in January 2009 notification from the Dutch Tax Authorities was received that the claims brought by the test claimant for the recovery of withholding taxes going back to 2003 had been accepted and would be repaid in the near future. Following the ruling in the Netherlands which essentially states that the Dutch tax authorities should not have levied a "withholding tax" (WHT) on dividend payments to tax exempt bodies (such as UK pension funds) located within the European Union but outside the Netherlands, a similar process for reclaiming WHT in other EU Member States is now on-going.

As a result of a precedent for the change in WHT has been set by the Netherlands, other Member States have now reduced the level of WHT of non-residents; recovery is therefore probable, but the timing and amount of income is uncertain.

## **22. Funding Arrangements**

In line with Regulation 62 of the Local Government Pension Scheme Regulations 2013 the Fund's independent qualified actuary undertakes a funding valuation every 3 years for the purpose of setting employer contribution rates for the forthcoming triennial period. The last full valuation took place as at 31 March 2016.

The key elements of the funding policy are 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;
- ensure that employer contribution rates are as stable as possible;

- 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;
- reflect the different characteristics of employing bodies in determining contribution rates where the administering authority considers it reasonable to do so;
- use reasonable measures to reduce the risk to other employers and ultimately the taxpayer from an employer defaulting on its pension obligations.

At the 31 March 2016 actuarial valuation the Fund was assessed as being 81% funded (84% at 31 March 2013). This corresponded to a deficit of £529.3m (£379.2m at 31 March 2013).

The aim is to achieve 100% solvency over a period of 21 years and to provide stability in employer contribution rates by spreading any increases in rates over a period of time.

The aggregate employer future service contribution rate (the primary contribution rate, a weighted average of all employers' primary rates) as 16.7% of pensionable pay.

The aggregate employer total contribution rate (primary plus secondary) required to restore the funding ratio to 100%, using a recovery period of 21 years from 1 April 2017, is 24.6% of pensionable pay (assuming the membership remains broadly stable and pay increases are in line with assumptions).

Across the Fund as a whole, the contributions required to remove the shortfall using a recovery period of 21 years from 1 April 2017 would be £28.6m per annum, increasing at 3.5% per annum. This is equivalent to approximately 7.9% per annum of pensionable pay (assuming the membership remains broadly stable and pay increases are in line with assumptions).

The key assumptions used by the actuary to calculate the past service liabilities and the cost of future benefit accrual are set out in the following table:

	Valuation as at 31 March 2016	Valuation as at 31 March 2013
<b>Financial Assumptions</b>		
Discount rate for periods in service	4.5% pa	5.4% pa
Discount rate for periods after leaving service	4.5% pa	5.4% pa
Rate of revaluation of pension accounts	2.0% pa	2.4% pa
Rate of pension increases on:		
- non Guaranteed Minimum Pensions	2.0% pa	2.4% pa
- post 1988 Guaranteed Minimum Pensions	1.8% pa	2.0% pa
Pensionable pay increase	3.5% pa	3.9% pa
<b>Demographic Assumptions</b>		
Post-retirement mortality assumption (normal health) - base table	Standard SAPS S2P tables with scaling factors of 95% for men and 100% for women	SAPS normal tables with scaling factors of 105% for men and women
Post-retirement mortality assumption - future improvements	CMI 2014 core projections with long annual improvement rate of 1.5%	CMI 2012 core projections with long annual improvement rate of 1.5%
Retirement cash sum	Each member is assumed to surrender pension on retirement, so total cash received is 80% of the maximum amount permitted	Each member is assumed to surrender pension on retirement, so total cash received is 80% of the maximum amount permitted

### 23. Actuarial Present Value of Promised Retirement Benefits

The CIPFA Code of Practice indicates that Pension Fund accounts should disclose the actuarial present value of promised retirement benefits as set out in the accounting standard IAS 26 and that the actuarial present value should be calculated on assumptions set in accordance with IAS 19 rather than on funding assumptions (set out in Note 22 to these accounts).

The Pension Fund Accounts do not take account of the liabilities to pay pensions and other benefits in the future. Instead, as permitted under IAS 26, the Pension Fund has opted to disclose the actuarial present value of promised retirement benefits by way of this note to the accounts. This requires the actuarial valuation of the liabilities on an IAS 19 basis to be prepared at triennial valuations only, the most recent being as at 31 March 2016.

The actuarial present value of promised retirement benefits has been calculated based on projected salaries and is included in the table below. The corresponding fair value of Fund Assets is also shown to indicate the level of deficit within the Fund when the liabilities are valued using IAS 19 assumptions. The figures for 2013 are provided for comparison purposes.

	Value as at 31 March 2016 £m	Value as at 31 March 2013 £m
Fair value of net assets	2,321	2,085
Actuarial present value of the promised retirement benefits	3,365	2,905
Surplus / -deficit in the Fund as measured for IAS26 purposes	-1,044	-820



As the liabilities above are calculated on an IAS 19 basis, they differ from those calculated for the triennial valuation because different assumptions are applied. The main IAS19 assumptions used are as follows:

	31 March 2016 (% p.a.)	31 March 2013 (% p.a.)
Discount rate	3.4	4.4
RPI Inflation	2.9	3.4
CPI Inflation	1.8	2.4
Rate of increase to pensions in payment *	1.8	2.4
Rate of increase to deferred pensions *	1.8	2.4
Rate of general increase in salaries **	3.3	3.9

\* In excess of Guaranteed Minimum Pension increases in payment where appropriate

\*\* In addition, we have allowed for the same age related promotional salary scales as used in the actuarial valuation of the Fund at the appropriate date

## 24. Funding Strategy Statement

The Local Government Pension Scheme Regulations 2013 require administering authorities to prepare a Funding Strategy Statement. This statement has been adopted by the Pension Fund Committee and has been published on the County Council's website at [durham.gov.uk](http://durham.gov.uk). The Funding Strategy Statement has been reviewed and updated by the Pension Fund Committee during 2016/17.

The purpose of the Funding Strategy Statement is to:

- establish a clear and transparent fund specific strategy which will identify how employers' pension liabilities are best met going forward;
- support the regulatory requirement to maintain as nearly constant employer contribution rates as possible;
- take a prudent longer term view of funding the Pension Fund's liabilities.

## 25. Investment Strategy Statement

In accordance with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, the Pension Fund has prepared and reviewed a written statement of its investment policy. The Investment Strategy Statement sets out the principles for investing Fund monies. The document was reviewed by the Pension Fund Committee during 2016/17 and can be found on the Council's website at [durham.gov.uk](http://durham.gov.uk).



## **Pension Fund**

# **Funding Strategy Statement**

---

**TABLE OF CONTENTS**

<b>Section</b>	<b>Page</b>
<b>A</b> Statutory Background and Key Issues	84
<b>B</b> Purpose of the Funding Strategy Statement	85
<b>C</b> Purpose and Aims of the Pension Fund	85
<b>D</b> Responsibilities of the Key Parties:	
The Administering Authority	87
Individual Employers	88
The Fund Actuary	89
<b>E</b> Funding Targets, Solvency and Employer asset shares	
Risk Based Approach	89
Solvency and 'funding success'	90
Probability of funding success	90
Funding Target	91
Application to different types of body	91
Full Funding and Solvency	92
Recovery Periods	92
Stepping	93
Grouping	93
Asset shares notionally allocated to employers	94
Roll forward of Asset shares	94
Fund Maturity	95
<b>F</b> Special Circumstances relating to Certain Employers	
Interim reviews	96
Guarantors	96
Bonds and other Securitisation	97
Subsumed Liabilities	98
Orphan Liabilities	98
Commencement of Employers	99
Cessation of Participation	99
<b>G</b> Links to Investment Policy set out in the Investment Strategy Statement	100
<b>H</b> Identification of Risks and Counter-Measures	100
<b>I</b> Monitoring and Review	104

## STATUTORY BACKGROUND AND KEY ISSUES

1. The Local Government Pension Scheme (England and Wales) (Amendment) Regulations 2004 came into effect on 1 April 2004. They originally provided the statutory framework from which Local Government Pension Schemes (LGPS) administering authorities were required to prepare a Funding Strategy Statement (FSS) by 31 March 2005. The requirements at the date of writing this Statement are now set out under Regulation 58 of the Local Government Pension Scheme Regulations 2013 (the Regulations).
2. Key issues:
  - After consultation with such persons as it considers appropriate (including officers and elected members and Fund employers), the administering authority is required to prepare and publish their funding strategy.
  - In preparing the FSS, the administering authority has to have regard to:
    - guidance published by CIPFA in October 2012 entitled "Guidance on Preparing and Maintaining a Funding Strategy Statement and to the Fund's Statement of Investment Principles" and updated guidance published by CIPFA in September 2016.
    - its Investment Strategy Statement (ISS) or Statement of Investment Principles (SIP) published under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the Investment Regulations).
  - The FSS must be revised and published whenever there is a material change in policy either on the matters set out in the FSS or the ISS or SIP.
  - Each Fund Actuary must have regard to the FSS as part of the fund valuation process and the Fund Actuary has therefore been consulted on the contents of this FSS.
  - The FSS addresses the issue of managing the need to fund benefits over the long term, whilst at the same time, allowing for scrutiny and accountability through improved transparency and disclosure.
  - Until 1 April 2014, the Scheme was a defined benefit final salary scheme. From 1 April 2014, the Scheme is a defined benefit career average revalued earnings scheme. The benefits at the date of writing this Statement are specified in the Regulations. Constraints on the levels of employee contributions are also specified in the Regulations.
  - Employer contributions are determined in accordance with the Regulations, which require that an actuarial valuation is completed every three years by the Fund Actuary.
3. This Statement was reviewed as part of the triennial valuation as at 31 March 2016, and has been updated in March 2017.

**(B) PURPOSE OF THE FUNDING STRATEGY STATEMENT**

4. The purpose of this Funding Strategy Statement (FSS) is to document the processes by which the Administering Authority:
- establishes a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward;
  - supports the regulatory requirement of the desirability of maintaining as nearly constant a primary rate of employer contribution rates as possible;
  - enables overall employer contributions to be kept as constant as possible and (subject to the Administering Authority not taking undue risks and ensuring that the regulatory requirements are met) at reasonable cost to the taxpayers, scheduled, designating and admitted bodies;
  - ensures that the regulatory requirements to set contributions so as to ensure the solvency and long-term cost efficiency of the Fund are met; and
  - takes a prudent longer-term view of funding the Fund's liabilities.

The intention is for this Strategy to apply comprehensively for the Fund as a whole to reflect its best interests, recognising that there will always be conflicting objectives which need to be balanced and reconciled. Whilst the position of individual employers must be reflected in the Statement, it must remain a single Strategy for the Administering Authority to implement and maintain.

**(C) PURPOSE AND AIMS OF THE PENSION FUND**

5. The purpose of the fund is to:

Invest monies in respect of contributions, transfer values and investment income to produce a Fund to pay Scheme benefits over the long term and in so doing to smooth out the contributions required from employers over the long term.

6. The aims of the fund are to:

- **Comply with Regulation 62 of the Regulations and specifically to adequately fund benefits to secure the Fund's solvency while taking account of the desirability of maintaining as nearly constant primary employer contribution rates as possible**

The Administering Authority aims to keep employer contributions as nearly constant as possible, whilst taking account of:

- the regulatory requirement to secure solvency and long term cost efficiency, which should be assessed in the light of the risk profile of the Fund and risk appetite of the Administering Authority and employers

- the requirement to ensure that costs are reasonable to Scheduled Bodies, Admission Bodies, other bodies and to taxpayers (subject to not taking undue risks), and
- maximising return from investments within reasonable risk parameters

In order to achieve nearly constant employer contribution rates there may be a need to invest in assets that match the employer's liabilities. In this context, 'match' means assets which behave in a similar manner to the liabilities as economic conditions alter. For the liabilities represented by benefits payable by the Local Government Pension Scheme, such assets would tend to comprise gilt edged investments.

The Administering Authority currently invests a large proportion of the Fund in equities, which are perceived as having higher long-term rates of return consistent with the requirement to maximise the returns from investments, within reasonable risk parameters. These assets are more risky in nature than fixed interest investments, and this can lead to more volatile returns in the short-term and a failure to deliver the anticipated returns in the long term.

This can have an effect on employer contribution rates as the funding position of the Pension Fund is measured at the triennial valuations. The impact of this can be reduced by smoothing adjustments at each actuarial valuation. Smoothing adjustments recognise that markets can rise and fall too far.

The Administering Authority recognises that there is a balance to be struck between the investment policy adopted, the smoothing mechanisms used at valuations, and the resultant stability of employer contribution rates from one valuation period to the next.

The Administering Authority also recognises that the position is potentially more volatile for admission bodies with short term contracts where utilisation of smoothing mechanisms is less appropriate.

- **Manage employers' liabilities effectively**

The Administering Authority seeks to manage employers' liabilities effectively. In a funding context, this is achieved by seeking actuarial advice and regular monitoring of the investment of the Fund's assets through quarterly meetings of the Pension Fund Committee and appropriate segregation of employers for funding purposes.

- **Ensure that sufficient resources are available to meet all liabilities as they fall due**

The Administering Authority recognises the need to ensure that the Fund has sufficient liquid assets to pay pensions, transfer values and other expenses. This position is continuously monitored and the cash available from contributions and cash held by Fund Managers is reviewed on a quarterly basis by the Pension Fund Committee.

- **Maximise the returns from investments within reasonable risk parameters.**

The Administering Authority recognises the desirability of maximising returns from investments within reasonable risk parameters, through investment in unmatched investments. Investment returns higher than those of fixed interest and index-linked bonds are sought from investment in equities, property and other growth assets. The Administering Authority ensures that risk parameters are reasonable by:

- ❖ Taking advice from its professional advisers, e.g. the Fund Actuary, Investment advisers and investment managers
- ❖ Controlling levels of investment in asset classes through the SIP or ISS
- ❖ Limiting default risk by restricting investment to asset classes recognised as appropriate for UK Pension Funds.
- ❖ Analysing the volatility and absolute return risks represented by those asset classes in collaboration with the Investment Adviser and Fund Managers, and ensuring that they remain consistent with the risk and return profiles anticipated in the funding strategy statement.
- ❖ Limiting concentration risk by developing a diversified investment strategy.
- ❖ Monitoring the mismatching risk, i.e. the risk that the investments do not move in line with the Fund's liabilities.

#### **(D) RESPONSIBILITIES OF THE KEY PARTIES**

7. Although a number of parties including investment fund managers and external auditors have responsibilities to the fund, the three parties whose responsibilities to the Fund are of particular relevance are the Administering Authority, the individual employers and the Fund Actuary:
8. The administering authority should:
  - Administer the Fund
  - Collect employer and employee contributions as set out in the Regulations
  - Determine a schedule of due dates for the payment of contributions - Section 70(1)(a) of the Pensions Act 2004 suggests that Administering Authorities are now required to report breaches as defined in Section 70 (2) of the 2004 Act. This places monitoring of the date of receipt of employer contributions on the Administering Authority and therefore places a duty to report material late payments of contributions to the Pensions Regulator.
  - Take action to recover assets from admission bodies whose Admission Agreement has ceased and other bodies whose participation in the Fund has ceased.

- Invest surplus monies in accordance with the Regulations.
- Pay from the Fund the relevant entitlements as set out in the Regulations.
- Ensure that cash is available to meet liabilities as and when they fall due.
- take measures as set out in the regulations to safeguard the fund against the consequences of employer default
- Manage the valuation process in consultation with the Fund's Actuary.
- Ensure effective communications with the Fund's Actuary to:
  - Ensure that the Fund Actuary is clear about the content of the Funding Strategy Statement;
  - Ensure reports are made available as required by guidance and regulation;
  - Agree timetables for the provision of information and valuation results;
  - Ensure provision of accurate data; and
  - Ensure that participating employers receive appropriate communications.
- Consider the appropriateness of interim valuations.
- Prepare and maintain an FSS and a SIP or ISS, both after proper consultation with interested parties, and
- Monitor all aspects of the fund's performance and funding and amend the FSS and SIP or ISS regularly as part of the on-going monitoring process.
- Effectively manage any potential conflicts of interest arising from its dual role as both Administering Authority and as a Scheme Employer.
- Enable the local Pension Board to review the valuation process as set out in their terms of reference

9. The individual employers should:

- Deduct contributions from employees' pay correctly.
- Pay all ongoing contributions, including their own as determined by the actuary, promptly by the due date.
- Pay any exit payments required in the event of their ceasing participation in the Fund.
- Develop a policy on certain discretions and exercise discretions within the regulatory framework, ensuring that the Administering Authority has copies of current policies covering those discretions.



- Make additional contributions in accordance with agreed arrangements in respect of, for example, additional membership or pension, augmentation of scheme benefits and early retirement strain, and
- Notify the administering authority promptly of all changes to membership, or as may be proposed, which affect future funding.
- Noting, and if desired responding to, any consultation regarding the Funding Strategy Statement, the Statement of Investment Principles, or other policies.

10. The fund actuary should:

- Prepare triennial valuations including the setting of employers' contribution rates at a level to ensure solvency and long term cost efficiency after agreeing assumptions with the administering authority and having regard to the FSS and the Regulations.
- Prepare advice and calculations in connection with bulk transfers, the funding aspects of individual benefit-related matters, valuations of exiting employers and other forms of security for the Administering Authority against the financial effect on the Fund of the employer's default. Such advice will take account of the funding position and Funding Strategy Statement, as well as other relevant matters when instructed to do so.
- Assist the Administering Authority in assessing whether employer contributions need to be revised between actuarial valuations as required or permitted by the Regulations.
- In response to a request from the Administering Authority, assess the impact of Regulatory changes on costs.
- Ensure that the Administering Authority is aware of any professional guidance or other professional requirements which may be of relevance to his or her role in advising the Administering Authority.

## **(E) FUNDING TARGETS, SOLVENCY AND EMPLOYER ASSET SHARES**

### **Risk based approach**

11. The Fund utilises a risk based approach to funding strategy.
12. A risk based approach entails carrying out the actuarial valuation on the basis of the assessed likelihood of meeting the funding objectives. In practice, three key decisions are required for the risk based approach:
- what the Solvency Target should be (the funding objective - where the Administering Authority wants the Fund to get to),
  - the Trajectory Period (how quickly the Administering Authority wants the Fund wants to get there), and

- the Probability of Funding Success (how likely the Administering Authority wants it to be now that the Fund will actually achieve the Solvency Target by the end of the Trajectory Period).

These three choices, supported by complex risk modelling carried out by the Fund Actuary, define the discount rate and, by extension, the appropriate levels of contribution payable. Together they measure the riskiness of the funding strategy.

These three terms are considered in more detail below.

### **Solvency and 'funding success'**

13. The Administering Authority's primary aim is long-term solvency. Accordingly, employers' contributions will be set to ensure that 100% of the liabilities can be met over the long term. The Solvency Target is the amount of assets which the Fund wishes to hold at the end of the Trajectory Period (see later) to meet this aim.
14. The Fund is deemed to be solvent when the assets held are equal to or greater than 100% of the Solvency Target. The Administering Authority believes that its funding strategy will ensure the solvency of the Fund because employers collectively have the financial capacity to increase employer contributions should future circumstances require, in order to continue to target a funding level of 100%
  - For Scheduled Bodies, and certain other bodies, of sound covenant whose participation is indefinite in nature, appropriate actuarial methods and assumptions are taken to be measurement by use of the Projected Unit method of valuation, and using assumptions such that, if the Fund's financial position continued to be assessed by use of such methods and assumptions, and contributions were paid in accordance with those methods and assumptions, there would be a chance of at least 80% that the Fund would continue to be 100% funded over a time period considered appropriate at the time of assessment. The level of funding implied by this is the Solvency Target. For the purpose of this Statement, the required level of chance is defined as the Probability of Maintaining Solvency.
  - For certain Admission Bodies, bodies closed to new entrants and other bodies whose participation in the Fund is believed to be of limited duration through known constraints or reduced covenant, and for which no access to further funding would be available to the Fund after exit, the required Probability of Maintaining Solvency will be set at a level higher than 80% dependent on circumstances. For most such bodies, the chance of achieving solvency will be set commensurate with assumed investment in an appropriate portfolio of Government index linked and fixed interest bonds after exit.

### **Probability of Funding Success**

15. The Administering Authority deems funding success to have been achieved if the Fund, at the end of the Trajectory Period, has achieved the Solvency Target. The Probability of Funding Success is the assessed chance of this happening based on the level of contributions payable by members and employers.

16. Consistent with the aim of enabling employers' contribution rates to be kept as nearly constant as possible, the required chance of achieving the Solvency Target at the end of the relevant Trajectory Period for each employer or employer group can be altered at successive valuations within an overall envelope of acceptable risk. The Administering Authority will not permit contributions to be set following a valuation that have an unacceptably low chance of achieving the Solvency Target at the end of the relevant Trajectory Period.
17. At the 2016 valuation, the Trajectory Period used was 25 years, and the probability of Funding Success was set to be 67%.

### **Funding Target**

18. In order to satisfy the legislative requirement to secure long term cost efficiency the Administering Authority's aim is for employer contributions to be set so as to make provision for the cost of benefit accrual, with an appropriate adjustment for any surplus or deficiency. This is achieved through the setting of a Funding Target.
19. The Funding Target is the amount of assets which the Fund needs to hold at the valuation date to pay the liabilities at that date as indicated by the chosen valuation method and assumptions. It is a product of the triennial actuarial valuation exercise and is not necessarily the same as the Solvency Target. It is instead the product of the data, chosen assumptions, and valuation method. The valuation method including the components of Funding Target, future service contributions and any adjustment for surplus or deficiency set the level of contributions payable, and dictate the chance of achieving the Solvency Target at the end of the Trajectory Period (defined below). The Funding Target will be the same as the Solvency Target only when the methods and assumptions used to set the Funding Target are the same as the appropriate funding methods and assumptions used to set the Solvency Target (see above).
20. Consistent with the aim of enabling employers' primary contribution rates to be kept as nearly constant as possible:
- Contribution rates are set by use of the Projected Unit valuation method for most employers. The Projected Unit method is used in the actuarial valuation to determine the cost of benefits accruing to the Fund as a whole and for employers who continue to admit new members. This means that the future service (primary) contribution rate is derived as the cost of benefits accruing to employee members over the year following the valuation date expressed as a percentage of members' pensionable pay over that period.
  - For employers who no longer admit new members, the Attained Age valuation method is normally used. This means that the future service (primary) contribution rate is derived as the average cost of benefits accruing to members over the period until they die, leave the Fund or retire.

### **Application to different types of body**

21. Some comments on the principles used to derive the Solvency and Funding Targets for different bodies in the Fund are set out below.

- **Scheduled Bodies and certain other bodies of sound covenant**  
The Administering Authority will adopt a general approach in this regard of assuming indefinite investment in a broad range of assets of higher risk than low risk assets for Scheduled Bodies and certain other bodies which are long term in nature.
- **Admission Bodies and certain other bodies whose participation is limited**  
For Admission Bodies, bodies closed to new entrants and other bodies whose participation in the Fund is believed to be of limited duration through known constraints or reduced covenant, and for which no access to further funding would be available to the Fund after exit the Administering Authority will have specific regard to the potential for participation to cease (or to have no contributing members), the potential timing of such exit, and any likely change in notional or actual investment strategy as regards the assets held in respect of the body's liabilities at the date of exit (i.e. whether the liabilities will become 'orphaned' or whether a guarantor exists to subsume the notional assets and liabilities).

### **Full Funding and Solvency**

22. The Fund is deemed to be fully funded when the assets held are equal to 100% of the Funding Target, where the funding target is assessed based on the sum of the appropriate funding targets across all the employers/groups of employers..
23. The Fund is deemed to be solvent when the assets held are equal to or greater than 100% of the Solvency Target.

### **Recovery Periods**

24. The Recovery Period in relation to an employer is the period between the valuation date and the date on which solvency is targeted to be achieved.
25. Where a valuation shows the Fund to be in surplus or deficit against the Funding Target, employers' contribution rates will be adjusted to reach the solvent position over a number of years. The Recovery Period in relation to an employer or group of employers is therefore a period over which any adjustment to the level of contributions in respect of a surplus or deficiency relative to the Funding Target used in the valuation is payable.
26. The Recovery Period applicable for each employer is set by the Fund Actuary in consultation with the Administering Authority and the employer, with a view to balancing the various funding requirements against the risks involved due to such issues as the financial strength of the employer and the nature of its participation in the Fund.
27. The Administering Authority recognises that a large proportion of the Fund's liabilities are expected to arise as benefits payments over a long period of time. For employers of sound covenant, the Administering Authority is therefore prepared to agree Recovery Periods that are longer than the average future working lifetime of the membership of that employer. In general for employers that are closed to new entrants and are of sufficient term, the Recovery Period is set to be the estimated future working lifetime of the active membership (i.e. the estimated period of time

until the last active member leaves or retires). The Administering Authority recognises that such an approach is consistent with the aim of keeping employer contribution rates as nearly constant as possible.

28. However, the Administering Authority also recognises the risk involved in relying on long Recovery Periods and has agreed with the Actuary a maximum recovery period of 30 years for both, for employers which are assessed by the Administering Authority as being a long term secure employer. It is the intention of the Administering Authority to agree with employers a Recovery Period of as short a time as possible within this 30 year limit having regard to the affordability of the revised contribution rate in general taking into account the legislative requirements of securing solvency and maintaining as nearly a constant a contribution rate as possible. A period of 21 years has been used for Durham County Council at the 2016 valuation, the largest employer in the Fund. Recovery Periods for other employers or employer groups may be shorter and may not necessarily be the same as each other, in order to suitably balance risk to the Fund and cost to the employer.
29. For each individual employer the following will also be taken into account:
- covenant and strength of any guarantee relating to an employer and hence the risk of default
  - length of participation in the Fund
  - whether the employer is closed to new entrants or is likely to have a contraction in its membership of the Fund

### **Stepping**

30. The Administering Authority will also consider at each valuation whether new contribution rates should be payable immediately or reached by being stepped over a number of years. Stepping is a generally accepted method of smoothing the impact of rate changes for local authority pension funds. In consultation with the Actuary, the Administering Authority accepts that long term employers may step up to the new rates. This is in line with the aim of having contribution rates as nearly constant as possible. The Administering Authority usually allows a maximum of three steps however, in exceptional circumstances up to six steps may be used.

### **Grouping**

31. In some circumstances it may be desirable to group employers within the Fund together for funding purposes (i.e. to calculate employer contribution rates). Reasons might include reduction of volatility of contribution rates for small employers, facilitating situations where employers have a common source of funding or accommodating employers who wish to share the risks related to their participation in the Fund.
32. The Administering Authority recognises that grouping can give rise to cross subsidies from one employer to another over time. Employers may be grouped entirely, such that all of the risks of participation are shared, or only partially grouped such that only specified risks are shared. The Administering Authority's

policy is to consider the position carefully at initial grouping and at each valuation and to notify each employer that is grouped which other employers it is grouped with and details of the grouping method used. If the employer objects to this grouping, it will be set its own contribution rate.

33. Where employers are grouped together for funding purposes, this will only occur with the consent of the employers involved.
34. All employers in the Fund are grouped together in respect of the risks associated with payment of lump sum benefits on death in service, and, from 1 April 2016, survivors pensions on death in service and payment of ill health pensions – in other words, the cost of such benefits is shared across the employers in the Fund. Such benefits can cause funding strains which could be significant for some of the smaller employers without insurance or sharing of risks. The Fund, in view of its size, does not see it as cost effective or necessary to insure these benefits externally and this is seen as a pragmatic and low cost approach to spreading the risk.
35. Where employers are pooled together for funding and contribution purposes, all risks are shared within the group and they have a single contribution rate.

### **Asset shares notionally allocated to employers**

36. In order to establish contribution rates for individual employers or groups of employers it is convenient to notionally subdivide the Fund as a whole between the employers (or group of employers where grouping operates), as if each employer had its own asset share within the Fund.
37. This subdivision is for funding purposes only. It is purely notional in nature and does not imply any formal subdivision of assets, or ownership of any particular assets or groups of assets by any individual employer or group.

### **Roll-forward of asset shares**

38. The asset share allocated to each employer will be rolled forward allowing for all cash flows associated with that employer's membership, including contribution income, benefit outgo, transfers in and out and investment income. In general no allowance is made for the timing of contributions and cash flows for each year are assumed to be made half way through the year with investment returns assumed to be uniformly earned over that year. However, where significant one-off employer contributions have been paid, allowance is made for the timing of such contributions.
39. Further adjustments are made for:
  - A notional deduction to meet the expenses paid from the Fund in line with the assumption used at the previous valuation.
  - Allowance for any known material internal transfers in the Fund (cash flows will not exist for these transfers). The Fund Actuary will assume an estimated cash

flow equal to the value of the liabilities determined consistent with the Funding Target transferred from one employer to the other unless some other approach has been agreed between the two employers.

- Allowance for lump sum death in service and other benefits shared across all employers in the Fund (see earlier).
- An overall adjustment to ensure the notional assets attributed to each employer is equal to the total assets of the Fund which will take into account any gains or losses related to the orphan liabilities.

40. In some cases information available will not allow for such cash flow calculations. In such a circumstance:

- Where, in the opinion of the Fund Actuary, the cash flow data which is unavailable is of low materiality, estimated cash flows will be used.
- Where, in the opinion of the Fund Actuary, the cash flow data which is unavailable is material, the Fund Actuary will instead use an analysis of gains and losses to roll forward the asset share. Analysis of gains and losses methods are less precise than use of cash flows and involve calculation of gains and losses relative to the surplus or deficiency exhibited at the previous valuation. Having established an expected surplus or deficiency at this valuation, comparison of this with the liabilities evaluated at this valuation leads to an implied notional asset holding.

41. Analysis of gains and losses methods will also be used where the results of the cash flow approach appears to give unreliable results perhaps because of unknown internal transfers.

### **Fund maturity**

42. To protect the Fund, and individual employers, from the risk of increasing maturity producing unacceptably volatile contribution adjustments as a percentage of pay the Administering Authority will normally require contributions as monetary amounts from employers in respect of any disclosed funding deficiency.

43. In certain circumstances, for secure employers considered by the Administering Authority as being long term in nature, contribution adjustments to correct for any disclosed deficiency may be set as a percentage of payroll. Such an approach carries an implicit assumption that the employer's payroll will increase at an assumed rate. If payroll fails to grow at this rate, or declines, insufficient corrective action will have been taken. To protect the Fund against this risk, the Administering Authority will monitor payrolls and where evidence is revealed of payrolls not increasing at the anticipated rate, the Administering Authority will consider requiring deficit contributions as monetary amounts rather than percentages of payroll.

## **(F) SPECIAL CIRCUMSTANCES RELATED TO CERTAIN EMPLOYERS**

### **Interim reviews**

44. Regulation 64 of the Regulations provides the Administering Authority with a power to carry out valuations in respect of employers who are likely to become an exiting employer, and for the Actuary to certify revised contribution rates, between triennial valuation dates.
45. The Administering Authority's overriding objective at all times in relation to employers is that, where possible, there is clarity over the Funding Target for that body, and that contribution rates payable are appropriate for that Funding Target. However, this is not always possible as any exit date may be unknown (for example, participation may be assumed at present to be indefinite), and also because market conditions change daily.
46. The Administering Authority's general approach in this area is as follows:
  - Where the exit date is known, and is more than 3 years hence, or is unknown and assumed to be indefinite, the Administering Authority will generally not deem it necessary to carry out an interim valuation.
  - For Admission Bodies admitted under paragraph 1(d) of Part 3, Schedule 2 of the Regulations falling into the above category, the Administering Authority sees it as the responsibility of the relevant Scheme Employer to instruct it if an interim valuation is required. Such an exercise would be at the expense of the relevant Scheme Employer unless otherwise agreed.
  - A material change in circumstances, such as the exit date becoming known, material membership movements or material financial information coming to light may cause the Administering Authority to informally review the situation and subsequently formally request an interim valuation.
  - For an employer whose participation is due to cease within the next 3 years, the Administering Authority will keep an eye on developments and may see fit to request an interim valuation at any time.
47. Notwithstanding the above guidelines, the Administering Authority reserves the right to request an interim valuation of any employer at any time if Regulation 64(4) of the Regulations applies.

### **Guarantors**

48. Some employers may participate in the Fund by virtue of the existence of a Guarantor. The Administering Authority maintains a list of employers and their associated Guarantors. The Administering Authority, unless notified otherwise, sees the duty of a Guarantor to include the following:
  - If an employer exits and defaults on any of its financial obligations to the Fund, the Guarantor is expected to provide finance to the Fund such that the



Fund receives the amount certified by the Fund Actuary as due, including any interest payable thereon.

- If the Guarantor is an employer in the Fund and is judged to be of suitable covenant by the Administering Authority, the Guarantor may defray some of the financial liability by subsuming the residual liabilities into its own pool of Fund liabilities. In other words, it agrees to be a source of future funding in respect of those liabilities should future deficiencies emerge.

49. During the period of participation of the employer a Guarantor can at any time agree to the future subsumption of any residual liabilities of an employer. The effect of that action would be to reduce the Funding and Solvency Target for the employer, which would probably lead to reduced contribution requirements.

### **Bonds and other securitisation**

50. Paragraph 6 of Part 3, Schedule 2 of the Regulations creates a requirement for a new Admission Body to carry out, to the satisfaction of the Administering Authority (and the Scheme Employer in the case of an Admission Body admitted under paragraph 1(d)(i) of that Part), an assessment taking account of actuarial advice of the level of risk on premature termination by reason of insolvency, winding up or liquidation.

51. Where the level of risk identified by the assessment is such as to require it, the admission body shall enter into an indemnity or bond with an appropriate party. Where it is not desirable for an Admission Body to enter into an indemnity or bond, the body is required to secure a guarantee in a form satisfactory to the Administering Authority from an organisation who either funds, owns or controls the functions of the admission body.

52. The Administering Authority's approach in this area is as follows:

- In the case of Admission Bodies admitted under Paragraph 1(d) of Part 3, Schedule 2 of the Regulations and other Admission Bodies with a Guarantor, and so long as the Administering Authority judges the relevant Scheme Employer or Guarantor to be of sufficiently sound covenant, any bond exists purely to protect the relevant Scheme Employer on default of the Admission Body. As such, it is entirely the responsibility of the relevant Scheme Employer or Guarantor to arrange any risk assessments and decide the level of required bond. The Administering Authority will be pleased to supply some standard calculations provided by the Fund Actuary to aid the relevant Scheme Employer, but this should not be construed as advice to the relevant Scheme Employer on this matter. The Administering Authority notes that levels of required bond cover can fluctuate and recommends that relevant Scheme Employers review the required cover regularly, at least once a year.
- In the case of:
  - admission bodies admitted under paragraph 1(e) of Part 3, Schedule 2;
  - admission bodies admitted under paragraph 1(d) of Part 3, Schedule 2 where the administering authority does not judge the Scheme Employer to be of sufficiently strong covenant;

- other admission bodies with no Guarantor or where the administering authority does not judge the Guarantor to be of sufficiently strong covenant;

the administering authority must be involved in the assessment of the required level of bond to protect the Fund. The admission will only be able to proceed once the Administering Authority has agreed the level of bond cover. The Administering Authority will supply some standard calculations provided by the Fund Actuary to aid the relevant Scheme Employer to form a view on what level of bond would be satisfactory. The Administering Authority will also on request supply this to the Admission Body or Guarantor. This should not be construed as advice to the Scheme Employer, Guarantor or Admission Body. The Administering Authority notes that levels of required bond cover can fluctuate and will recommend the relevant Scheme Employer to jointly review the required cover with it regularly, at least once a year.

### **Subsumed liabilities**

53. Where an employer is exiting the Fund such that it will no longer have any contributing members, it is possible that another employer in the Fund agrees to provide a source of future funding in respect of any emerging deficiencies in respect of those liabilities.
54. In such circumstances the liabilities are known as subsumed liabilities (in that responsibility for them is taken on by the accepting employer). For such liabilities the Administering Authority will assume that the investments held in respect of those liabilities will be the same as those held for the rest of the liabilities of the accepting employer. Generally this will mean assuming continued investment in more risky investments than Government bonds.

### **Orphan liabilities**

55. Where an employer is exiting the Fund such that it will no longer have any contributing members, unless any residual liabilities are to become subsumed liabilities, the Administering Authority will act on the basis that it will have no further access for funding from that employer once any exit valuation, carried out in accordance with Regulation 64 of the Regulations, has been completed and any sums due have been paid. Residual liabilities of employers from whom no further funding can be obtained are known as orphan liabilities.
56. The Administering Authority will seek to minimise the risk to other employers in the Fund that any deficiency arises on the orphan liabilities such that this creates a cost for those other employers to make good the deficiency. To give effect to this, the Administering Authority will seek funding from the outgoing employer sufficient to enable it to match the liabilities with low risk investments, generally Government fixed interest and index linked bonds.
57. To the extent that the Administering Authority decides not to match these liabilities with Government bonds of appropriate term then any excess or deficient returns will be added to or deducted from the investment return to be attributed to the other employer's notional assets.

58. Liabilities in the Fund which are already orphaned will be assumed to be 100% funded on the appropriate funding target at each triennial valuation. This will be achieved by the Actuary notionally re-allocating assets within the Fund as required.

### **Commencement of Employers**

59. When a new employer starts in the Fund, and members transfer from another employer in the Fund, a notional transfer of assets is needed from the original employer to the new employer. The approach used will depend on the circumstances surrounding the commencement of the new employer and some comments are set out below.
60. When a new admission body starts in the Fund due to an outsourcing event, they will usually start as fully funded on the Funding Target appropriate to the new employer. This means that any past service surplus or deficit for the members who are transferring to the new employer remains with the original employer and does not transfer to the new employer.
61. For academies, a prioritised share of fund approach is followed. This involves fully funding the non-active members of the original employer at the previous triennial valuation, and using the residual assets to calculate the funding level applicable to the active members of the original employer. This is rolled forward in line with the progression of the overall funding level of the original employer during the period from the last valuation date to the date of commencement of the academy. The funding level applicable to the active members is then used to calculate the notional asset transfer to the new employer.
62. In other circumstances the notional asset transfer will often be subject to the agreement between the relevant parties and the Administering Authority (who will take advice from the Fund Actuary). In the event of any dispute the Administering Authority will take make the final decision having taken account of the issues related to the setting up of the new employer.

### **Cessation of participation**

63. Where an employer becomes an exiting employer, an exit valuation will be carried out in accordance with Regulation 64 of the Regulations. That valuation will take account of any activity as a consequence of exit regarding any existing contributing members (for example any bulk transfer payments due) and the status of any liabilities that will remain in the Fund.
64. In particular, the exit valuation will distinguish between residual liabilities which will become orphan liabilities, and liabilities which will be subsumed by other employers.
- For orphan liabilities the Funding Target in the exit valuation will anticipate investment in low risk investments such as Government bonds.
  - For subsumed liabilities the exit valuation will anticipate continued investment in assets similar to those held in respect of the subsuming employer's liabilities.

65. Regardless of whether the residual liabilities are orphan liabilities or subsumed liabilities, the departing employer will be expected to make good the funding position revealed in the exit valuation. In other words, the fact that liabilities may become subsumed liabilities does not remove the possibility of an exit payment being required.

**(G) LINKS TO INVESTMENT POLICY SET OUT IN THE STATEMENT OF INVESTMENT PRINCIPLES OR INVESTMENT STRATEGY STATEMENT**

66. The current investment strategy, as set out in the SIP or ISS, is summarised below:

**General Principles and diversification**

67. The Fund believes that the emphasis of investment over the long term should be on real assets, particularly equities and property. These are most likely to maximise the long term returns. The balance between UK and Overseas equities is, however, a matter of investment judgement. The Fund should also be diversified to include other real assets, such as Index-Linked and 'monetary' assets, such as Bonds and Cash.
68. The neutral benchmark proportions of the various asset classes have been determined by the Fund in consultation with the Investment Advisers and are reviewed at least once every three years to coincide with the Triennial Actuarial Valuation.
69. The active Investment managers are expected to adopt an active asset allocation policy to take advantage of the shorter term relative attractions of the various asset types.
70. The Administering Authority has produced this Funding Strategy Statement having taken a view on the level of risk inherent in the investment policy set out in the SIP or ISS and the funding policy set out in this document.
71. The SIP or ISS sets out the investment responsibilities and policies relevant to the Fund.
72. The Administering Authority will continue to review both documents to ensure that the overall risk profile remains appropriate.

**(H) IDENTIFICATION OF RISKS AND COUNTER-MEASURES**

73. The Administering Authority seeks to identify all risks to the Fund, will monitor the risks and take appropriate action to limit the impact of them wherever possible. The Administering Authority will ensure that funding risks are included within their overarching risk management framework and strategy, linking to their risk register and risk management policy as appropriate and includes defining a role for the Local Pension Board within this framework.
74. For ease of classification some of the key risks may be identified as follows:
75. Investment

These include:

- assets not delivering the required return (for whatever reason, including manager underperformance)
- systemic risk with the possibility of interlinked and simultaneous financial market volatility
- having insufficient funds to meet liabilities as they fall due
- inadequate, inappropriate or incomplete investment and actuarial advice is taken and acted upon
- counterparty failure

The specific risks associated with assets and asset classes are:

- equities – industry, country, size and stock risks
- fixed income - yield curve, credit risks, duration risks and market risks
- alternative assets – liquidity risks, property risk, alpha risk
- money market – credit risk and liquidity risk
- currency risk
- macroeconomic risks

The Administering Authority reviews each investment manager's performance quarterly and annually considers the asset allocation of the Fund by carrying out an annual review meeting. The Administering Authority also annually reviews the effect of market movements on the Fund's overall funding position.

## 76. Employer

These include:

- the risk arising from ever changing mix of employers, from short term and exiting employers, and the potential for a shortfall in payments and / or orphaned liabilities.

The Administering Authority will put in place a Funding Strategy Statement which contains sufficient detail on how funding risks are managed in respect of the main categories of employer (e.g. scheduled and admission bodies) and other pension fund stakeholders.

The Administering Authority maintains a knowledge base on their employers, their basis of participation and their legal status and will use this information to set a funding strategy for the relevant employers

## 77. Liability

These include:

- Interest rates being lower than expected
- Pay increases being higher than expected
- Price inflation being higher than expected
- The longevity horizon continuing to expand
- Deteriorating patterns of early retirements

The Administering Authority will ensure that the Actuary investigates these matters at each valuation. Prudent management of the fund should ensure that sound policies and procedures are in place to manage, e.g. potential ill health or early retirements.

78. Regulatory

These include:

- Changes to general and LGPS specific regulations, e.g. more favourable benefits package, potential new entrants to the scheme, e.g. part-time employees
- Changes to national pension requirement and/or Inland Revenue rules

79. Liquidity and maturity

These include:

- An increased emphasis on outsourcing and alternative models for service delivery may result in active members leaving the LGPS
- Transfer of responsibility between different public sector bodies
- Scheme changes which might lead to increased opt-outs
- Spending cuts and their implications

All of these may result in workforce reductions that would reduce membership, reduce contributions and prematurely increase retirements in ways that may not have been taken into account in previous forecasts.

The Administering Authority's policy is to require regular communication between itself and employers and to ensure reviews of maturity at overall Fund and employer level where material issues are identified.

80. Governance

These include:

- Administering authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements)
- Administering authority not advised of an employer closing to new entrants
- An employer ceasing to exist with insufficient funding or adequacy of a bond

The Administering Authority requires regular communication with employers to ensure that it is made aware of any such changes in a timely manner.

81. Choice of Solvency and Funding Targets

The Administering Authority recognises that future experience and investment income cannot be predicted with certainty. Instead, there is a range of possible outcomes, and different assumed outcomes will lie at different places within that range.

The more optimistic the assumptions made in determining the Funding Target and Solvency Target, the more that outcome will sit towards the 'favourable' end of the range of possible outcomes, the lower will be the probability of experience actually matching or being more favourable than the assumed experience, and the lower will be the Funding Target and Solvency Target calculated by reference to those assumptions.

The Administering Authority will not adopt assumptions for Scheduled Bodies and certain other bodies which, in its judgement, and on the basis of actuarial advice received, are such that it is less than 55% likely that the strategy will deliver funding success (as defined earlier in this document). Where the probability of funding success is less than 65% the Administering Authority will not adopt assumptions which lead to a reduction in the aggregate employer contribution rate to the Fund.

The Administering Authority's policy will be to monitor the underlying position assuming no such excess returns are achieved to ensure that the funding target remains realistic relative to the low risk position.

## 82. Smoothing of Assets

These include:

- The utilisation of a smoothing adjustment in the solvency measurement introduces an element of risk, in that the smoothing adjustment may not provide a true measure of the underlying position

The Administering Authority's policy is to review whether an approach is suitable and if so ensure the impact of this adjustment remains within acceptable limits.

## 83. Recovery Period

These include:

- Permitting surpluses or deficiencies to be eliminated over a recovery period rather than immediately introduces a risk that action to restore solvency is insufficient between successive measurements

The Administering Authority's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the permitted length of Recovery Period where appropriate. Details of the Administering Authority's policy are set out earlier in this Statement.

## 84. Stepping

These include:

- Permitting contribution rate changes to be introduced by annual steps rather than immediately introduces a risk that action to restore solvency is insufficient in the early years of the process

The Administering Authority's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the number of permitted steps as appropriate. Details of the Administering Authority's Policy are set out earlier in this Statement.

**(I) MONITORING AND REVIEW**

85. The Administering Authority must keep the FSS under review and make appropriate revisions following a material change in policy. The triennial valuation exercise will establish contribution rates for all employers contributing to the fund within the framework provided by the strategy.





## Pension Fund

# Investment Strategy Statement

### Table of Contents

<b>Paragraph</b>		<b>Page</b>
1	Introduction	106
2	Investment Responsibilities	106
3	Investment Beliefs and Objectives	108
4	Investment strategy and the process for ensuring suitability of investments	109
5	Risk measurement and management	110
6	Approach to asset pooling	112
7	Environmental, Social and Corporate Governance policy and policy of the exercise of rights (including voting rights) attaching to investments	116
Appendix 1	Myners' Principles	116

# **INVESTMENT STRATEGY STATEMENT**

## **DURHAM COUNTY COUNCIL PENSION FUND MARCH 2017**

### **1 Introduction**

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 ('the 2016 Investment Regulations') require administering authorities to formulate and to publish a statement of its investment strategy, in accordance with guidance issued from time to time by the Secretary of State.

This Investment Strategy Statement (ISS) has been designed to be a living document and is an important governance tool for the Durham County Council Pension Fund ('the Pension Fund'). This document sets out the investment strategy of the Pension Fund, provides transparency in relation to how the Pension Fund investments are managed, acts as a risk register, and has been kept as short in order to be read in as user-friendly manner as is possible. This document replaces the Pension Fund's Statement of Investment Principles.

This statement will be consulted on at least every three years and reviewed by the Pension Fund Committee ('the Committee') more frequently should any significant change occur.

### **2 Investment Responsibilities**

The County Council, as Administering Authority for the Pension Fund, has delegated the investment arrangements of the Pension Fund to the Pension Fund Committee (the "Committee") who decide on the investment policy most suitable to meet the liabilities of the Pension Fund and the ultimate responsibility for the investment policy lies with it. The Committee is made up of elected representatives of the County Council, Darlington Borough Council, Further Education Colleges, Other Statutory Bodies, Admitted Bodies and Member Representatives.

The Committee has full delegated authority to make investment decisions.

#### **2.1 The Pension Fund Committee has responsibility for:**

- Determining overall investment strategy and strategic asset allocation and ensuring that investments are sufficiently diversified, are not over concentrated in any one type of investment, and that the Pension Fund is invested in suitable types of investments;
- Preparing policy documents including the ISS and Funding Strategy Statement (FSS). Monitoring compliance with the ISS and reviewing its contents following any strategic changes and at least every three years;
- Appointing the investment managers, custodian, the Pension Fund actuary and any independent external advisers felt to be necessary for the good stewardship of the Pension Fund;
- Reviewing on a regular basis the investment managers' performance against established benchmarks, and satisfying themselves as to the investment managers' expertise and the quality of their internal systems and controls;
- Reviewing on a regular basis the performance of the independent external advisers;

- In cases of unsatisfactory performance of the investment managers and independent external advisers, taking appropriate action;
- Reviewing policy on social, environmental and ethical matters and on the exercise of rights, including voting rights; and
- Reviewing the funds allocated to investment managers on a regular basis to ensure that the strategic asset allocation is maintained (rebalancing).

## **2.2 The investment managers are responsible for:**

- The investment of the Pension Fund assets in respect of which they are appointed in compliance with applicable rules and legislation, the constraints imposed by this document and the detailed Investment Management Agreement covering their portion of the Pension Fund's assets;
- Stock selection within asset classes;
- Preparation of quarterly reports, including a review of investment performance;
- Attending meetings of the Committee as requested;
- Where specifically instructed, voting in accordance with the Pension Fund's policy.

## **2.3 The Global Custodian is responsible for:**

- Its own compliance with prevailing legislation;
- Providing the administering authority with quarterly valuations of the Pension Fund's assets and details of all transactions during the quarter;
- Collection of income, tax reclaims, exercising corporate administration and cash management;
- Such other services as the Pension Fund shall procure, for example, in connection with performance measurement and reporting or fund accounting.

## **2.4 The Investment Adviser is responsible for:**

- Assisting the Corporate Director Resources and the Committee in determining the overall investment strategy, the strategic asset allocation and that the Pension Fund is invested in suitable types of investment, and ensuring that investments are sufficiently diversified.
- Assisting the Corporate Director Resources and the Committee in the preparation and review of Policy documents;
- Assisting the Corporate Director Resources and the Committee in their regular monitoring of the investment managers' performance;
- Assisting the Corporate Director Resources and the Committee, where required, in the selection and appointment of investment managers, custodians and Pension Fund Actuary;
- Advising and assisting the Corporate Director Resources and the Committee on other investment related issues, which may arise from time to time; and
- Providing continuing education and training to the Committee.

## **2.5 The Actuary is responsible for:**

- Providing advice as to the structure of the Pension Fund's liabilities, the maturity of the Pension Fund and its funding level in order to aid the

Committee in balancing the short term and long-term objectives of the Pension Fund.

- Carrying out its responsibilities as set out in the FSS.
- Undertaking the statutory triennial valuation of the Pension Fund's assets and liabilities.

## **2.6 The Corporate Director Resources is responsible for:**

- Ensuring compliance with this document and bringing breaches thereof to the attention of the Committee;
- Ensuring that this document is regularly reviewed and updated in accordance with the 2016 Investment Regulations;
- Exercising delegated powers granted by the County Council to:
  - Administer the financial affairs in relation to the County Council's functions as a pension fund administering authority;
  - Exercise those discretions under the Local Government Pension Scheme Regulations 2013 as appear from time to time in Pension Fund Statements of Policy; and
  - Authorise, in cases of urgency, the taking of any action by an investment manager of the Pension Fund which is necessary to protect the interests of the Pension Fund.
  - Managing the cash balances of the Pension Fund which the Investment Managers have not invested.

## **3 Investment Beliefs and Objectives**

The Pension Fund has the following investment beliefs which help to inform the investment strategy derived from the decision making process:

- Funding, investment strategy and contribution rates are linked
- The strategic asset allocation is the key factor in determining the risk and return profile of the Pension Fund's investments
- Investing over the long term provides opportunities to improve returns
- Diversification across asset classes can help to mitigate against adverse market conditions and assist the Pension Fund to produce a smoother return profile due to returns coming from a range of different sources
- Managing risk is a multi-dimensional and complex task but the overriding principle is to avoid taking more risk than is necessary to achieve the Pension Fund's objectives
- Environmental, Social and Governance are important factors for the sustainability of investment returns over the long term
- Value for money from investments is important, not just absolute costs.
- Asset pooling will help reduce costs whilst providing more choice of investments and will therefore be additive to Pension Fund returns
- High conviction active management can add value to returns

The Administering Authority's primary aim is long-term solvency. Accordingly, employers' contributions will be set to ensure that 100% of the liabilities can be met over the long term. The Solvency Target is the amount of assets which the Fund requires to hold to meet its objective of paying all benefits arising as they fall due.

#### 4 Investment strategy and the process for ensuring suitability of investments.

The Pension Fund's objective is to pay benefits as they fall due. The Pension Fund is currently assessed to have a deficit in respect to previously accrued liabilities, and so the strategy is focused on recovering this deficit as well as maintaining affordable contributions for future benefit accrual, without taking undue risks. Having a thorough understanding of the risks facing the Pension Fund is crucial and these are covered later in the statement.

The Pension Fund's asset strategy, along with an overview of the role each asset plays is set out in the table below:

<b>Asset class</b>	<b>Allocation %</b>	<b>Benchmark &amp; Performance Target</b>	<b>Role (s) within the strategy</b>
Global Equities	15.0	MSCI All Country World Index (unhedged) in GBP terms +3%	Long term growth in excess of inflation expected; Generate investment income i.e. dividends.
	15.0	MSCI World index +2.5%	
Emerging Market Equities	7.0	MSCI Emerging Markets Net Index +2.5%	
Index Linked Gilts	20.0	FTSE Over 5 Year Index-Linked Gilt Index +0.5%	Provide protection from changes in inflation both in terms of capital value and income
Global Bonds	15.0	UK 3-month LIBOR +3.0%	Diversified source of income and provides a degree of protection from changes in interest rates. Some growth above gilts expected
Dynamic Asset Allocation	20.0	UK 3-month LIBOR +3.0%	Diversification and Tactical Asset Allocation
Global Property	8.0	UK Retail Price Inflation +5.0%	Diversification; Generate investment income; Provide some inflation-sensitive exposure; Illiquidity premium

The Committee is responsible for the Pension Fund's asset allocation which is determined via a triennial strategy review as part of the valuation process. The review is both qualitative and quantitative and is undertaken by the Committee in conjunction with the actuary, officers and investment adviser. The review considers:

- The required level of return that will mean the Pension Fund can meet its future benefit obligations as they fall due

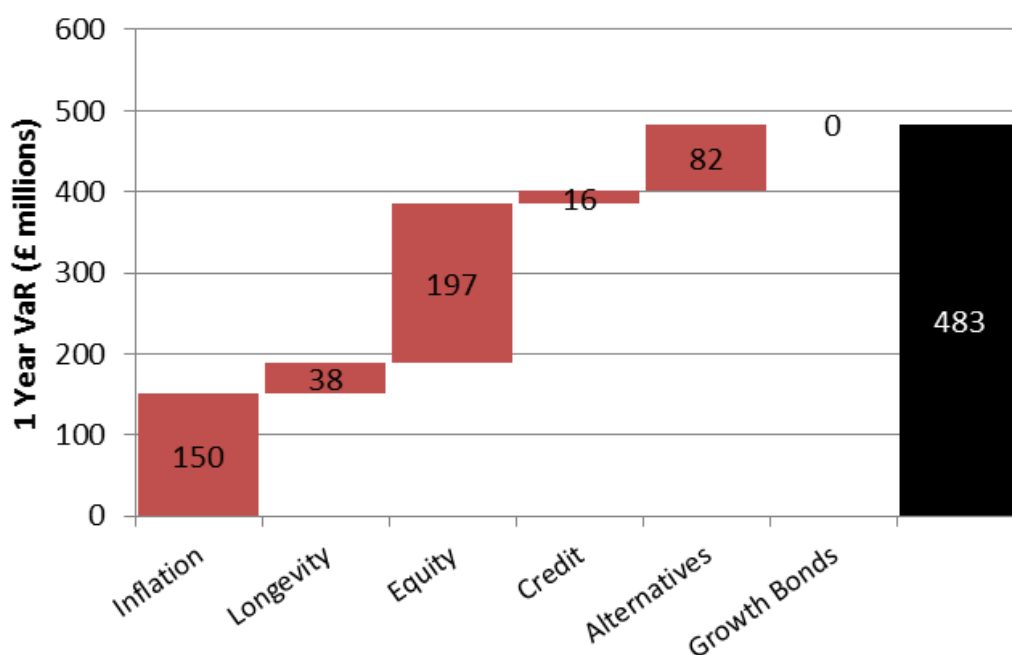
- The level of risk that the Pension Fund can tolerate in absolute terms, and in relation to its funding level and deficit
- An analysis of the order of magnitude of the various risks facing the Pension Fund is established in order that a priority order for mitigation can be determined
- The desire for diversification across asset class, region, sector, and type of security.

## 5 Risk measurement and management

The Committee assesses risks both qualitatively and quantitatively, with the starting point being the triennial strategy review. Risks are considered, understood and then prioritised accordingly.

### (a) Investment risks

The Committee uses Risk Attribution Analysis to determine the order of magnitude of the main investment risks the Pension Fund is facing. The chart below shows the VaR (Value at Risk, essentially the minimum losses that would occur in a 1-in-20 event) facing the Pension Fund, split into major risk categories.



As an additional illustration of risk, the table below shows how a range of events (in isolation) could impact the Pension Fund:

<b>Event</b>	<b>Event movement</b>	<b>Impact on Deficit</b>
Fall in equity markets	30% fall in equities	£305m
Rise in Inflation	1% increase in inflation	<i>To add once information available from Actuary</i>
Fall in interest rates	1% fall in interest rates	n/a
Active Manager underperformance	3% underperformance from all active managers	£78m

As shown in both the Value-at-Risk attribution chart and the table above, the most significant risk that the Pension Fund is running is in relation to equities. Whilst not immaterial the risks being run by the use of active management is far smaller.

### *Equities*

The largest risk that the Pension Fund is running is in relation to its equity holdings. Should equity market conditions deteriorate significantly this will have a negative impact on the funding level. The Pension Fund holds equities in order to provide the necessary returns to ensure that the Pension Fund remains affordable. The Committee believes that the extra returns that are expected to be generated by equities compensates the level of risk equities bring to the Pension Fund, but does believe in diversification, and looks to mitigate equity risk by investing significantly in bonds and alternatives. The Pension Fund is a long term investor but does require income over and above contributions received in order to pay pensions. A strategy is therefore being investigated that would seek income from alternative assets and bonds, rather than from equities, in order to avoid being a forced seller at a low point in the market.

### *Inflation*

The Pension Fund's liabilities are impacted by inflation both explicitly and implicitly. The Pension Fund will seek to invest in a range of assets that provide returns in excess of inflation and in some cases provide an inflation linked income, subject to a tolerable level of volatility.

### *Alternatives*

The Pension Fund has a significant amount of assets allocated to a range of alternatives; primarily via a dynamic asset allocation fund, but also through property. The level of diversification these assets provide helps to reduce the Funds reliance on returns from equities. Illiquid assets such as property can also be a valuable source of income.

### *Active Manager Risk*

Investment Managers are appointed to manage the Pension Fund's investments on its behalf. This risk is small relative to other risks; however the Pension Fund still addresses this risk. Extensive due diligence is used before managers are selected, with a number of different managers chosen to prevent concentration risk. The

investment managers are also monitored regularly by the Committee, Officers and by the Pension Fund's investment adviser.

The Pension Fund's portfolio is well diversified across asset classes, geography and asset managers. As different asset classes have varying correlations with other asset classes, the Pension Fund by investing in a range of different investments can minimise the level of risk run to a degree.

### **(b) Demographic Risks**

The Pension Fund is subject to a range of demographic risks, but with particular reference to investment strategy, the Committee is aware of the potential for the Pension Fund to mature over time as the pensioner liability increases. A mature pension fund is likely to take less investment risk over time and this is considered at each strategy review. The more mature a pension fund, the more likely it is that disinvestments would need to be made to pay benefits. The Pension Fund is not in that situation at present as income from contributions and investments are greater than benefit payments. However, this situation is monitored regularly and formally as part of the actuarial valuation and strategy review.

### **(c) Cashflow Management Risks**

The Pension Fund is becoming more mature and although it is cashflow positive after taking investment income into account, managing cashflow will become an increasingly important consideration in agreeing the investment strategy. Should this position change and cash outflows exceed cash inflows, mitigating actions would be taken such as investing in assets which produce cashflows.

### **(d) Governance Risks**

The Pension Fund believes that there is a benefit to the Pension Fund to be gained from good governance in the form of either or both of an increased return and/or decreased risk. Poor governance could lead to opportunities and risks being missed, and have a detrimental effect on the funding level and deficit.

### **(e) Environmental, Social and Governance ('ESG') Risks**

The Committee believes that ESG risks should be taken into account on an ongoing basis and are an integral part of the Pension Fund's strategy and objective of being a long term investor.

The Committee believes that engagement is key in relation to strong corporate governance, which in turn will enhance returns. Details of the Pension Fund's policies can be found later in this statement.

## **6 Approach to asset pooling**

In order to satisfy the requirements of the Local Government Pension Scheme: Investment Reform and Guidance issued by the Department for Communities and Local Government (DCLG) in November 2015, the Administering Authority has elected to become a shareholder in Border to Coast Pensions Partnership (BCPP) Limited. BCPP Limited will



be an FCA (Financial Conduct Authority) regulated Operator and Alternative Investment Fund Manager (AIFM).

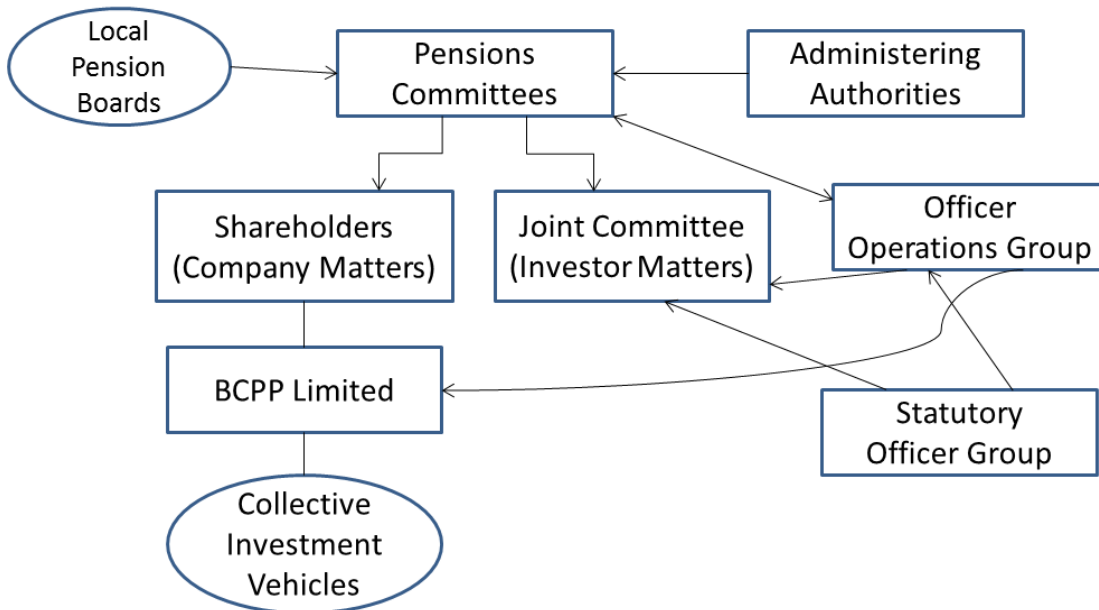
BCPP is a partnership of the administering authorities of the following Funds:

- Bedfordshire Pension Fund
- Cumbria Pension Fund
- Durham Pension Fund
- East Riding Pension Fund
- Lincolnshire Pension Fund
- North Yorkshire Pension Fund
- Northumberland Pension Fund
- South Yorkshire Pension Fund
- South Yorkshire Passenger Transport Pension Fund
- Surrey Pension Fund
- Teesside Pension Fund
- Tyne and Wear Pension Fund
- Warwickshire Pension Fund

The partner Funds submitted their proposal to Government on 15<sup>th</sup> July 2016 and have received written confirmation from the Secretary of State to confirm that the proposal meets the criteria laid down in the guidance issued in November 2015 and set out below:

- a) Asset pool(s) that achieve the benefits of scale;
- b) Strong governance and decision making;
- c) Reduced costs and excellent value for money; and
- d) An improved capacity to invest in infrastructure.

The proposed governance structure of BCPP is as follows:



## **Assets to be invested in BCPP Ltd**

The Pension Fund's intention is to invest its assets via BCPP Ltd as and when suitable sub-funds become available. An indicative timetable for participating administering authorities to invest through BCPP Ltd was set out in the July 2016 submission to Government.

The key criteria for the Pension Fund's assessment of a BCPP Ltd sub-funds will be as follows:

- that the sub-fund enables access to an appropriate investment that meets the objectives and benchmark criteria set by the Pension Fund; and
- that there is financial benefit to the Pension Fund in investing in the sub-fund offered by BCPP Ltd.

At the time of preparing this statement, the detailed parameters and objectives of the BCPP sub-fund range were not finalised.

The Pension Fund has determined that the following assets will be **held outside** of BCPP Ltd:

- any investments in closed end funds that may be made as a result of the 2017 strategy review, though new allocations to these asset classes will be made through BCPP Ltd once suitable sub-funds have been established;
- investments in pooled property funds, though new allocations to property will be made through BCPP Ltd once suitable sub-funds have been established, and existing investments will be transferred once a cost effective way of transferring is established.

Any investments in closed end funds will remain with the Pension Fund for the remaining fixed life of these investment vehicles, until all assets have been returned to the Pension Fund. There is no liquid secondary market for these types of investment and there is a risk that sales would only be possible at material discounts to net asset value. Therefore, the Committee is of the view that it is in the best interests of the Pension Fund to retain these investments.

Any assets not invested in BCPP Ltd will be reviewed at least every three years to determine whether the rationale remains appropriate, and whether it continues to demonstrate value for money. The next such review will take place no later than 2020.

## **Structure and governance of BCPP Ltd**

The July 2016 submission to Government of the proposed BCPP pooling arrangement provided a statement addressing the structure and governance of the arrangement, the mechanisms by which the Pension Fund can hold the BCPP Ltd to account and the services that will be shared or jointly procured.

At the time of preparing this statement, the terms on which the administering authority will participate in BCPP Ltd, both as an owner (via a shareholding) and as a customer (via a seat on the Joint Committee) were not finalised. As the pooling arrangement develops and the structure and governance are fully established, the Pension Fund will include this information in future iterations of the ISS.

## **7 Environmental, Social and Corporate Governance policy and policy of the exercise of rights (including voting rights) attaching to investments**

The Committee must act with the best financial interests of the beneficiaries, present and future, in mind. The Committee believes that companies should be aware of the potential risks associated with adopting practices that are socially, environmentally or ethically unacceptable. As part of the investment decision-making process, Investment Managers are required to consider such practices and assess the extent to which this will detract from company performance and returns to shareholders.

Investment Managers are required to exercise voting rights on behalf of the Pension Fund when it is in the best interests of the Pension Fund. The quarterly report from investment managers should include details of voting activity.

The Pension Fund has never sought to implement a policy that explicitly excludes certain types of investments, companies or sectors except where they are barred by UK law. The Pension Fund believes that its influence as a shareholder is better deployed by engaging with companies, in order to influence behaviour and enhance shareholder value. The Pension Fund believes that this influence would be lost through a divestment or screening approach. The Pension Fund actively engages with companies through its investment managers.

Ultimately the Pension Fund will always retain the right to disinvest from certain companies or sectors in the event that all other approaches are unsuccessful and it is determined that the investment is no longer aligned with the interests of the Pension Fund or that the issue poses a material financial risk.

The Pension Fund is committed to the principles of active asset ownership set out in the UK Stewardship Code and is developing a statement of compliance for assessment by the Financial Reporting Council.

### **Myners Principles**

Although not specifically referenced in the Regulations, the Committee feels that assessment of compliance with the Myners Principles is a valuable governance tool. A copy of the Pension Fund's Myners Compliance Statement can be found in Appendix 1.

### **Advice Taken**

In creating this statement, the Pension Fund has taken advice from its Investment Adviser. Also, in relation to each of the constituent parts, such as the asset allocation and risk mitigation, the Pension Fund has taken advice from its Investment Adviser, Mercer, and the Scheme Actuary, Aon Hewitt. In providing investment advice, Mercer is regulated by the Financial Conduct Authority.

## **Appendix 1 – Myners Principles**

This appendix sets out the extent to which Durham County Council as the Administering Authority of the Durham County Council Pension Fund complies with the six principles of investment practice set out in the document published in November 2012 by CIPFA, the Chartered Institute of Public Finance and Accountancy, and called "Principles for Investment Decision Making and Disclosure in the Local Government Pension Scheme in the United Kingdom 2012", in future, compliance with guidance given by the Secretary of State will be reported.

### **Principle 1 —Effective decision-making**

Fully compliant: Investment decisions are made by those with the skill, information and resources necessary to take them effectively. A programme covering investment issues is being developed for new members joining the Committee and training is provided to all members.

### **Principle 2 –Clear objectives**

Fully compliant: The overall investment objective for the Pension Fund is set out in the Funding Strategy Statement.

### **Principle 3 –Risk and Liabilities**

Fully compliant: The overall investment objective is considered by the Pension Fund. The risks associated with the major asset classes in which the Pension Fund's assets are invested is regularly considered. A risk register has been completed for the Pension Fund and reports from Internal and External Audit are considered by the Committee.

### **Principle 4 –Performance Assessment**

Partial compliance: Appropriate benchmarks have been set in consultation with the investment adviser and the actuary. Benchmarks are considered regularly as part of the review of the Strategic Asset Allocation. Performance against benchmarks is considered quarterly at the Committee. Investment Managers' performance is measured quarterly. Separate monitoring of Committee performance and investment adviser performance has yet to be established.

### **Principle 5 –Responsible Ownership**

Partial compliance: The Pension Fund's policy for socially responsible investing is set out in the Statement of Investment Principles and (from April 2017) the Investment Strategy Statement. Explicit written mandates agreed with all investment managers. Investment Managers are required to exercise voting rights on behalf of the Pension Fund when it is in the best interests of the Pension Fund. Normal practice is to allow the Investment Managers to follow their in-house voting policy unless otherwise instructed by the Committee. The mandates do not specifically incorporate the principle of the US Department of Labor Interpretative Bulletin on activism.

## **Principle 6 –Transparency and Reporting**

Fully compliant: The Committee acts in a transparent manner, communicating with its stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives through the publication of Committee reports and Minutes on the County Council website. The Funding Strategy Statement and the Statement of Investment Principles are also available on the internet and are included in the Pension Fund's Annual Report and Accounts. The Annual Report and Accounts includes the statutory documents that the Pension Fund is required to provide.

The Pension Fund provides regular communication to scheme members in a Newsletter and Annual Statements which are considered the most appropriate form.

## **COMMUNICATIONS POLICY STATEMENT**

Durham County Council is the administering authority for the Durham County Council Pension Fund. This Communication Policy Statement has been drawn up to comply with regulation 106B of the Local Government Pension Scheme Regulations 1997 (as amended) and to ensure the Council offers clear communication to stakeholders of the Local Government Pension Scheme.

### ***WHO WE COMMUNICATE WITH***

- Scheme members (active members, pensioners and deferred members);
- Representatives of scheme members;
- Prospective scheme members;
- Employers participating in the scheme;
- Advisers (for example actuaries, investment advisers, Local Government Pensions Committee);
- Other bodies (for example prospective employing authorities and their representatives).

### ***KEY OBJECTIVES***

- To ensure communication is clear, factual and concise;
- To ensure communication is designed and delivered in a manner appropriate to its audience;
- To ensure that the correct information reaches the right people at the right time.

## **COMMUNICATING WITH SCHEME MEMBERS**

Scheme members need access to detailed information about the scheme and their own benefits to allow them to make informed choices about their own pension benefits.

The Council provides:

- **Scheme literature**  
The pension section produces a summary guide to benefits in the scheme along with specific guides for certain circumstances, such as how divorce can affect scheme benefits or on the internal dispute resolution procedure.
- **Annual benefit statements**  
All active members are sent a benefit statement each year setting out the benefits they have earned in the scheme up to 31 March that year.  
  
All deferred members are sent a benefit statement each year setting out the current value of their deferred benefits payable at the earliest date on or after age 60 that unreduced benefits can be paid to them. The statement also sets out the effect of pension increases on their benefits since they left service.
- **Newsletters**  
All active members and pensioners are sent a copy of each issue of the relevant newsletter.

- Telephone helpline  
All newsletters contain contact telephone numbers for general enquiries. Active members, pensioners and deferred members can contact the Pension Administration Team by telephone between 8:30am and 4:30pm on weekdays. The newsletters also contain the email address where general enquiries can be submitted.

## **COMMUNICATING WITH EMPLOYERS PARTICIPATING IN THE SCHEME**

Employers need to be kept up to date with developments in the scheme and need to be informed of consultation exercises that could influence the future of the scheme.

Employers are sent written information on scheme developments as and when changes are proposed to the scheme. Employers are often sent copies of circulars provided by the Employers' Organisation or are directed to copies of these circulars via web-links.

Meetings with individual employers are arranged as necessary or as requested to deal with any significant pension issues that arise. Support is provided to employers who want to provide further pension information to their employees - this includes pre-retirement seminars and mid-life seminars.

All employers are invited to attend the Annual Meeting of the Pension Fund Committee. Copies of the annual report and accounts for the Pension Fund are distributed at this meeting and are also sent to all employers in the scheme.

## **COMMUNICATING WITH PROSPECTIVE MEMBERS**

The Pension Administration Team issues pension packs to prospective members. These contain a summary of the benefits of scheme membership, information comparing the scheme with other pension options, a nomination form, an opt-out form and an authorisation form for investigating potential pension transfers into the scheme.

## **COMMUNICATING WITH REPRESENTATIVES OF SCHEME MEMBERS**

The Pension Administration Team produces a summary guide to benefits in the scheme along with specific guides for certain circumstances, such as how divorce can affect scheme benefits or on the internal dispute resolution procedure. This information is available to representatives of scheme members.

The Pension Administration Team telephone helpline is also available between 8:30am and 4:30pm on weekdays for any queries representatives of scheme members may have.

The main local government unions are represented on the Pension Fund Committee. This means they are sent agenda items and minutes from the meetings as well as being able to attend the meetings (albeit in a non-voting capacity).

**FUND PUBLICATIONS**

<b>COMMUNICATION DOCUMENT</b>	<b>AVAILABLE TO</b>	<b>WHEN PUBLISHED</b>
Starter Packs	Prospective members	When required
Summary scheme guide	Prospective members Active members	When required
Newsletter: Pensions News	Active members	When required
Annual benefit statement	Active members Deferred members	Once per year
Newsletter: Years Ahead	Pensioners	When required
Payslips	Pensioners	Once a year or upon a change to net pension of more than £5
P60s	Pensioners	Once per year
Pension Increase Information	Pensioners	Once per year
Update letter on changes to regulations and other issues	Employers	When required
Valuation report	Employers	Every three years
Report and accounts	All stakeholders	Once per year – distributed to all employers and available on the DCC website and on request to all



## PARTICIPATING BODIES AND CONTRIBUTION RATES

The contribution rates of participating bodies for 2016/17, as set by the Fund's actuary, are shown below, expressed as a percentage of employees' pensionable pay and an additional annual payment where applicable:

Employer	Employer Contributions		Employer	Employer Contributions	
	% of pensionable pay	Additional Annual Payment (£)		% of pensionable pay	Additional Annual Payment (£)
Apollo Studio Academy	17.20%		Lin Housing Limited	8.50%	
Barnard Castle School	23.10%	73,900	Longfield Academy Trust	13.10%	51,600
Barnard Castle Town Council	18.70%		Making Space	13.60%	
Bishop Auckland College	13.20%	18,400	Mears Limited	0.00%	
Bishop Auckland Town Council	18.70%		Mellors Catering Services Limited	13.10%	
Blackwell Grange Golf Club Ltd	13.60%		MITIE Cleaning Limited	29.70%	
Bowes Museum	0.00%		MITIE PFI Limited	29.90%	
BRandH Academy Limited	12.90%	1,800	Monk Hesledon Parish Council	18.70%	
Brandon & Byshottles Parish Council	18.70%		Morrison Facility Services Limited	0.00%	
Bulloughs	21.40%		Murton Parish Council	18.70%	
Carillion (AMBS) Limited	13.40%		Murton Welfare Association	20.40%	
Carillion Services Limited	21.50%		New College Durham	13.10%	202,000
Carmel Education Trust	13.90%	26,900	New College Durham Academies Trust	13.40%	67,300
Catering Academy Limited	13.20%		New Seaham Academy	18.60%	4,700
Central Durham Joint Crematoria	18.70%		North East Council of Addiction	0.00%	
Cestria Community Housing	12.70%		North Lodge Parish Council	18.70%	
Chilton Town Council	18.70%		Orion Solutions	25.50%	
Churchill Contract Services Limited	18.70%		Park View Community School	11.40%	32,800
Cleves Cross Primary School	17.00%	27,300	Parkside Academy	15.20%	36,800
Co Durham & Darlington Fire & Rescue	13.10%	93,800	Peterlee Town Council	18.70%	
Compass Contract Services Ltd	20.10%		Queen Elizabeth Sixth Form College	15.60%	
County Durham Housing Group	13.80%		Reid Street Primary School	16.40%	10,600
Creative Management	13.80%		Ribbon Academy Trust	13.10%	34,800
Dale & Valley Homes Limited	13.80%	45,200	Seaham Town Council	18.70%	
Darlington Borough Council	13.60%	1,992,000	Sedgefield Town Council	18.70%	
Darlington College	13.60%	66,000	Shildon Town Council	18.70%	
Derwentside College	13.60%	97,100	Shotton Hall Academy Trust	11.40%	35,600
Derwentside Homes	14.40%		Shotton Parish Council	18.70%	
Durham City Homes	13.80%		South Hetton Parish Council	18.70%	
Durham County Council	13.80%	22,515,000	Spennymoor Town Council	18.70%	
Durham Police & Crime Commissioner	11.80%	773,000	St Aidan's CE Academy	13.60%	57,700
Easington Academy	13.70%	22,300	St Bede's Catholic School & Sixth Form College	13.40%	51,000
Easington Colliery Parish Council	18.70%		St Bede's RC Primary School	13.20%	3,600
Easington Village Parish Council	18.70%		St George's CE Academy	16.70%	4,300
East Durham College	11.90%	26,000	St John's Catholic School & Sixth Form College	13.50%	34,200
East Durham Homes Limited	13.80%	445,000	St John's CE Primary School	12.60%	1,500
Education Village	12.80%	43,500	Staindrop School	15.00%	27,500
Federation of Mowden Schools Academy Trust	10.80%	3,800	Stanley Town Council	18.70%	
Ferryhill Town Council	18.70%		Taylor Shaw Longfield	20.20%	
Firthmoor Primary School	14.90%	9,100	Taylor Shaw Primary	14.70%	
Fishburn Parish Council	18.70%		Teesdale Housing Association	23.00%	3,300
Framwellgate Moor Parish Council	18.70%		Teesdale School	14.30%	18,600
Future Leisure in Coxhoe	7.00%		The Excel Academy Partnership	12.40%	21,900
Great Aycliffe Town Council	18.70%		The Federation of Abbey Schools Academy Trust	13.20%	7,000
Greater Willington Town Council	18.70%		The Forge	12.20%	
Harbour Support Services	13.80%		The Hermitage Academy	13.30%	30,300
Heathfield Academy Trust	15.80%	19,500	Thornley Parish Council	18.70%	
Hopewood Academy	10.50%	36,800	Three Rivers Housing	22.90%	
Horden Parish Council	18.70%		Trimdon Foundry Parish Council	18.70%	
Hummersknott Academy Trust	13.70%	46,300	Trimdon Parish Council	18.70%	
Hurworth Primary School	13.50%	5,400	Tudhoe Learning Trust	12.50%	46,500
Hurworth School Limited	12.40%	9,800	Wates Construction Limited	18.80%	
Hutton Henry Parish Council	18.70%		West Park Academy	12.70%	6,900
Investing in Children CIC	13.80%		Wheatley Hill Parish Council	18.70%	
IT Systems & EVAT Partnership	12.80%		Wingate Parish Council	18.70%	
KGB Cleaning & Support Services	0.00%		Woodham Academy	14.30%	37,100
King James I Academy	14.00%	34,600	Wyvern Academy	13.10%	
Lanchester Parish Council	18.70%				
Leisureworks	12.80%	4,600			

## MEMBERSHIP STATISTICS

The following table provides details of the number of pensionable employees in the scheme and the number of pensioners.

	Number of Pensionable employees		Number of Pensioners	
	at 31/3/16	at 31/3/17	at 31/3/16	at 31/3/17
<b>Scheduled Bodies</b>				
Apollo Studio Academy	5	5	0	0
Bishop Auckland College	150	151	66	72
BRandH Academy	32	36	3	3
Carmel College	89	91	4	7
Central Durham Joint Crematoria Cttee	3	3	8	8
Co Durham & Darlington Fire & Rescue	99	88	48	56
Cleves Cross Primary	36	42	1	1
Darlington Borough Council	1,720	1,615	1,774	1,860
Darlington College	181	177	122	125
Derwentside College	111	106	90	93
Durham County Council	11,657	11,685	13,857	14,050
Durham Police & Crime Commissioner	917	901	393	420
Easington Academy	44	0	2	0
East Durham College	221	228	93	101
Education Village	122	124	10	11
Firthmoor Primary	17	20	0	1
Hopewood Academy	49	54	1	0
Hummersknott Academy Trust	111	110	9	13
Hurworth Primary	3	5	1	1
Hurworth School Limited	37	43	1	1
Investing in Children	4	4	2	2
IT Systems & EVAT Partnerships	6	6	1	1
King James 1 Academy	51	51	9	9
Lingfield Education Trust	80	84	0	1
Longfield Academy Trust	139	114	12	10
Marchbank Academy	10	8	0	0
New College Durham	360	352	152	159
New College Durham Academies Trust	71	67	14	15
New Seaham Primary	8	8	0	1
North East Learning Trust	0	123	0	8
Parish Councils	56	58	37	42
Park View Academy	44	48	6	6
Parkside Sports College	30	33	9	9
Polam Hall School	47	53	0	0
Queen Elizabeth 6th Form College	62	67	18	20
Reid Street Primary School	22	24	3	4
Ribbon Academy Trust	54	58	2	3
St Aidan's Academy	26	21	8	10
St Augustine's	14	15	1	1
St Bede's Academy	48	50	3	4
St Bede's RC Primary	14	17	2	2
St George CE Academy	22	25	3	2
St John's Catholic School & Sixth Form College	64	60	4	8
St John's CE Primary School	15	16	0	0
Staindrop School	27	23	5	7
Teesdale Education Trust	30	0	4	0
The Academy at Shotton Hall	48	0	1	0
The Dove Academy Trust	0	35	0	0

	Number of Pensionable employees		Number of Pensioners	
	at 31/3/16	at 31/3/17	at 31/3/16	at 31/3/17
The Durham Martyrs Multi Academy Trust	0	34	0	1
The Excel Academy Partnership	35	44	5	5
The Fed of Abbey Schools Academy Trust	52	56	2	2
The Fed of Mowden Schools	21	23	0	1
The Hermitage Academy Trust	64	67	4	6
Town Councils	144	159	116	123
Tudhoe Learning Trust	91	144	4	4
UTC South Durham	0	10	0	0
West Park Academy	43	46	1	1
Woodham College	40	42	3	3
Wyvern Academy	0	33	0	4
<b>Admission Bodies</b>				
Barnard Castle School	37	34	33	34
Blackwell Grange Golf Club	1	2	0	0
Bowes Museum	5	5	12	13
Bulloughs	8	8	0	1
Carillion	11	10	3	3
Catering Academy Ltd.	2	2	0	0
Cestria	130	133	31	40
Churchill Services Ltd.	2	1	0	0
Compass Group UK	2	2	5	5
County Durham Housing Group	141	148	6	1
Creative Management	2	1	1	1
Dale and Valley Homes	59	48	12	18
Derwentside Homes	158	188	98	99
Durham City Homes	73	74	3	5
East Durham Homes	116	101	85	96
F.L.I.C.	4	3	0	0
Harbour Support Services	2	2	0	0
Keepmoat	15	4	8	15
Leisureworks	18	14	22	24
Livin	118	124	36	37
Making Space	26	23	2	5
Mears	49	42	42	46
Mellors Catering Services	3	3	0	0
Mitie Cleaning	1	1	1	1
Mitie PFI	1	1	2	2
Morrison's	56	53	19	22
Murton Welfare Association	3	3	0	0
N.E.C.A	3	3	1	1
Orian Solutions	2	2	0	1
Taylor Shaw	29	28	9	12
Teesdale Housing	4	4	4	4
The Forge	2	1	0	0
Three Rivers Housing	1	0	0	0
Wates Construction Ltd	0	0	2	1
<b>Former employers</b>	0	0	364	355
<b>Totals</b>	<b>18,530</b>	<b>18,630</b>	<b>17,715</b>	<b>18,139</b>

## **GLOSSARY OF TERMS**

### **Accounting Period**

The period of time covered by the Statement of Accounts, normally 12 months starting on 1 April. The end of the period is the Balance Sheet/ Net Assets Statement date.

### **Accounting Policies**

The principles, conventions, rules and practices applied that specify how transactions and other events should be reflected in the financial statements.

### **Accounting Standards**

Accounting standards are authoritative statements of how particular types of transactions and other events should be reflected in financial statements and accordingly compliance with accounting standards will normally be necessary for financial statements to give a true and fair view.

### **Accruals**

The concept that income, and expenditure are recognised as they are earned or incurred, not as money is received or paid.

### **Actuary**

An actuary is an expert on pension scheme assets and liabilities. Every three years, the Actuary for the Local Government Pension Scheme determines the rate of employer contributions due to be paid to the Pension Fund.

### **Actuarial Basis**

The technique applied when estimating the liabilities to be recognised for defined benefit pension schemes in the financial statements.

### **Actuarial Gains**

These may arise on a defined benefit pension scheme's liabilities and assets. A gain represents a positive difference between the actuarial assumptions and actual experience (e.g. liabilities during the period were lower than estimated).

### **Actuarial Losses**

These may arise on a defined benefit pension scheme's liabilities and assets. A loss represents a negative difference between the actuarial assumptions and actual experience (e.g. liabilities during the period were higher than estimated).

### **Added Years**

Additional years of service awarded discretionally to increase the benefits to employees taking early retirement.

### **Additional Voluntary Contributions (AVCs)**

An option available to individuals to secure additional pension benefits by making regular payments in addition to the contributions payable to the Pension Fund on basic earnings.

### **Admitted Bodies**

Organisations that take part in the Local Government Pension Scheme with the agreement of the Pension Fund. Examples of such bodies are companies providing services that were once provided by local authorities in the Pension Fund.

### **Annual Governance Statement**

The statement gives assurance that appropriate mechanisms are in place to direct and control the activities of the County Council.

### **Amortisation**

Amortisation is the equivalent of depreciation for intangible assets.

### **Apportionment**

A way of sharing costs using an appropriate method, e.g. floor area for an accommodation-related service.

### **Appropriation**

The transfer of sums to and from reserves, provisions, and balances.

**Asset Allocation**

The distribution of the Fund's assets between asset classes and/ or world markets.

**Audit of Accounts**

An independent examination of the Pension Fund's financial affairs.

**Balanced Management**

A type of multi-asset management where a manager is responsible for all asset classes. A fund using this style is a "balanced" fund.

**Benchmark**

A yardstick against which the investment policy or performance of a fund manager can be compared.

**Bonds**

A type of investment in certificates of debt issued by the government of a company. These certificates represent loans which are repayable at a future specified date with interest.

**BPS (Basis points)**

One basis point is a unit equal to one hundredth of a percentage point.

**Chartered Institute of Public Finance and Accountancy (CIPFA)**

The principal accountancy body dealing with local government finance.

**Code**

The Code of Practice on Local Authority Accounting. A publication produced by CIPFA constituting proper accounting practice for Local Authorities.

**Contingent Asset**

Potential benefits that the Pension Fund may reap in the future due to an event that has happened in the past.

**Contingent Liabilities**

Potential costs that the Pension Fund may incur in the future due to something that has happened in the past.

**Corporate Governance**

The promotion of corporate fairness, transparency and accountability. The structure specifies the responsibilities of all stakeholders involved and the rules and procedures for making decisions.

**Creditors**

Persons or bodies to whom sums are owed by the Pension Fund.

**Custody**

Safe-keeping of securities by a financial institution. The Custodian keeps a record of client investments and may also collect income, manage cash, process tax claims and provide other services according to client instructions.

**Debtors**

Persons or bodies who owe sums to the Pension Fund.

**Deferred Pension**

The inflation-linked retirement benefits payable from normal retirement age to a member of the Fund who has ceased to contribute as a result of leaving employment or opting out of the pension scheme before normal retirement age.

**Defined Benefit Scheme**

Defined benefit pension schemes prescribe the amounts members will receive as a pension regardless of contributions and investment performance. Employers are obliged to fund any shortfalls.

**Depreciation**

The fall in the value of an asset, as recorded in the financial records, due to wear and tear, age and obsolescence.

**Derivative**

Contracts that derive their value from an underlying financial asset. Often used as a hedge against changes in value.

**Dividend**

Part of a company's after tax earnings, distributed to shareholders in the form of cash or shares.

**Equities**

Ordinary shares in UK and overseas companies traded on a stock exchange. Shareholders have an interest in the profits of the company and are entitled to vote at shareholder's meetings.

**Fair Value**

The value for which an asset can be exchanged or a liability can be settled in a market related transaction.

**Financial Instrument**

A contract that gives rise to a financial asset in one entity and a financial liability, or equity instrument, in another.

**Fitch**

Fitch Ratings is a rating agency providing credit ratings research and risk analysis of financial institutions across the world. Credit ratings are used by investors as indications of the likelihood of receiving the money owed to them in accordance with the terms on which they invested.

**Fixed Interest Securities**

Investments in government (in the main) and company stocks which guarantee a fixed rate of interest. The securities represent loans that are repayable at a future date but which can be traded on a recognised stock exchange before the repayment date.

**FIDs and Manninen**

A claim has been lodged for Durham County Council Pension Fund and other Pension Funds for repayment of tax credits overpaid on Foreign Income Dividends (FIDs) and other dividends, referred to by name of the person whose case set the precedent, Manninen.

**Futures**

A contract made to purchase or sell an asset at an agreed price on a specified future date.

**GAAP**

Generally Accepted Accounting Practice.

**Gilts**

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

**Impairment**

Impairment of an asset is caused either by a consumption of economic benefits e.g. physical or deterioration in the quality of the service provided by the asset. A general fall in prices of a particular asset or type of asset is treated as a revaluation.

**Index Linked Securities**

Investments in government stock that guarantee a rate of interest linked to the rate of inflation. These securities represent loans to government which can be traded on recognised stock exchanges.

**Investment**

An asset which is purchased with a view to making money by providing income, capital appreciation, or both.

**Investment Properties**

Interest in land and/or buildings in respect of which construction work and development have been completed and which are held for their investment potential rather than for operational purposes, any rental income being negotiated at arms length.

**Investment Strategy Statement (ISS)**

The ISS details the policy which controls how a pension fund invests.

**LAAP Bulletin**

CIPFA's Local Authority Accounting Panel (LAAP) periodically issues bulletins to local authority practitioners, providing guidance on topical issues and accounting developments and, when appropriate, clarification on the detailed accounting requirements.

**Liabilities**

An obligation to transfer economic benefits. Current liabilities are usually payable within one year.

**Managed Fund**

A type of investment where a number of investors pool their money into a fund, which is managed by a professional fund manager.

**Market Value**

The monetary value of an asset as determined by current market conditions.

**Materiality**

An expression of the relative significance of a particular issue in the context of the organisation as a whole.

**Mid-market price**

The mid-point between the bid price and the offer price for a security based on quotations for transactions of normal market size by recognised market-makers or recognised trading exchanges.

**Minority Interest**

The interest in a subsidiary entity that is attributable to the share held by, or on behalf of persons other than the reporting authority.

**Moody's**

Moody's Investor Service is a rating agency, providing credit ratings, research, and risk analysis of financial institutions across the world. Credit ratings are used by investors as indications of the likelihood of receiving the money owed to them in accordance with the terms on which they invested.

**Myners' Principles**

A set of principles issued by Government which Pension Schemes are required to consider and to which they must publish their degree of compliance.

**Net Realisable Value**

The expected sale price of stock in the condition in which it is expected to be sold. This may be less than cost due to deterioration, obsolescence or changes in demand.

**Non Current Assets**

Tangible or intangible assets that yield benefits to the authority and the services it provides for a period of more than one year. Tangible assets have physical substance, for example land, buildings and vehicles. Intangible assets do not have physical substance but are identifiable and controlled by the authority through custody or legal rights, for example software licences.

**Passive Management**

A style of management that seeks to achieve performance equal to market or index returns.

**Pooled Fund**

A pooled fund pools investors' money and invests in a portfolio of shares, bonds and cash.

**Portfolio**

A number of different assets considered and managed as a whole by an investment manager, to an agreed performance specification.

**Prior Period Adjustment**

Those material adjustments relating to prior years' accounts, that are reported in subsequent years arising from changes in accounting policies or from the correction of fundamental errors. They do not include minor corrections or adjustments of accounting estimates made in prior years.

### **Provisions**

Provisions represent sums set aside to meet any specific future liabilities or losses arising from contractual obligations or as a result of past events. These events are likely or certain to be incurred and a reliable estimate can be made of the amount of the obligation.

### **Prudential Code**

The Government removed capital controls on borrowing and credit arrangements with effect from 1st April 2004 and replaced them with a Prudential Code under which each local authority determines its own affordable level of borrowing. The Prudential Code requires authorities to set specific prudential indicators on an annual basis.

### **Public Works Loans Board (PWLB)**

A government agency providing long and short-term loans to local authorities at interest rates only slightly higher than those at which Government itself can borrow.

### **Return**

The total gain from holding an investment over a period, including income, and increase or decrease in market value.

### **Risk**

Risk is the variability of returns. Investments with a greater risk usually promise higher investment returns.

### **Scheduled Bodies**

County and Borough Councils and other similar bodies whose staff automatically qualify to become members of the Pension Fund.

### **Section 151 Officer**

The officer designated under Section 151 of the Local Government Act 1972 to have overall responsibility for the administration of the financial affairs of the County Council and the preparation of the County Council's Statement of Accounts.

### **Statements of Recommended Accounting Practice (SORP)**

A publication produced by CIPFA, recognised by the Accounting Standards Board (ASB), that provides comprehensive guidance on the content of the County Council's Statement of Accounts.

### **Transfer Values**

Amounts paid to or received from other local and public authorities, private occupational or personal pension schemes in respect of pension rights already accumulated by employees transferring from or to the participating authorities.

### **Treasury Management Policy and Strategy**

A plan outlining the approach to treasury management activities. This includes setting borrowing and investment limits to be followed for the following year and is published annually in the Medium Term Financial Plan document.

### **Unit Trusts**

A unit trust is a pooled fund in which small investors can buy and sell units. The pooled fund purchases investments and the returns are passed on to the unit holders. It enables a broader spread of investments than investors could achieve individually.



## CONTACTS FOR FURTHER INFORMATION

**For further information on issues relating to the Pension Fund, please contact the Corporate Director Resources.**

*Telephone*            03000 260 000

*E-mail*                HELP@DURHAM.GOV.UK

or you can write to:

Corporate Director Resources  
Durham County Council  
County Hall  
DURHAM  
DH1 5UE

or visit Durham County Council's website at [durham.gov.uk](http://durham.gov.uk)