AGENDA ITEM 3 (a)
DRAFT

FALKIRK COUNCIL

MINUTE of MEETING of the PENSIONS COMMITTEE held in the MUNICIPAL BUILDINGS, FALKIRK on THURSDAY 5 JUNE 2014 at 9.30 A.M.

PRESENT:	Councillors Jim Blackwood Colin Campbell Steven Carleschi Tom Coleman Depute Provost Patrick (Convener) Mary Keggan Alistair Redpath
ATTENDING:	Alastair McGirr, Pensions Manager Bryan Smail, Chief Finance Officer Brian Pirie, Democratic Services Manager, Committee Services Officer
ALSO IN ATTENDANCE:	Bruce Miller, Investment Manager, Lothian Pension Fund Stephen Docherty, Victoria MacLean and Natalie Winterfrost, Aberdeen Asset Management Roger Pim, SL Capital Partners

PE1. APOLOGIES

An apology was intimated on behalf of Councillor C Martin, Falkirk Council.

PE2. DECLARATIONS OF INTEREST

No declarations were made.

PE3. MINUTES

Decision

(a) The minute of the meeting of the Pensions Committee held on 6 March 2014 was approved;

(b) The minute of the meeting of the Pensions Committee held on 17 March 2014 was approved; and

(c) The minute of the meeting of the Pensions Panel held on 29 May 2014 was noted.

PE4. LOCAL GOVERNMENT PENSION SCHEME - 2015 UPDATE

The Committee considered a report by the Chief Finance Officer providing an update on the ongoing work as part of the reform of the Local Government Pension Scheme (LGPS).

The report summarised the current position in regard to the development of enabling legislation and advised that, following, the development of a Heads of Agreement on scheme design, a Heads of Agreement on Governance was being developed. In terms of Governance arrangements, no agreement had been reached in regard to the relationship between the proposed Pensions Committees and Boards and discussions were ongoing between employers and Unions.

The report then summarised developments in England and Wales; in particular the findings of a report by Hymans Robertson on behalf of the Department of Communities and Local Government on the future structure of the LGPS. The report had concluded that significant savings could be achieved if Funds invested collectively, made greater use of passive management and moved away from all "Fund of Fund" structures.

Decision

The Committee noted report.

PE5. PENSION FUND - GENERAL GOVERNANCE MATTERS

The Committee considered a report by the Chief Finance Officer presenting an update on various matters associated with the governance of the Falkirk Council Pension Fund. The areas covered within the report included:-

- The impact of the UK Government's budget on defined contribution Pension Schemes;
- New powers from HM Revenue to investigate pension liberation fraud;
- The implications of the Pensions Act 2014
- The risk arising from falling asset values and of the decision by Clackmannanshire Council to cut the pay of its employees; and
- The role of the Local Authority Pension Fund forum and its research and engagement partner PIRC.

Decision

The Committee noted the report and agreed to update the risk register to reflect the adverse impact of rising interest rates on asset values but the potentially beneficial effect of rising rates on fund liabilities.

PE6. INVESTMENT IN SOCIAL/AFFORDABLE HOUSING

The Committee considered a report by the Chief Finance Officer providing an update on its decision to invest in social housing and in affordable housing.

The Committee agreed on 17th March 2014 (ref PE99) to appoint Hearthstone plc to manage a £30m investment in social housing and affordable housing, with equal investments in each sector. The report provided further information on the investment process, with £30m being invested in Hearthstone plc's Housing Fund for Scotland and made available to Castle Rock Edinvar (CRE), Hearthstone's strategic partner in the venture. It was proposed that investment in social housing would be delivered by means of a loan to CRE while the investment in affordable housing will be through the purchase of newly built properties.

Decision

The Committee noted the report.

PE7. FUND MANAGER PERFORMANCE REVIEW

The Committee considered a report by the Chief Finance Officer reviewing the overall performance of the Fund and of the undernoted Fund Managers:-

- Aberdeen Asset Management;
- Baillie Gifford Bonds;
- Baillie Gifford Diversified Growth;
- Legal and General;
- Newton Investment Management;
- Schroder Investment Management UK Equities; and
- Schroder Investment Management Property.

Decision

The Committee noted the Fund Managers' performance and the action taken by them during the quarter to 31 March 2014, in accordance with their investment policies.

PE8. PRIVATE EQUITY AND ALTERNATIVES UPDATE

The Committee considered a report by the Chief Finance Officer on the progress of the Pension Fund's private equity and alternatives programme arising from the Investments Programme of SL Capital (Standard Life), Wilshire Associates, Grosvenor Capital and M&G for the quarter ending 31 March 2014.

In considering the various reports the Committee was invited to consider committing to a new infrastructure fund being launched by Grosvenor CM (and, if so, the amount to be committed).

Decision

The Committee agreed to delay its decision in regard to the Grosvenor CM option until it had considered the report on Investment in UK/Scottish Infrastructure later in the agenda.

PE9. ORDER OF BUSINESS

In terms of Standing Order 14.2(i), Depute Provost Patrick advised of a variation to the order of business from that detailed on the agenda for the meeting. The following items have been recorded in the order that they were taken.

PE10. EXCLUSION OF PUBLIC

RESOLVED in terms of Section 50A(4) of the Local Government (Scotland) Act 1973, to exclude from the meeting the press and public for the following item of business on the ground that it would involve the likely disclosure of exempt information as defined in Paragraph 9 of Part 1 of Schedule 7A to the said Act.

PE11. INVESTMENT IN UK/SCOTTISH INFRASTRUCTURE

The Committee considered a report by the Chief Finance Officer setting out the details of a potential investment in UK and Scottish infrastructure.

The Committee and panel had previously considered investing in UK/Scottish infrastructure and had, in December 2013 (ref PE), requested further information on a proposal from the Lothian Pension Fund that it and the Fund collaborate.

The report set out the proposal by Lothian Pension Fund together with an appraisal by Hymans Robertson.

The report highlighted issues, and in particular:-

- the pace of deployment of capital;
- the strong likelihood of investments being made from the PFI/PPP universe;
- the timing of deals which means that in practical terms the investment decision; and requires to be delegated to the Chief Finance Officer.

Bruce Miller left the meeting during consideration of this item.

Decision

The Committee agreed to:-

(1) collaborate with Lothian Pension Fund in making infrastructure investments in the UK to the value of £30m;

(2) **delegate the investment decision to the Chief Finance Officer; and**

(3) **request that the Chief Finance Officer reports on investments made in relation to this mandate.**

Bruce Miller rejoined the meeting at this point.

PE12. PRIVATE EQUITY AND ALTERNATIVES UPDATE (continued)

Decision

The Committee agreed not to commit to the new infrastructure fund being launched by Grosvenor CM.

PE13. FUND MANAGER REVIEW

The Committee heard a presentation by Stephen Docherty, Victoria MacLean and Natalie Winterfrost of Aberdeen Assets Management.

The presentation covered:-

- The management team's equity approach;
- Investment process;
- Fund valuation and diversity;
- Fund performance.

The Convenor thanked Mr Docherty, Miss MacLean and Miss Winterfrost for their comprehensive presentation.

Decision

The Committee noted the presentation.

PE14. FUND MANAGER REVIEW

The Committee heard a presentation by Rodger Pim of SL Capital Partners.

The presentation covered:-

- The background to SL Capital Partners and its structure;
- SL Capital's platform and one team approach;
- Overview of Falkirk Council's commitments with SL Capital Partners.

The Convenor thanked Mr Pim for his detailed presentation.

Decision

The Committee noted the presentation.

AGENDA ITEM 3 (b)
DRAFT

FALKIRK COUNCIL

MINUTE OF MEETING OF THE PENSIONS PANEL
THURSDAY 11 SEPTEMBER 2014 AT 2.00 P.M.
MUNICIPAL BUILDINGS, FALKIRK

PRESENT:- **Officers – Falkirk Council**

Jason Koumides, Pensions Accountant
Alastair McGirr, Pensions Manager
Antonia Sobieraj, Committee Services Officer

Organisations

Andrew Douglas, Unison
Councillor Archie Drummond, Clackmannanshire Council
Sandy Harrower, UCATT
Gordon Laidlaw, Scottish Autism
Ed Morrison, Scottish Children's Reporter Administration's (SCRA)
Susan MacKay, Clackmannanshire Council
Ian McLean, Pensioner Representative
Alistair Redpath, Pensioner Representative
Alison Stewart, Head of Finance, Forth Valley College.
William Watson, Stirling Council
Jennifer Welsh, SEPA (Convener)

Attending

Patrick Hand and Jamie Cumming, Aberdeen Asset Management (for agenda item 12) (minute item 12)
Catherine McFadyen, Hyman's Robertson (for agenda item 5) (minute item 6)
Allan MacDougall and Janice Hayward, PIRC Ltd (for agenda item 9) (minute item 10)
Bruce Miller, Investment Manager, Lothian Pension Fund

1. CONVENERSHIP OF MEETING

In terms of Standing Order 12.1, the Clerk presided at the start of the meeting in the absence of the Convener and invited a member of the Panel to take the Chair for the duration of the meeting. Jennifer Welsh, SEPA thereafter took the Chair with the consent of members present.

2. APOLOGIES

Apologies were intimated on behalf of Bryan Smail, Chief Finance Officer, Falkirk Council.

3. DECLARATIONS OF INTEREST

No declarations were made.

4. MINUTES

Decision

(a) The minute of the meeting of the Pensions Panel held on 29 May 2014 was approved; and

(b) The minute of the meeting of the Pensions Committee held on 5 June 2014 was noted.

5. PENSION FUND - UNAUDITED ANNUAL REPORT AND ACCOUNTS 2013/14

The Panel considered a report by the Chief Finance Officer on the Falkirk Pension Fund's Unaudited Annual Report and Accounts for 2013/2014 and (a) referring to Regulation 31A of the Local Government Pension Scheme (Administration)(Scotland) Regulations 2008, which requires administering authorities to publish a pension fund annual report, recognising that pension fund accounts are separate from other accounts of the administering authority, and (b) attaching as an appendix for inspection, a copy of the Fund's Unaudited Annual Report and Accounts for 2013/14.

Decision

The Panel noted the report and the publication of the Unaudited Falkirk Council Pension Fund Annual Report and Accounts for 2013/14.

6. LONGEVITY ANALYSIS REPORT - CLUB VITA - UPDATE BY HYMANS ROBERTSON

The Panel considered a report by the Chief Finance Officer on the initial findings of the Pension Fund's participation in the Club Vita longevity analysis.

The Committee had agreed at its meeting on 12 December 2013 to the proposal from Hymans Robertson for the Fund to participate in Club Vita. This would enable a detailed analysis of the Fund's longevity experience to be undertaken and allowed for the use of data which was specific to the Falkirk Pension Fund. The availability of the more accurate longevity data meant that Fund calculations, such as cessation valuations, bulk transfers and funding assessments would in future be of a more reliable nature. Other benefits included having robust evidence based longevity assumptions allowing the Fund to pay due attention to longevity risk

The Panel also heard from Catherine McFadyen, Hyman's Robertson who provided detail on the following:-

- The longevity risk including addressee and scope;
- The longevity, affluence, lifestyle, retirement health and occupational 'DNA' data;
- The concentration of longevity risk;
- The implications for funding; and
- The future longevity uncertainty.

The Convener thanked Ms McFadyen for her comprehensive presentation.

Decision

The Panel noted the report and presentation.

7. LOCAL GOVERNMENT PENSION SCHEME - NEW SCHEME DEVELOPMENTS

The Panel considered a report by the Chief Finance Officer providing an update on the recent developments in relation to the ongoing reform of the Local Government Pension Scheme (LGPS) through the Public Service Pensions Act 2013 with effect from 1 April 2015.

The report detailed that a Heads of Agreement on scheme design and governance had now been reached between COSLA, Trades Unions and the Scottish Government.

The statutory arrangements requiring to be set in place were as undernoted:-

- The main scheme regulations were made and described how benefits and contributions would be determined under the CARE arrangements. A number of defects had been identified in the Regulations and a set of amendments was awaited;
- The transitional regulations were made and described how existing members' accrued rights would be treated in the new scheme; and
- Governance regulations would be available in first draft in October 2014 with the final version expected in January 2015 and would specify how the governance requirements of the 2013 Act were to be applied in the LGPS.

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The report thereafter highlighted that the necessary work on the main scheme and transitional regulations was unlikely to impede software development or Fund implementation plans. In contrast however the timetable for the production of the governance regulations meant that in order to comply with the April 2015 deadline, Funds would have to undertake their governance reviews in advance of final regulations being available.

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The other pertinent developments included:-

- Employer training - training events for fund managers on 18 September and 2 October 2014 aimed mainly at Payroll and HR practitioners. Around 35 employer delegates were signed up for each event. A further resource for employers was provided at www.lgpsregs.org for scheme rules and explanatory guides;
- Employee information - the Fund members' information website www.scotlgps2015.org; and
- The new Pensions Administration System would replace the existing in-house system and was Heywood's "Altair" product used by the majority of Scottish and English/Welsh LGPS Funds.

Decision

The Panel noted the latest developments in relation to the implementation of the LGPS (Scotland) 2015.

8. LOCAL GOVERNMENT PENSION SCHEME - GOVERNANCE ISSUES

The Panel considered a report by the Chief Finance Officer providing an update on the recent developments in relation to the governance arrangements in respect of the ongoing reform of the Local Government Pension Scheme (LGPS) through the Public Service Pensions Act 2013 with effect from 1 April 2015.

The report detailed that a Heads of Agreement on scheme governance had now been reached between COSLA, Trades Unions and the Scottish Government and the statutory regulations underpinning governance rules would be finalised in early 2015.

The key milestones were as detailed below:-

- The consultation period for the draft regulations from 16 October to 27 November 2014;
- The Scottish Public Pensions Agency (SPPA) review of consultation comments from 28 November to 19 December 2014;
- The final drafting of regulations from 5 to 16 January 2015; and
- The ministerial signing off of the regulations on 27 January 2015.

The report thereafter detailed the following requirements within the Act for the operation of the Pensions Board including:-

- Ensuring the secure compliance with the scheme regulations and other legislation relating to the governance and administration of the scheme and the Pensions Regulator;
- To undertake any such other matters as the scheme regulations may specify;
- Having an equal number of employer and member representatives (a minimum of 4 trade union and 4 employer);
- That the scheme manager should be satisfied that members did not represent a conflict of interest; and
- That meetings should take place concurrently with the Pensions Committee.

In furtherance of the requirement to establish a Pension Board it was proposed to consult Fund Employers and Trade Unions for their views as to how the new arrangements could best operate and the report provided information on the consultation action plan and associated implementation timescales.

Decision

The Panel noted the report.

9. GENERAL GOVERNANCE MATTERS

The Panel considered a report by the Chief Finance Officer presenting an update on various matters associated with the governance of the Falkirk Council Pension Fund.

The areas covered within the report included the following:-

- The Pension Fund's Risk Register;
- Social Housing;
- Local Infrastructure;
- Prudential Additional Voluntary Contributions (AVC's); and
- The Local Authority Pension Fund Forum (LAPFF) of 58 local authority Pension Funds.

Decision

The Panel noted the report.

10. CORPORATE GOVERNANCE UPDATE

The Panel received a presentation by Allan MacDougall and Janice Hayward, PIRC Ltd

The presentation included information on the undernoted:-

- The value of corporate governance including the key milestones and fundamental objectives;
- The Regulators including the Financial Conduct Authority, the Prudential Regulatory Authority (PRA) and the Financial Reporting Council (FRC);

- The Boardroom themes; and
- Practice and Stewardship including shareholder engagement in terms of the UK Stewardship Code principles, responsible investment and the development of a broader Stewardship Plan and the protection of shareholder value.

The Convener thanked Mr MacDougall and Ms Hayward for their comprehensive presentation.

Decision

The Panel noted the presentation.

11. ORDER OF BUSINESS

In terms of Standing Order 14.2(i), the Convener advised of a variation to the order of business from that detailed on the agenda for the meeting. The following items have been recorded in the order that they were taken.

12. FUND MANAGER REVIEW

The Panel received a presentation Patrick Hand and Jamie Cumming, Aberdeen Asset Management.

The areas covered by the presentation included:-

- Business Update;
- Performance and Attribution;
- Equity;
- Current Positioning; and
- Portfolio Review.

The Convener thanked Mr Hand and Mr Cumming for their comprehensive presentation.

Decision

The Panel noted the presentation.

13. PRIVATE EQUITY AND ALTERNATIVES UPDATE

The Panel considered a report by the Chief Finance Officer on the progress of the Pension Fund's private equity and alternatives programme arising from the Investments Programme of SL Capital (Standard Life), Wilshire Associates, Grosvenor Capital and M&G for the quarter ending 30 June 2014.

Decision

The Panel noted the progress of the Pension Fund's private equity, infrastructure and credit markets programme for the quarter ending 30 June 2014.

14. FUND MANAGER PERFORMANCE REVIEW

The Panel considered a report by the Chief Finance Officer reviewing the overall performance of the Fund and of the undernoted Fund Managers:-

- Aberdeen Asset Management;
- Baillie Gifford Bonds;
- Baillie Gifford Diversified Growth;
- Legal and General;
- Newton Investment Management;
- Schroder Investment Management UK Equities; and
- Schroder Investment Management Property.

Decision

The Panel noted the Fund Managers' performance and the action taken by them during the quarter to 30 June 2014, in accordance with their investment policies.

AGENDA ITEM 4

FALKIRK COUNCIL

Subject:	**FALKIRK COUNCIL PENSION FUND - REPORT TO THOSE CHARGED WITH GOVERNANCE ON THE 2013/14 AUDIT**
Meeting:	**PENSIONS COMMITTEE**
Date:	**25 SEPTEMBER 2014**
Author:	**CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 This report invites the Committee to consider a report from Audit Scotland issued in accordance with the International Standard on Auditing (ISA 260) "Report to those charged with Governance on the 2013/14 Audit".

2. BACKGROUND

2.1 Regulation 31A of the Local Government Pension Scheme (Administration)(Scotland) Regulations 2008 requires administering authorities to publish a pension fund annual report and accounts that are separate from the other accounts of the administering authority. The fund annual report and accounts also require to be subject to a separate audit.

2.2 The audit for 2013/14 is being undertaken by the Fund's external auditors, Audit Scotland.

3. AUDIT PROCESS

3.1 The Annual Audit Plan was presented to the Pensions Committee on 6 March, 2014.

3.2 The Fund's Unaudited Annual Report and Accounts for 2013/14 were submitted for audit on 30 June 2014 in line with the required statutory deadline.

3.3 Under International Standard on Auditing 260 (ISA 260), auditors, before certifying the accounts, are required to communicate matters relating to the audit to those charged with governance. The report, referred to as the ISA 260, is to be provided in sufficient time to enable remedial action to be taken if necessary. Audit Scotland's ISA 260 report for 2013/14 is attached for information.

4. AUDIT OUTCOME

4.1 The ISA 260 reports that, subject to a final review, the audit will be unqualified.

4.2 The accounts have been adjusted for misstatements and other minor presentational and typographical matters. A monetary error relating to a duplicate journal entry was identified that resulted in a £30k overstatement of creditors. This amount was deemed immaterial to the accounts as a whole and accordingly I have proposed that no adjustment be made as a result.

5. MATTERS ARISING

5.1 The matters on which the auditor has specifically commented are as follows:

- Investment Management Expenses
- Presentational Matters
- Employee / Employer Contributions
- Bank Account
- Cash Balances

Investment Management Expenses

The Fund has incorporated the direct expenses associated with its Private Equity and Infrastructure assets within its investment management expenses. Due to the complex nature of 'fund of funds' and pooled investments there is difficulty in obtaining and guaranteeing the accuracy of the second layer of fees that arise from these complex structures. The Fund thought it appropriate to report the estimated figure for these expenses as a note rather than include it within its investment management expenses. The Fund awaits guidance from CIPFA on best practice going forward.

Presentational Matters

This comment relates to a lack of clarity regarding the change in market value note. The Fund is in compliance with the CIPFA exemplar Local Government Pension Scheme Fund Accounts however will review disclosure in 2014/15 to ensure greater clarity.

Employee / Employer Contributions

Audit have expressed concern over the late receipt, in some instances, of employer year end returns. The delay in receiving this information means that the Fund is unable to verify completely that the contributions reported on year end returns match the contributions remitted during the year. Delays also hold up progress in producing annual benefit statements, undertaking annual allowance tax checks, etc. The Fund is presently awaiting returns from 3 employers out of around 35 individual returns. The Fund continually emphasises to employers the importance of accurate and timeous returns.

Bank Account

The Local Government Pension Scheme regulations require the Fund to operate its own bank account through which all payments and receipts should be processed. Whilst receipts are credited directly to the Fund bank account, payments are made initially from the Council's bank account with re-imbursement being made immediately from the Fund bank account.

The issue of not charging payments to the Fund bank account straight away is not unique to Falkirk Council and is essentially due to the fact that Funds are reliant on the operating systems of their administering authority. Unfortunately these systems tend to be rigid and do not have the capacity to split transactions between more than one bank account.

The purchase of a new pension administration system may allow this matter to be addressed to some degree.

Cash Balances

The Fund had a £301k balance held by Falkirk Council at year end and was unable to fully verify £3k of this. This balance will be investigated on an on-going basis to ensure all balances can be confirmed.

6. CONCLUSION

6.1 The Fund's external auditors, Audit Scotland, have completed their report to those charged with governance and anticipate being able to issue an unqualified audit certificate.

6.2 Matters arising from the audit will be taken forward as appropriate in preparing the 2014/15 accounts.

7. RECOMMENDATION

7.1 The Committee is asked to note the ISA 260 report from Audit Scotland.

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

NIL

Falkirk Council Pension Fund

Report to those charged with governance on the 2013/14 audit

AUDIT SCOTLAND

Prepared for members of the Pension Committee

September 2014

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

Contents

Introduction

1. International Standard on Auditing (UK and Ireland) 260 (ISA 260) requires auditors to report specific matters arising from the audit of the financial statements to those charged with governance of a body in sufficient time to enable appropriate action.

2. This report sets out for the Pension Committee consideration the matters arising from the audit of the financial statements for 2013/14 that require to be reported under ISA 260. We are drawing to your attention those matters we think are worthy of note, so that you can consider them before the financial statements are approved and certified.

3. An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements prepared by management; however this does not relieve management of their responsibilities in this respect. This report has been prepared for the use of Falkirk Council Pension Fund and no responsibility to any third party is accepted.

Status of the audit

4. Our work on the financial statements is now substantially complete. The issues arising from the audit were included in a matters arising discussed with the Pensions Manager and Pensions Accountant on 21 August 2014. A copy of the matters arising schedule and the Pension Manager's response to the issues raised was copied to the Depute Chief Finance Officer to ensure that he agreed with any proposed amendments to the accounts.

5. We received the unaudited financial statements on 30 June 2014, in accordance with the agreed timetable. The working papers were of a good standard and the staff provided good support to the audit team. This enabled us to complete our on-site fieldwork by 20 August 2014.

Matters to be reported to those charged with governance

Conduct and scope of the audit

6. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in the Annual Audit Plan presented to the Pensions Committee on 6 March 2014, and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in May 2011.

7. As part of the requirement to provide full and fair disclosure of matters relating to our independence we can confirm that we have not undertaken non-audit related services. The 2013/14 agreed fee for the audit was disclosed in the Annual Audit Plan. As we did not carry out any additional work outwith our planned activity this fee remains unchanged.

Fraud

8. In our Annual Audit Plan we highlighted the responsibility audited bodies have for establishing arrangements to prevent and detect fraud and other irregularities. In presenting this report to the Pensions Committee we seek confirmation from those charged with governance of any instances thereof that have arisen that should be brought to our attention. A specific confirmation from management in relation to fraud has been included in the draft letter of representation.

Audit opinion & representations

9. Subject to the satisfactory conclusion of any outstanding matters and receipt of a revised set of financial statements for final review, we anticipate being able to issue an unqualified auditor's report on 25 September 2014 (the proposed report is attached at Appendix A). There are no anticipated modifications to the audit report.

10. We are required to report to those charged with governance all unadjusted misstatements which we have identified during the course of our audit, other than those of a trivial nature which we regard as errors less than £1,000.

11. A number of presentational adjustments were identified within the financial statements during the course of our audit. These were discussed with senior finance officers who agreed to amend the unaudited financial statements.

12. In addition, one monetary error was identified which was not processed through the financial statements by management. This related to the duplication of a lump sum payment offset by other payments that had been omitted from the financial statements. If adjusted the net impact on the balance sheet would be that net assets would increase by £30,000.

13. It is our responsibility to request that all errors be corrected although the final decision on this matter rests with those charged with governance taking into account advice from officers and materiality. Management explained that this adjustment was immaterial to the financial statements.

14. As part of the completion of our audit we seek written assurances from the Chief Finance Officer on aspects of the financial statements and judgements and estimates made. A draft letter of representation under ISA580 is attached at Appendix B. This should be signed and returned by the Chief Finance Officer with the signed financial statements prior to the independent auditor's opinion being certified.

Accounting and internal control systems

15. No material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

Matters arising from the audit

16. In our view, the following issue requires to be brought to your attention regarding the appropriateness of accounting policies or accounting estimates and judgements, the timing of transactions, the existence of material unusual transactions or the potential effect on the financial statements of any uncertainties.

Presentational Matters

17. The financial statements comply with pension fund accounting regulations. There are some areas where disclosures have improved since last year including the following:

- Disclosure of any single investment which exceeds either 5% of the Net Assets available for benefits, or 5% of any class or type of security.
- Disclosure of investment holdings and income in line with example accounts provided by CIPFA.

18. There is still scope for further improvement including more accurate disclosure of the change in market value of investments.

Resolution - The disclosure of the change in market value of investments is in line with the CIPFA exemplar Local Government Pension Scheme fund accounts. However, management acknowledge that this can be confusing and will review the disclosure for 2014/15 to ensure greater clarity.

Investment Management Expenses

19. Investment management expenses recorded in the Pension Fund Account are incomplete. The Fund has made improvements in disclosure from 2012/13 to include direct expenses from Private Equity and Infrastructure managers. However, indirect investment manager fees that arise from the 'fund of funds structures' are not included. Instead, they are accounted for within 'Profit and losses on disposal of investments and changes in market value of investments'. The calculation of these fees is a complex area, particularly in regard to pooled investment funds, and it is not always possible to calculate these fees accurately.

20. The Pension Fund has sought to address this issue by attaching an estimate of these expenses to note 15 in the accounts. This matter does not relate solely to Falkirk Council Pension Fund but also applies to other pension funds in Scotland.

Resolution - The Pensions Manager has made efforts to improve the Fund's transparency with regard to investment manager fees. At present the CIPFA Code of Practice on Local Authority Accounting 2013/14 does not make specific reference to investment management expenses however CIPFA has released an exposure draft on the subject which is under consultation. The Fund plans to implement the best practice recommended by CIPFA.

Bank Account

21. Under the terms of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 pension funds are required to maintain a separate bank account. Although Falkirk Council Pension Fund operates a separate bank account transactions are processed through the main council bank accounts and then monies are transferred in or out of the pension fund bank account. As a result of transactions being passed through the Council's bank account it is difficult to determine at any given point the status of the account i.e. is the balance due to the Council or to the pension fund. If the balance is due to the pension fund then the Council are liable to pay interest to the fund at no less than a commercial rate. The Fund's view is that there are considerable economic and practical advantages to processing payments in this manner. The Pensions Manager feels that this approach complies with the scheme requirements.

Employer/Employee Contributions

22. A number of scheme employers did not file their year-end contribution returns by the required deadline date meaning that the Fund was unable to verify its employer and employees contributions during the year-end process. This included one of the major employers who were unable to return data in the specified format because of the introduction of a new payroll system and still have areas where data has been omitted. There is currently one employer reporting that their remittance should be £36,000 more than what was received during the year. Therefore there a risk of error. However, even if the full amount of £36,000 is incorrect this would not be material to the accounts. Our audit opinion is therefore not affected by this issue. This is still in the process of being investigated.

Resolution - The Fund will continue to impress on employers the importance of submitting correct data timeously and in the correct format.

Cash Balances

23. The cash balances in the Net Asset Statement include £301,000 described as balances held by Falkirk Council. This amount is a balancing figure after accounting for all transactions relating to the Council, and management have provided a list of transactions that discloses that all save £3,000 of this amount can be attributed to the pension fund. Of the remaining balance management have confirmed that it is likely to be fully attributable to the pension fund but this has yet to be fully verified. Based on management assurances and work completed to verify the balance to date we have not treated this as an unadjusted error and we are satisfied that this issue does not impact on our audit opinion.

Resolution - the remaining balance is to be investigated on an on-going basis

Outstanding Information

24. A response is awaited in respect of the difference of £36,000 between the contributions data return of an employer and the amounts included in the fund accounts discussed at paragraph 22 above.

Acknowledgements

25. We would like to express our thanks to the staff of the Pensions section of Falkirk Council for their help and assistance during the audit of this year's financial statements which has enabled us to provide an audit report within the agreed timetable.

Appendix A: Proposed Independent Auditor's Report

Independent auditor's report to the members of Falkirk Council as administering body for Falkirk Council and the Accounts Commission for Scotland

I certify that I have audited the financial statements of Falkirk Council Pension Fund for the year ended 31 March 2014 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the fund account, the net assets statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 (the 2013/14 Code).

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Accounts Commission for Scotland, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Respective responsibilities of the Responsible Financial Officer and auditor

As explained more fully in the Statement of Responsibilities, the Chief Finance Officer is responsible for the preparation of financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Chief Finance Officer; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the financial statements:

- give a true and fair view in accordance with applicable law and the 2013/14 Code of the financial transactions of the fund during the year ended 31 March 2014, and of the amount and disposition at that date of its assets and liabilities
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2013/14 Code
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973 and the Local Government in Scotland Act 2003.

Opinion on other prescribed matter

In my opinion the information given in the Explanatory Foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I am required to report by exception

I am required to report to you if, in my opinion:

- adequate accounting records have not been kept
- the financial statements are not in agreement with the accounting records
- I have not received all the information and explanations I require for my audit
- the Governance Compliance Statement does not comply with guidance from the Scottish Ministers.

I have nothing to report in respect of these matters.

Fiona Mitchell-Knight FCA
Assistant Director (Audit Services)
Audit Scotland
4th Floor, South Suite
Athenaeum building
8 Nelson Mandela Place
Glasgow
G2 1BT

25 September 2014

Fiona Mitchell-Knight is eligible to act as an auditor in terms of Part VII of the Local Government (Scotland) Act 1973.

Appendix B: ISA 580 - Letter of Representation

Fiona Mitchell Knight
Assistant Director of Audit
Audit Scotland
4th Floor, South Suite
The Athenaeum Building
8 Mandela Place
Glasgow
G2 1BT

25 September 2014

Dear Fiona,

Falkirk Council Pension Fund
Annual Accounts 2013/14

1. This representation letter is provided in connection with your audit of the financial statements of Falkirk Council Pension Fund for the year ended 31 March 2014 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view of the financial position of Falkirk Council Pension Fund, as at 31 March 2014 and its income and expenditure for the year then ended.

2. I confirm to the best of my knowledge and belief, and having made appropriate enquiries of the Pensions Manager and the Pension Accountant, the following representations given to you in connection with your audit of Falkirk Council Pension Fund for the year ended 31 March 2014.

General

3. I acknowledge my responsibility and that of Falkirk Council Pension Fund for the financial statements. All the accounting records requested have been made available to you for the purposes of your audit. All material agreements and transactions undertaken by Falkirk Council Pension Fund have been properly reflected in the financial statements. All other records and information have been made available to you, including minutes of all management and other meetings.

4. The information given in the Annual Report to the financial statements, including the Explanatory Foreword, presents a balanced picture of the Falkirk Council Pension Fund and is consistent with the financial statements.

5. I confirm that the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole. I am not aware of any uncorrected misstatements other than those identified in the auditor's report to those charged with governance (ISA260).

Legality of Financial Transactions

6. The financial transactions of Falkirk Pension Fund are in accordance with the relevant legislation and regulations governing its activities.

Financial Reporting Framework

7. The financial statements have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 and in accordance with the requirements of Local Government (Scotland) Act 1973 including all relevant presentation and disclosure requirements.

8. Disclosure has been made in the financial statements of all matters necessary for them to show a true and fair view of the transactions and state of affairs of Falkirk Council Pension Fund for the year ended 31 March 2014.

Accounting Policies & Estimates

9. All material accounting policies adopted are as shown in the Statement of Accounting Policies included in the financial statements. The continuing appropriateness of these policies has been reviewed since the introduction of IAS 8 and on a regular basis thereafter, and takes account of the requirements set out in the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.

10. The significant assumptions used in making accounting estimates are reasonable and properly reflected in the financial statements. There are no changes in estimation techniques which should be disclosed due to their having a material impact on the accounting disclosures.

Actuarial Assumptions

11. The pension assumptions made by the actuary in the IAS19 report on the Fund have been reviewed and I can confirm that they are consistent with management's own view

Fraud

12. I have considered the risk that the financial statements may be materially misstated as a result of fraud. I have disclosed to the auditor any allegations of fraud or suspected fraud affecting the financial statements. There have been no irregularities involving management or employees who have a significant role in internal control or that could have a material effect on the financial statements.

Corporate Governance

13. I acknowledge, as the officer with responsibility for the proper administration of the Fund's financial affairs under section 95 of the Local Government (Scotland) Act 1973, my responsibility for the corporate governance arrangements and internal controls. I have reviewed the corporate governance compliance statement and the disclosures I have made comply with the guidance from the Scottish Ministers. There have been no changes in the corporate governance arrangements or issues identified, since the 31 March 2014 which require disclosure.

Related Party Transactions

14. All transactions with related parties have been disclosed in the financial statements. I have made available to you all the relevant information concerning such transactions, and I am not aware of any other matters that require disclosure in order to comply with the requirements of IAS24, as interpreted by the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.

Investment Management Expenses

15. Investment management expenses do not reflect the total cost related to fund of fund investments. The fees related to the indirect expenses of these funds are included within 'Profit and losses on disposal of investments and changes in market value of investments'. The Fund has been successful to some extent in obtaining a more granular disclosure of these fees. However the fund of funds structure makes full disclosure a complex and intricate process. We will work with fund managers and the fund custodian to ensure further disclosure in 2014/15 and will await best practice guidance being published by CIPFA

Investment Assets and Current Assets

16. On realisation in the ordinary course of the Fund's business the investment and current assets in the net asset statement are expected, in my opinion, to produce at least the amounts at which they are stated. In particular, adequate provision has, in my opinion, been made against all amounts owing which are known or may be expected to be irrecoverable.

Investment Liabilities and Current Liabilities

17. All liabilities have been provided for in the books of account as at 31 March 2014.

Contractual commitments

18. All outstanding call payments due to unquoted limited partnership funds have been fully included in the accounts for the period to 31 March 2014.

Employer / Employee Contributions

19. The contribution figures recorded in the accounts represent payments made by employing bodies on a monthly basis throughout the year and processed through the ledger. In addition, a year end reconciliation is carried out between the ledger and annual returns from employing bodies. These annual returns provide an additional source of assurance of total payments

made in the year. The Fund will continue to impress on employers the importance of submitting correct data timeously and in the correct format.

Bank Account

20. The fund maintains a separate bank account but payments and some receipts are initially processed through the Council's bank accounts. The transactions for the fund processed through the Council's bank accounts are promptly repaid or transferred and consequently the balance owed to or due by the Council at any time is not significant

Events Subsequent to the Net Asset Statement

21. There have been no material events since the date of the Net Asset Statement which necessitate revision of the figures in the financial statements or notes thereto including contingent assets and liabilities.

22. Since the date of the net asset statement no events or transactions have occurred which, though properly excluded from the financial statements, are of such importance that they should be brought to your notice.

Yours sincerely

Bryan Smail
Chief Finance Officer

FALKIRK COUNCIL

Subject: **FALKIRK COUNCIL PENSION FUND - ANNUAL ACCOUNTS 2013/14**
Meeting: **PENSIONS COMMITTEE**
Date: **25 SEPTEMBER 2014**
Author: **CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 The purpose of this report is to ask the Pensions Committee to review the Audited Accounts and Annual Report of the Fund for 2013/14 and to ask the Pensions Committee to give its approval.

2. AUDIT PROCESS

2.1 The Pension Fund Annual Report and Accounts 2013/14 have now been audited and copies are attached. The auditor's certificate is free from qualification.

2.2 Matters arising have been highlighted by Audit Scotland in their ISA 260 document and have been reported to Committee in the preceding report.

2.3 A copy of the audited accounts and annual report will be posted on the Pension Fund website and will be brought to the attention of all Fund employers.

3. RECOMMENDATION

3.1 Members of the Pensions Committee are asked to review the Audited Falkirk Council Pension Fund Annual Report and Accounts 2013/14.

3.2 The Pensions Committee is asked to approve the Audited Falkirk Council Pension Fund Annual Report and Accounts 2013/14

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

NIL

CONTENTS

FOREWORD BY THE CHIEF FINANCE OFFICER

As prescribed by Regulations, the Pension Fund annual report and accounts are audited in their own right, separate and removed from Falkirk Council's annual financial statements. These provide the reader with a wide range of information about the Fund including details on the governance and performance of Administration and Investment aspects, as well as the more traditional financial statements. These financial statements include the Pension Fund Account which details the Income and Expenditure of the Fund during the year, and the Net Asset Statement which provides comment on the value of assets held at year end. Both these sections are further supplemented by the Notes to the Accounts.

The Pension Fund Account at year end 31 March 2014 shows that contributions in 2013/14 have risen to £76m from £69m in 2012/13. This rise is the result of a combination of factors, including Auto-enrolment and increased strain costs arising from employer efficiency programmes. The Fund Account also shows that the market value of investments, including profits from trading, has risen by £123m during the year, reflecting a continuing improvement in financial markets.

The Fund's Net Asset Statement at year end 31 March 2014 shows that the Fund had £1.58bn of assets under its management compared with £1.46bn at 31 March 2013. The improved asset value is mainly the result of the returns on fund investments of 6.9% against a benchmark target over the year of 6%. This out performance is particularly welcome given the fact that the low yield on government bonds continues to require a high value to be placed on Fund liabilities.

Pension Funds by their very nature have long-term time horizons. The Falkirk Council Pension Fund as part of the Local Government Pension Scheme with its underpinning statutory framework is well placed to recognise this. In consequence, a Funding Strategy Statement allows employers with strong covenants to recover a deficit position over 20 years and a stability mechanism allows employers to budget for their contributions over the medium term. This is particularly important given the financial pressures prevalent across the public sector.

The Pensions Committee took a decision in March to invest £30m in social/affordable housing. This is an innovative mandate and follows extensive background research and market soundings. The mandate was awarded to Hearthstone in associate with Castle Rock Edinvar.

Looking forward, there are a variety of significant challenges on the immediate horizon. The LGPS is being updated, most notably to a career average basis, in April 2015 to meet the requirements of the Public Service Pensions Act 2013. A Heads of Agreement on scheme design between COSLA, Unions and Scottish Government has been reached but similar agreement on governance arrangements remains the subject of discussion. This will require a review of the Fund's existing governance arrangements to reflect the introduction of the required Scheme Manager and Pension Board.

Work is also underway with the Fund employers and actuary in preparation for the 2014 triennial actuarial valuation. This will set employer contribution rates for the next 3 years and will occur within the framework of the Funding Strategy Statement mentioned above. One benefit arising from the inevitable rise in interest rates is that it will reduce the measurement of the Fund's liabilities.

The complexity of the new Scheme allied with other recent amendments to the LGPS which will involve multiple calculations of employee benefits requires investment in a new pensions system which will be fit for purpose going forward. This will of itself be a challenging project.

The Pension Act 2014 provides for contracting out to be abolished from April 2016. This will impact on both employees and employers and is particularly unwelcome given the financial pressures both are facing.

It is noteworthy that the debate in England and Wales on Fund numbers and structure has now moved on to consider questions of the relative merits of passive versus active management and the benefits of models which aggregate Fund investment. It is inevitable that this debate will impact on Scotland.

Many of these matters were covered in the Fund's annual Pensions and Investment Conference in March.

Bryan Smail

Bryan Smail, CPFA MBA
Chief Finance Officer
30 June 2014

STATEMENT OF RESPONSIBILITIES FOR THE STATEMENT OF ACCOUNTS

THE ADMINISTERING AUTHORITY'S RESPONSIBILITIES

The Authority is required to:-

- Make arrangements for the proper administration of the financial affairs of the Falkirk Council Pension Fund and to ensure that one of its officers has the responsibility for the administration of those affairs. In this Authority, that officer is the Chief Finance Officer;

- Manage the Fund's affairs to secure economic, efficient and effective use of its resources and safeguard its assets; and

- Approve the Statement of Accounts.

THE CHIEF FINANCE OFFICER'S RESPONSIBILITIES

The Chief Finance Officer is responsible for the Statement of Accounts which have been properly prepared in accordance with the Local Government (Scotland) Act 1973, and the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 (the Code) and the 2007 Pensions Statement of Recommended Practice (the 2007 Pensions SORP).

In preparing this Statement of Accounts, the Chief Finance Officer has:-

- selected suitable accounting policies and then applied them consistently;
- made judgements that were reasonable and prudent; and
- complied with the accounting code of practice.

The Chief Finance Officer has also:-

- kept proper accounting records which were up to date; and
- taken reasonable steps to prevent and detect fraud and other irregularities.

STATEMENT OF ACCOUNTS

The Statement of Accounts presents a true and fair view of the financial position of the Falkirk Council Pension Fund as at 31 March 2014 and its income and expenditure for the year ended 31 March 2014.

Bryan Smail

Bryan Smail, CPFA MBA
Chief Finance Officer
30 June 2014

FUND AND GOVERNANCE OVERVIEW

Fund Overview

Under the statutory provisions of the Local Government Pension Scheme, Falkirk Council is designated as an “Administering Authority” and is required to operate and maintain a pension fund - the Falkirk Council Pension Fund (“the Fund”).

The Fund is used to pay pensions, lump sum benefits and other entitlements to scheme members and their dependants. Contributions to the Fund are made by employee members and by participating employers. The Fund also receives income from its investments, which include equities, property and bonds.

Fund employers include Clackmannanshire, Falkirk and Stirling Councils, Scottish Police Authority, Scottish Fire and Rescue Service, Central Scotland Joint Valuation Board, the Scottish Environment Protection Agency (SEPA), the Scottish Children’s Reporter Administration (SCRA), Forth Valley College, Falkirk Community Trust Ltd and a number of non-profit making charitable bodies in Central Scotland.

An actuarial valuation of the Fund is undertaken every three years and acts as an independent financial health check to determine how much money needs to be paid to the Fund so that it can continue to pay benefits both now and in the future. The last valuation was produced on 31 March 2011 and showed that the Fund was 86% funded, meaning that it had 86% of monies needed to pay the benefits of scheme members based on the rights they had accumulated to that date. Two important aspects highlighted by the actuary were the risks posed to the Fund from future improvements in mortality rates and the challenges to the Fund from a maturing membership.

Whilst the impact of an ageing workforce on future cash-flows should not be under-estimated, it is important to note that the time horizon of the Fund is long term. Consistent with this, the funding strategy is to allow employers with strong financial covenants to recover any deficit position over a period of up to 20 years. A stability mechanism within the strategy also helps employers budget for their contributions in the short term and helps smooth out volatility from what could be significant changes in the employer contribution rate.

The Fund operates under the auspices of the Local Government Pension Scheme. Scheme membership is made up of active, deferred and pensioner members. To be able to join the scheme, a person must be employed by a participating employer and not be eligible to join one of the other public sector pension schemes.

Investment Management of the Fund is undertaken by external fund managers and overseen by the Council’s Pensions Section. Administration of the Fund is undertaken in-house by the Pensions Section.

Governance Overview

Prior to the Local Government Elections of May, 2012, all Pension Fund business of Falkirk Council was delegated to its Investment Committee.

Following the publication in 2011 of statutory guidance relating to governance matters, the Authority undertook a wide ranging consultation which culminated in new governance arrangements being approved by Falkirk Council on 14 March 2012.

The new approach to governance means that pension fund business is delegated to a Pensions Committee with the support of an advisory Pensions Panel.

i) Pensions Committee

The Pensions Committee consists of nine members – six elected members from Falkirk Council and three members drawn from the Panel. The Committee meets on a quarterly basis with meetings being held mainly in public session. Members of the Committee are as follows:

Councillor John Patrick (Convener)	-	Elected Member (Falkirk Council)
Councillor Jim Blackwood	-	Elected Member (Falkirk Council)
Councillor Thomas Coleman	-	Elected Member (Falkirk Council)
Councillor Steve Carleschi	-	Elected Member (Falkirk Council)
Councillor Craig Martin	-	Elected Member (Falkirk Council)
Councillor Dr CR Martin	-	Elected Member (Falkirk Council)
Councillor Callum Campbell	-	Employer Representative (Stirling Council)
Mr Alastair Redpath	-	Pensioner Representative
Miss Mary Keggan	-	Union Representative

The Committee's key responsibilities are:-

- to oversee the administration of the Fund
- to manage the investments of the Fund
- to establish and review investment strategy
- to ensure the suitability and adequate diversification of investments
- to take proper advice in relation to investment matters
- to set the strategic asset allocation and individual manager benchmarks and targets
- to review the performance of investment managers on a regular basis
- to select and appoint investment managers and custodians as required
- to formulate and monitor a funding policy for the Fund
- to ensure the Fund is subject to actuarial valuations as required
- to approve the Annual Report and Accounts

(Councillors Patrick, Blackwood and Carleschi and Miss Keggan were active members of the Scheme during 2013/14. Mr Redpath is a pensioner member of the Scheme).

The Committee is supported at its meetings by officers and professional advisers. External Auditors were also in attendance at several of the 2013/14 meetings.

ii) Pensions Panel

The Panel comprises 15 members and includes Trade Union, Employer and Pensioner representatives. One member from each of these representative groups has been co-opted to sit on the Pensions Committee where they have full access to papers and voting rights. The Panel meets on a quarterly basis approximately two weeks prior to the corresponding Committee meeting. Members of the Panel are as follows:

Councillor Callum Campbell (Convener)	-	Employer Representative (Stirling Council)
Mr Willie Watson	-	Employer Representative (Stirling Council)
Mr Gordon Laidlaw	-	Employer Representative (Scottish Autism)
Mr Ed Morrison	-	Employer Representative (SCRA)
Mrs Jennifer Welsh	-	Employer Representative (SEPA)
Mrs Alison Stewart	-	Employer Representative (Forth Valley College)
Mrs Susan Mackay	-	Employer Representative (Clackmannanshire Council)
Councillor Archie Drummond	-	Employer Representative (Clackmannanshire Council)
Mrs Jackie McAuley	-	Employer Representative (Falkirk Council)
Vacant	-	Employer Representative (Falkirk Council)
Mr Alastair Redpath	-	Pensioner Representative
Mr Ian McLean	-	Pensioner Representative
Miss Mary Keggan	-	Union Representative
Mr Sandy Harrower	-	Union Representative
Mr Andy Douglas	-	Union Representative

The Panel's main responsibility is to provide advice and guidance to the Pensions Committee on all matters relating to the business of the Falkirk Council Pension Fund. The Panel is also supported by officers and professional advisers.

Full details of the governance arrangements are set out in the Governance Compliance Statement which has been reproduced in Pages 7 to 11 of this report.

iii) Member Training

The Fund's training policy recognises that those persons involved in the governance of the Fund should have the necessary level of skills and knowledge to allow them to carry out their duties. Accordingly, various seminars, conferences and in house training events are made available for Committee and Panel members to attend, During 2013/14, these included:

02/10/2013 – Baillie Gifford – Local Authority Investment Seminar
12/10/2013 – Local Government Pension and Investment Forum
15/11/2013 – In house Training Event – on Assets, Equities and Bonds
12/12/2013 – COSLA - Reform of LGPS in Scotland

The Fund also hosted sessions on i) Accounting for Pensions and ii) Tax for High Earners. In Spring 2014 the Fund held its own annual Pensions and Investment Conference.

A training needs survey was carried out in December, 2013, the results of which are being taken into account in shaping future training arrangements.

iv) Attendance at meetings

Under the Governance arrangements, members of the Pensions Committee are required to attend at least three out of four Committee meetings annually. An analysis of attendance during 2013/14 showed that members were achieving the desired standard.

The Fund's governance policy, including the Governance Compliance Statement and Governance Training Statement, are set out in the Governance Framework documents.

Communications

Communication with stakeholder groups was achieved through emails, publication of committee minutes, newsletters, payslip messaging and the new pension fund website. The range of topics covered included actuarial matters, benefits and regulatory changes, investment performance and investment manager/adviser presentations.

Statement of Investment Principles

The Fund has published a Statement of Investment Principles governing its decisions about Fund investments.

Funding Strategy Statement

The Fund's approach to dealing with the funding of its liabilities is set out in the Funding Strategy Statement.

More Information

Copies of the Statement of Investment Principles, the Funding Strategy Statement and the Governance Framework document are available from the Chief Finance Officer, Falkirk Council, Municipal Buildings, West Bridge Street, Falkirk FK1 5RS or at www.falkirkpensionfund.org.

GOVERNANCE COMPLIANCE STATEMENT

Regulation 27 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008 (SSI 2008/228) requires Administering Authorities to prepare and publish a written statement setting out the terms of their current governance arrangements. The undernoted Statement sets out the compliance arrangements in place during 2013/14 and meets the standards set out by the Scottish Public Pensions Agency in their paper of April 2011, entitled Governance Compliance Statement.

Principle A – Structure

	Requirement	Level of Compliance	Arrangements in Place
(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.	Full Compliance	Falkirk Council, as Administering Authority of the Falkirk Council Pension Fund, has established a Pensions Committee to which it has delegated the administration of benefits and strategic management of fund assets.
(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.	Full Compliance	The Pensions Committee includes three members co-opted from the Pensions Panel representing the interests of members, pensioners and employers.
(c)	That where a secondary committee or panel has been established, the structure ensures effective communication across both levels.	Full Compliance	The main channel of communication between the Pensions Committee and the Pensions Panel lies with the three Committee members who are also Panel members. Communication is also assisted by synchronising Panel meetings with a corresponding Committee meeting and through the sharing of minutes.
(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.	Full Compliance	Three places on the Pensions Committee are reserved for members of the Pensions Panel.

Principle B – Representation

	Requirement	Level of Compliance	Arrangements in Place
(a)	That all key stakeholders are afforded the opportunity to be represented within the main or secondary committee structure. These include:		
	(i) Employing authorities (including e.g. admission bodies);	Full Compliance	Representatives of major fund employers, including one admission body, sit on the Pensions Panel. A nominee from the Panel's employer representatives sits on the Pensions Committee.
	(ii) Scheme members (including deferred and pensioner scheme members);	Full Compliance	Non-pensioners are represented by the Trade Union Panel members and by the Union representative who sits on the Pensions Committee. Pensioners are represented by the pensioner members who sit on the Panel and the member who sits on the Committee.
	(iii) Where appropriate, independent professional observers; and	Not Compliant	There are no formal independent professional observers of Committee or Panel business. It is considered that: • the diversity of representation; (employers, pensioner and Unions) • the annual audit process; and • the attendance of professional advisors at most Panel and Committee meetings provide robust and adequate scrutiny of pension fund business.
	(iv) Expert advisors (on an ad-hoc basis).	Full Compliance	Support for the Pensions Committee and Pensions Panel is provided by the undernoted advisors: • actuary and investments, Hymans Robertson • corporate governance, PIRC Ltd • investment managers and custodian, as required.
(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.	Full Compliance	Panel members who are co-opted onto the Pensions Committee have equality of access to papers, meetings and training and have full opportunity to contribute to the decision making process, including the right to vote.

Principle C – Selection and role of lay members

Requirement		Level of Compliance	Arrangements in Place
(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.	Full Compliance	Members of the Pensions Committee are subject to the Falkirk Council Councillors' Code of Conduct. Members of the Pensions Panel have been appointed on the understanding that they are subject to the Falkirk Council Councillors' Code of Conduct. Induction and ongoing training continues to be delivered to Committee and Panel members.
(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.	Full Compliance	Declaration of interests is a standard procedure at the start of all Committee and Panel meetings. Declarations are noted in the minutes.

Principle D – Training/Facility Time/Expenses

Requirement		Level of Compliance	Arrangements in Place
(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.	Full Compliance	The administering authority's approach to training is set out in its training policy for the Pensions Committee and Pensions Panel members. Training is delivered in large part by addressing specific items at Committee and Panel meetings and complemented by visits to Fund Managers, bespoke training events and attendance at industry seminars and conferences. Expenses incurred by Committee and Panel members are met either by the Fund or the Falkirk Council scheme for payment of Members expenses.
(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.	Full Compliance	The Training Policy for the Pensions Committee and Pensions Panel applies uniformly to all members.
(c)	That the Administering Authority considers the adoption of annual training plans for committee members and maintains a log of all such training undertaken.	Full Compliance	The Training Policy for the Pensions Committee and Pensions Panel includes the requirement for members to undergo training needs analysis and the development of commensurate training plans. A register of training undertaken will be maintained.

Principle E – Voting

	Requirement	Level of Compliance	Arrangements in Place
(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.	Full Compliance	All members of the Pensions Committee including co-opted members have voting rights on the basis that they have executive responsibility for pension fund decision making.

Principle F – Meetings (Frequency/Quorum)

	Requirement	Level of Compliance	Arrangements in Place
(a)	That an Administering Authority's main committee or committees meet at least quarterly.	Full Compliance	The Pensions Committee hold quarterly meetings. Additional meetings are called as required.
(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.	Full Compliance	The Pensions Panel hold quarterly meetings and meets roughly two weeks in advance of the Pension Committee. Additional meetings are called as required.
(c)	That an Administering Authority that 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.	Full Compliance	The Council does include lay members on its Pensions Committee. However, in order to ensure that the interests of wider fund stakeholders can be represented, the Fund holds a Pensions & Investment Conference each year.

Principle G – Access

	Requirement	Level of Compliance	Arrangements in Place
(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.	Full Compliance	Members of the Pensions Committee and Pensions Panel have equal access to any committee papers, documents and advice that falls to be considered at meetings of the Pensions Committee.

Principle H – Scope

	Requirement	Level of Compliance	Arrangements in Place
(a)	That Administering Authorities have taken steps to bring wider scheme issues within the scope of their governance arrangements.	Full Compliance	The Pensions Committee and Panel agendas include reports pertaining to both administration and investment matters such as regulatory changes, actuarial valuation and funding level updates, admission agreements, investment strategy and Fund/ Investment Manager performance.

Principle I – Publicity

	Requirement	Level of Compliance	Arrangements in Place
(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.	Full Compliance	Employers, Unions and Pensioners have been consulted regarding the governance arrangements and invited to participate. Full details of the Governance arrangements are published on the Fund's website.

Certification

It is my opinion that the governance arrangements set out above provide reasonable and objective assurance that any significant risks impacting on the achievement of the principal objectives of the Pension Fund will be identified and actions taken to avoid or mitigate their impact.

Bryan Smail, CPFA MBA
Chief Finance Officer

Introduction

This part of the Annual Report provides a review of the Fund's administration, governance and investment activities during 2013/14 and a look forward at key themes expected to be of influence during 2014/15.

Business Context

Staffing

The Pensions Section of Falkirk Council provides an in-house pensions administration and investment service to enable the Council to fulfil its statutory obligations within the terms of Local Government Pension Scheme. This is augmented through the Fund's service level agreement with the Lothian Pension Fund for the purpose of providing investment support, particularly in the areas of monitoring and reporting upon manager performance.

The Pensions Section consists of 11.5 full time equivalent staff and is headed by the Pensions Manager, who in the main reports directly to the Chief Finance Officer.

The composition of the Section is as follows:

Role	Nos.	Average Years of Service	Pensions Qualification
Pensions Manager	1	31 years	Yes
Pensions Project Officer	1	43 years	Yes
Fund Accountant	1	7 years	Yes
Pensions Officers	2	28 years	Yes (1 post)
Pensions Support Officer	1	23 years	No
Accountancy Assistant	0.5	10 years	No
Trainee Pensions Officer	1	0 years	No
Pensions Assistants	4	13 years	No
Total	11.5		

Ethos

The Pensions Section contributes towards Falkirk Council's goals and values by discharging the Council's obligations as an administering authority. The Section recognises the need to provide an effective service and embraces the following mission statement:

- to meet targets
- to invest in people
- to adopt new and more efficient methods of service delivery
- to be responsive to our customers
- to monitor and report performance
- to achieve the goals we have set ourselves

The key objectives of the Pensions Section are:

- to provide an efficient and cost effective service that meets members' needs
- to safeguard and undertake the prudent investment of Fund assets
- to support the corporate activities of Falkirk Council and constituent Fund employers
- to ensure good governance of the Fund and compliance with statutory requirements

Functions

The principle activities of the Pensions Section are:

- to oversee the implementation of the Fund's investment strategy
- to oversee the implementation of the Fund's funding strategy
- to undertake the administration obligations of the Fund, including the payment of benefits
- to provide information, guidance and communications material to Fund stakeholders
- to undertake the accounting obligations of the Fund
- to support the Pensions Committee and Pensions Panel in its activities
- to contribute to the development of public sector pensions policy

The work of the Section can be characterised broadly as being either Administration, Investment, Accounting, Governance or Communications related. The bulk of activity and staff time is however focused on administration related matters.

Systems

All Pensions Section staff have access to up to date computer hardware and operating systems. In addition to normal desktop software, the range of services provided by the Section requires it to have access to the following systems:

System	Database	Purpose
In House Pensions Administration System	Ingres	Pensions Administration
Resourcelink	Oracle	Pensioner Payroll
Integra	Oracle	Financial Information System
Passport (Northern Trust)	Web Based	Custodian Information
Clydesdale Bank	Web Based	Fund Banking Information

Within the Pensions Administration System, archive records of all Fund leavers since 1986 are held in electronic format.

The majority of investment managers, who manage assets for the Fund, have developed web based applications to enable clients to obtain up to date valuations and reports. Consolidated investment valuations are maintained by the Fund's Custodian Northern Trust, who also safeguard the Fund's assets and keep a record of transactions undertaken by managers.

Risk Management

Pension fund management is not immune from risk, whether this be a physical failure of hardware or a breakdown in systems of control. Whilst it is not possible to eliminate risk completely from day to day operational activity, the nature of risk has been evaluated and strategies put in place to minimise its adverse effects. These are set out in the following documents:

- the Operational Risk Management Action Plan
- the Finance Business Continuity Plan
- the Pensions Contingency Plan
- the Pension Fund Risk Register
- the Fund's Statement of Investment Principles

An analysis of investment risk is set out in note 23 (on page 44 of the Annual Report and Accounts).

Risk is a regular item of discussion at the quarterly Pensions Committee Panel meetings. The risk register can be viewed at www.falkirkpensionfund.org.

Service Standards

The key performance standards of the Pensions Section are:

- to maintain pension administration costs to less than £25 pa per scheme member
- to meet all deadlines for accounts, payments, statistical returns and remittances
- to respond to enquiries within 14 days

Performance information is supplied to both CIPFA and the Scottish Executive as part of an annual review of performance across all Councils. In addition, a range of detailed service standards have been developed by the Pensions Section.

Annual Review of 2013/14 Activities

As with 2012/13, 2013/14 was dominated by the pensions reform agenda and in particular by the well-publicised trio of state initiatives – the Public Service Pensions Act 2013, and Workplace Pensions (i.e. auto enrolment) and State Pension Reform.

Public Service Pensions Act 2013

The Public Service Pensions Act 2013, which contained many of the recommendations from the Hutton Review, received Royal Assent in May 2013. This requires that from April, 2015 public sector schemes, including the Local Government Pension Scheme, have to conform to a prescribed set of standards, such as:

- Having a Career Average structure
- Aligning scheme retirement age with State Pension Age
- Protecting the accrued rights of existing members on a final salary basis
- Providing additional protection for older members
- Having a mechanism to cap future costs for employers
- Instituting a national Scheme Advisory Board and local Pension Boards
- Giving greater powers given to Treasury and the Pensions Regulator

The process for reforming the Local Government Pension Scheme (LGPS) is being taking forward in Scotland by the Scottish Local Government Pension Advisory Group (SLOGPAG). The group consists of representatives from COSLA, Scottish Government and Trade Unions. A *Heads of Agreement on Scheme Design* was published in January, 2014. This confirmed that the accrual rate for LGPS 2015 would operate on a 1/49ths basis with revaluation at the rate of the Consumer Price Index. A *Heads of Agreement on Governance* is awaited and is expected to set out the basis on which local pension boards and the national Scheme Advisory Board are to function.

During the year the Pensions Section has contributed to various consultations pertaining to scheme reform.

Workplace Pensions Reform

Better known as Auto-Enrolment (AE), this initiative became law on 1st October, 2012, but did not affect any Falkirk Council Pension Fund employers until 2013/14. In essence, with effect from their auto enrolment start data (i.e. staging date), employers have to enrol certain categories of non scheme members into their auto enrolment nominated pensions vehicle. For local authorities the AE pensions vehicle is the Local Government Pension Scheme (Scotland) or, for teachers, the Scottish Teachers Superannuation Scheme.

The AE rules are complex and onerous in terms of the obligations placed on Payroll and HR administrators. The Pensions Section hosted 2 full day training events in 2012/13 to help prepare fund employers for the workload ahead.

Different employers within the Fund have taken differing approaches to auto enrolment with some postponing the enrolment of non joiners until 2017 and others embracing the enrolment concept in full.

The onset of auto-enrolment has generated a substantial increase in scheme membership (see Page 18). Going forward consideration will have to be given as to whether an additional resource is needed to support the increased throughput of records.

State Pension Reform

The Pensions Act 2014 confirmed that the UK Government is going ahead with its policy to replace the basic and additional State Pensions with a single-tier pension of £144 p.w. The change is scheduled to take place in April, 2016.

A key element of the reform is the ending of the National Insurance Contracting-Out rebate which is currently enjoyed by members and their employers. The cost to Falkirk Council as an employer has been estimated as £4m p.a. with the cost to Scottish local government generally being put at £125m.

Other Activities

Other key initiatives successfully completed during 2013/14 were as follows:

- pensioner payroll year end including pensions increase and P60 distribution
- FRS 17 and IAS 19 exercise
- audited Pension Fund Annual Report and Accounts for 2012/13
- active and deferred member benefit statements and newsletter
- risk register
- cash management strategy
- hosting of annual conference and other Panel and Committee training events
- annual allowance tax assessments
- processing of 2,000 protection certificates
- various requests from employers for cessation information
- participation in Club Vita
- decision made to invest in social and affordable housing
- commitments made to Wilshire Private Equity Fund IX and M&G UK Companies Financing Funds

Performance Indicators

	Target	2010/11	2011/12	2012/13	2013/14
Annual Member Admin. Cost	Under £25 per member	£16.12	£16.45	£14.50	£15.77
Staff / Member ratio	Between 1:2500 and 1:3200	1:2893	1:2932	1:2972	1:3237
No of Complaints	0	4	1	1	3
* Answer ad hoc enquiries in 14 days	90%	71%	72%	73%	73%
Lump Sums payments	Pay within 7 days	92%	99%	99%	99%

*The enquiries completion rate in 2013/14 was affected by the resignation of a Pensions Assistant in September, 2013. This post has now been replaced with a Trainee Pensions Officer but appointment to that post was not made until April, 2014.

Business Outlook

Triennial Valuation

2014/15 promises to be an especially challenging year for local authority pension funds in Scotland. The early part of the year is likely to be dominated by preparations being made for the actuarial valuation of 31 March 2014. The valuation will set the employer contribution rates for the three years starting from 1st April 2015 and will be eagerly awaited by employers given the current level of financial settlements. Results are expected in late autumn.

The results of the valuation will also be the catalyst for a review of investment strategy through an asset / liability modelling exercise and could potentially trigger the movement of assets between asset classes. The outcome of the asset review may also be influenced by the Department of Communities and Local Government (DCLG) call for (i) funds to collaborate more widely through collective investment arrangements (ii) for fund of fund structures to be phased out and (iii) for a greater proportion of assets to be managed passively.

During 2013/14, the Fund participated in Club Vita, an analytical longevity review service provided through the Fund's actuarial advisers, Hymans Robertson. It is hoped that by participating in Club Vita, the actuary will be able to formulate more accurate longevity assumptions as part of the valuation process.

The Reform Agenda

The latter part of 2014/15 will inevitably focus on the next incarnation of the Local Government Pension Scheme, namely the Career Average Revalued Earnings (CARE) arrangement being introduced from 1st April, 2015. Various statutory instruments are expected to be laid in the first half of 2014/15 to flesh out the precise terms of the new arrangements and to enable administrators and software developers to formulate their preparations for CARE.

Although the CARE arrangement begins on 1st April, 2015, the rights of existing members are to be protected on a final salary basis, meaning that most members in the Fund will have a benefit that is a mixture of Final Salary and Career Average. The complexities of this arrangement mean that the existing in-house Pensions Administration System is no longer fit for purpose. A new system will therefore be procured in 2014/15 and a project plan put in place to migrate data to the new system.

Arrangements are in hand to provide the Pensions staff and Fund employers with training on the new CARE Scheme. Additionally, a Communications strategy has been agreed nationally by all Scottish Funds with the aim of publicising the new Scheme to members before April next year.

The impact of the Public Service Pensions Act 2013 is not confined to administrative matters, but also extends to governance matters by requiring Funds to establish Pension Boards to help support Pensions Committees in complying with scheme rules and any codes of practice from the Pensions Regulator.

Miscellaneous

In order to promote/improve the take up of AVCs within the Fund, Prudential have been appointed to act as joint AVC Providers with Standard Life. This option should be available by late summer 2014.

The Scottish Public Pensions Agency (SPPA) is assuming responsibility for the pensions administration of officers in the Police Pension Schemes and the Firefighters Pension Schemes. The Pensions Section currently administers the rights of active, deferred and pensioner members of the former Central Scotland Police and Central Scotland Fire and Rescue Service. The migration of data to SPPA is expected to take place in late 2014/15 with a view to SPPA assuming responsibility by April 2015.

The provision of monthly payslips for pensioners costs around £25,000 per annum. Other costs arise from the despatch of newsletters and benefit statements by post. It is intended during the next 18 months to investigate the alternatives to paper payslips, although this timeframe may be affected by the facilities available within the newly procured Pensions Administration System.

The action of Clackmannanshire and Stirling Councils to implement an across the board pay cut has generated around 4,000 Protection Certificates. This will create an administrative overhead for both the Pensions section and feeder Payroll sections.

Following the Fund's £30m investment in Social and Affordable Housing, attention will be focused on the speed with which capital can be deployed by the Fund Manager Hearthstone and new housing units delivered.

The Fund's service level agreement with City of Edinburgh Council is scheduled to be reviewed during 2014/15 at which time options for joint investment in infrastructure projects will be considered.

The Government's decision to reduce the Annual Allowance tax threshold to £40,000 and lifetime allowance to £1.25m from 1st April, 2014 means that the tax rules will assume even greater significance to higher earners with more members than ever before being affected.

Conclusion

2013/14 has seen the continuation of a number of important activities both from an investment and administrative perspective. 2014/15 promises to be equally challenging with no let up in the pace of reform or goals to be met.

MEMBERSHIP UPDATE

Membership numbers are most commonly affected by persons joining or leaving the Scheme as part of normal staff turnover. From time to time, however, there can be more significant membership movements resulting from factors such as economic circumstances, staff transfers, changes in scheme rules or Government initiatives.

The balance of membership between contributors and pensioners is an important indicator of the maturity of the Fund and is a major factor in determining investment strategy.

Factors affecting recent membership numbers are as follows:

i) 2013/14 has seen a substantial increase in the number of active members. This is the result of certain employers (e.g. Falkirk Council, Clackmannanshire Council, SEPA, Scottish Autism, Forth Valley College) implementing full auto enrolment including the enrolment of non scheme joiners and new employees. It should be borne in mind that a significant number of the new members will be part time and thus the overall effect on the scheme's maturity may not be as great as the increase in member numbers would suggest;

ii) the challenging financial environment of the past few years continues to result in a steady flow of employees being granted early retirement thus creating a downward pressure on active membership but increasing pensioner member numbers;

iii) in July 2011, around 400 active members with Falkirk Council were transferred to Falkirk Community Trust Ltd, thus increasing Admission Body numbers and reducing Scheduled Body numbers; and

iv) the number of deferred and pensioner members continues to grow reflecting early retirement initiatives and workforce fluidity amongst Fund employers.

Number of Scheme Members

	Membership 31/03/12	**Membership 31/03/13**	**Membership 31/03/14**
All Fund Employers			
Actives	12,668	12,880	14,690
Deferreds	5,085	5,204	5,320
Pensioners	8,119	8,372	8,693
	25,872	26,456	28,703
Maturity Level (% of Deferred + Pensioner members to Total)	51.04%	51.32%	48.82%
Scheduled Bodies			
Actives	11,286	11,450	13,086
Deferreds	4,518	4,599	4,685
Pensioners	7,779	7,996	8,284
	23,583	24,045	26,055
Admission Bodies			
Actives	1,382	1,430	1,604
Deferreds	567	605	635
Pensioners	340	376	409
	2,289	2,411	2,648

Figure A below shows that whilst total Fund membership (i.e. active, deferred and pensioner members) has been steady over the past few years, there has been a substantial rise in 2013/14.

Figure A - Fund Membership from 1996 – 2014 in aggregate

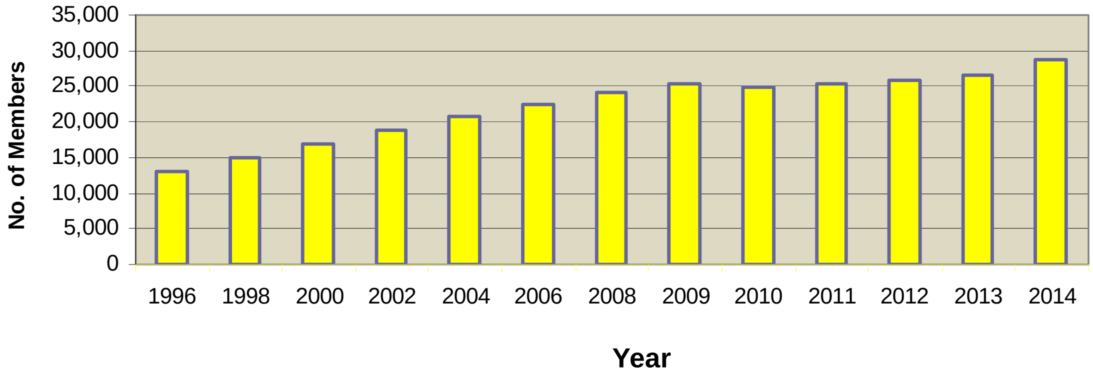
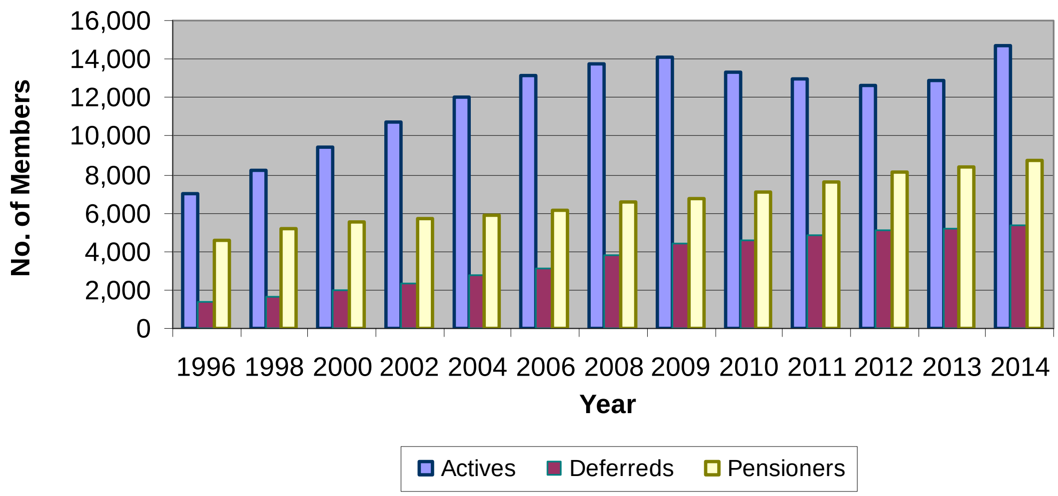


Figure B shows the growth in Membership split between active, deferred and pensioner members.

Figure B - Fund Membership from 1996 – 2014 by category



Statement by Schroders Investment Management Ltd, Fund Managers

The fragile economic recovery of 2013 paused in the first quarter. A number of factors helped stall the global economy and markets at the start of 2014.

US economic data improved over the course of 2013, prompting the Federal Reserve (Fed) to say in May that it might ‘taper’ its $85 billion a month quantitative easing programme. However, it took until December to confirm the start. This and severe weather held back the economy in the first quarter.

China’s previous rapid growth faltered in 2013 and continued to disappoint in the first quarter. Both manufacturing data and exports fell in the opening months of 2014. The radical policies of Prime Minister Shinzo Abe helped Japan’s economic indicators to start moving in the right direction in 2013. However, growth was subsequently revised down, while the trade deficit continued to widen. Fears about April’s rise in the consumption tax weighed on investors.

The struggles of many emerging markets beyond China continued. Several countries seen as vulnerable to a squeeze on money flows as a result of Fed tapering saw their currencies hit at the start of the year. Rising tensions over Ukraine was a major factor holding back markets in March.

In the eurozone, a fitful recovery finally began in the second quarter of 2013, helped by the European Central Bank cutting its interest rates in May to 0.5% and in November to 0.25%. Economic growth started to broaden out in 2014, albeit at a subdued rate. Elsewhere in Europe, the UK economy surprised many by its strength, while inflation remained subdued, although there were worries in some quarters that a new housing bubble is being inflated.

Lacklustre returns in the first quarter pared last year’s strong returns from developed market equities, but still left the MSCI World Index up 19.6% in dollar terms over the 12 months to March. Continued signs of growth in the eurozone helped the MSCI EMU Index advance 34.1% in dollar terms. Japan’s TOPIX Index was up 22.6% in dollars, despite a weak first quarter. The S&P 500 was only slightly behind, with a 22.4% rise which again breached all-time highs.

Fixed income markets changed tack over the 12 months. Bonds generally underperformed equities in 2013 as investors anticipated the Fed’s tapering and started to favour riskier assets. Yields on Treasuries and UK gilts rose above 3% by the year end. However, defying many predictions, fixed income broadly outperformed equities in the first quarter. Treasury yields fell sharply in January, prompted by emerging market volatility and weak US economic data, while emerging market debt subsequently recovered the losses suffered in January.

Schroder Investment Management Limited,
31 Gresham Street,
London EC2V 7QA

Investment Strategy

Following the Fund actuarial valuation on 31 March 2011, the Investment Committee agreed to implement a revised Investment Strategy in which the Fund was to decrease its allocation to traditional investments such as Equities and Bonds and increase its holding in Alternative Assets. In this context, Alternative Assets include Diversified Growth Funds, Credit Markets, Infrastructure and Private Equity.

The revised allocation targeted a 10% decrease in equities and 5% decrease in bonds. This restructuring enabled the Fund to appoint Baillie Gifford to manage a Diversified Growth mandate and Credit Suisse to manage an Infrastructure mandate, with both appointments taking place in 2011/12.

Throughout 2013/14 the Fund has continued to build upon this strategy, making additional commitments to the Private Equity and Credit Markets and seeking to reduce equity exposure as rebalancing opportunities arose. Given the strong performance of UK Equities during the year and an announcement from Baillie Gifford that it was closing its Diversified Growth fund to further investments, the opportunity was taken to reinvest £40m of equities in the Baillie Gifford Fund as part of a general rebalancing exercise.

The Fund also continued to progress its programme of Infrastructure investments, providing a further $13m in funding during the year to Grosvenor Capital Management – Grosvenor having taken ownership of the Customised Infrastructure Strategies Fund from Credit Suisse. The investments made to this Fund during the year has left it close to its commitment level.

A comparison of the strategic allocation of Fund Assets with the actual allocation at 31 March 2014 is set out below:

Asset Class	**Strategic Allocation %**	**Allocation as at 31/03/14 %**
Equities	**60**	**63**
Bonds	**10**	**9**
Property	**10**	**7**
Alternatives	**20**	**19**
• *Private Equity*	*5*	*5*
• *Infrastructure*	*5*	*2*
• *Diversified Growth*	*10*	*12*
Cash	**-**	**2**

The Fund is holding a 2% allocation to cash in anticipation of making imminent investments in Social and Affordable Housing and in UK Infrastructure. These investments will help to address the current underweight positions of Property and Infrastructure respectively, with the first capital outlays on course for 2014/15.

The Fund has also initiated work to further analyse its cash position. Initial forecasts suggest that the Fund will be cash positive by around £20m p.a. for each of the next few years (i.e. pension contributions will outstrip pension benefits by that margin). The Fund plans to build on this analysis, incorporating the results of the 2014 valuation and the implementation of the CARE scheme, to produce longer term forecasts, including an estimate of when the Fund will become cash neutral or negative.

As mentioned above, 2014 will see the Fund undertake its triennial valuation. This will be accompanied by a re-assessment of the investment strategy to be undertaken with the assistance of the Fund's investment adviser. In the meantime the Fund will continue to monitor global market conditions and respond to potential opportunities/threats as they occur.

Investment Monitoring

Regulation 10 of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) 2010 (SSI 2010/233) requires the periodic monitoring and review of investment managers performance. In 2012 the Fund entered into a shared service agreement with City of Edinburgh Council (Lothian Pension Fund) to assist with this activity.

As part of the monitoring process, Officers from the Lothian and Falkirk Funds have regular meetings with external managers to discuss their individual performance, process and strategy. Details of each Managers' performance and comment on their activities is provided to the Pensions Panel and Committee at the quarterly meetings. This helps to ensure that appropriate oversight and control is exercised by the Fund.

Investment Performance

The Fund's total returns over the short, medium and long term are set out below.

Short Term (1 year)
The Fund earned a return of 6.9% surpassing its benchmark by 0.9%. Strong performances in developed markets, particularly the UK, were negated slightly by exposure to emerging markets.

Medium Term (3 years)
The Fund's return of 8.8% has outperformed its benchmark return by 2.2%. Over this period, the Fund benefited from a strong performance by its Bond and UK Equity managers.

Longer Term (10 years)
The Fund's longer term performance of 7.9% has slightly outperformed the benchmark return by 0.2% p.a. This remains just ahead of price and wage inflation to which the pension fund liabilities are linked.

Returns showing the rolling 3 yearly performance of the Fund for the past decade are shown overleaf in the graph on page 23.

Annualised returns to 31 March 2014

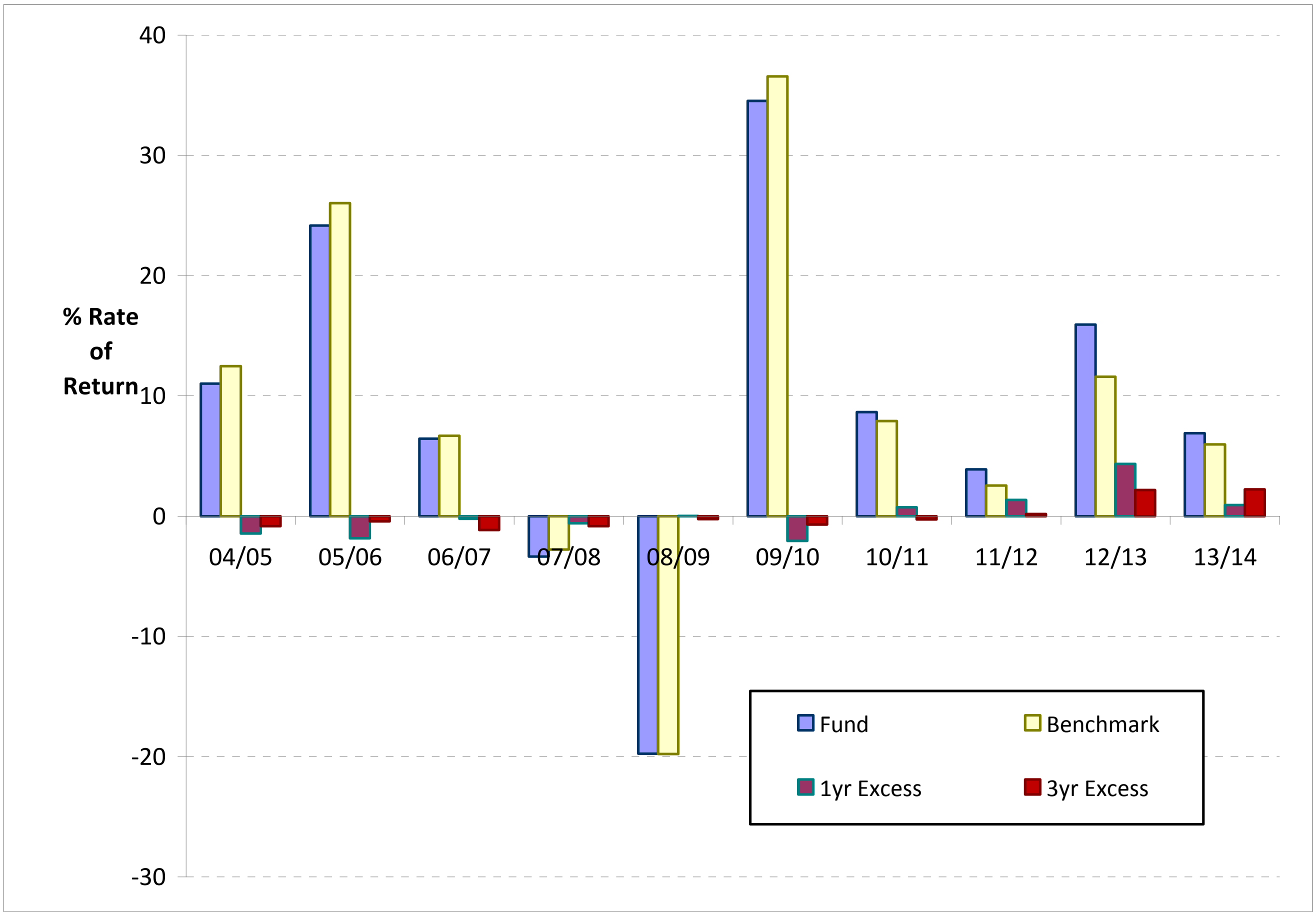
	1 Year	3 Years	10 Years
	%	%	%
Falkirk Council Pension Fund	6.9	8.8	7.9
Benchmark	6.0	6.6	7.7
Retail Prices Index	2.5	3.1	3.3
Consumer Price Index	1.7	2.6	2.7
National Average Earnings	3.0	1.3	2.8

Manager Returns

Individually, the Fund's investment managers had the following performance against benchmark over the financial year:

Investment Manager	Mandate	1 Year	Benchmark
		%	%
Aberdeen Asset Management	Global Equities	1.58	6.72
Baillie Gifford Life Ltd	Bonds	(0.61)	(0.85)
Baillie Gifford Life Ltd	Diversified Growth	1.63	0.5
Legal & General Investment Management Ltd.	Passive Equities	8.11	7.92
Newton Investment Management Ltd.	Global Equities	6.79	6.75
Schroder Investment Management Ltd.	UK Equities	17.91	8.81
Schroder Investment Management Ltd.	Property	10.26	11.87
Alternatives	Private Equity/ Infrastructure	2.09	0.35

Rolling 3 Years Performance
Annual periods ending 31st March including 1 year and rolling 3 years % excess returns



	Mar-05 %	Mar-06 %	Mar-07 %	Mar-08 %	Mar-09 %	Mar-10 %	Mar-11 %	Mar-12 %	Mar-13 %	Mar-14 %
Fund	11.02	24.18	6.46	-3.36	-19.75	34.53	8.65	3.91	15.94	6.89
Benchmark	12.47	26.03	6.7	-2.76	-19.77	36.57	7.92	2.55	11.59	5.96
1yr Excess	-1.45	-1.85	-0.23	-0.6	0.03	-2.04	0.73	1.36	4.35	0.93
3yr Excess	-0.84	-0.44	-1.14	-0.84	-0.25	-0.71	-0.28	0.19	2.16	2.23

Investment Holdings
The Fund's current 10 largest individual stock holdings are listed below -

Stock	Market Value as at 31st March 2014 (£)
VODAFONE GROUP ORD USD0.2095238	19,726,120.81
ASTRAZENECA ORD USD0.25	15,531,984.72
GLAXOSMITHKLINE ORD GBP0.25	15,484,884.80
ROYAL DUTCH SHELL 'B'ORD EUR0.07	15,086,769.38
ROCHE HLDGS AG GENUSSCHEINE NPV	14,324,114.22
BRITISH AMERICAN TOBACCO ORD GBP0.25	13,131,195.65
BP ORD USD0.25	12,820,147.20
NOVARTIS AG CHF0.50 (REGD)	12,242,653.19
NESTLE SA CHF0.10(REGD)	9,945,939.27
UNITED TECHNOLOGIES CORP COM	9,493,352.32

CORPORATE GOVERNANCE

As a responsible investor, the Fund seeks to promote corporate responsibility and good practice amongst all companies in which it invests. To this end, the Fund monitors investee companies to ensure they meet standards of acceptable practice in relation to their key stakeholders. During the year, the monitoring role was achieved by engaging with companies through:

- the Fund's Investment Managers (see note 18 to the financial statements, page 40);
- the Fund's Pensions and Investment Research Consultants (PIRC) who provide advice and research services on all matters pertaining to corporate governance and shareholder voting responsibilities; and
- the Fund's membership of the Local Authority Pension Fund Forum (LAPFF) comprising 58 local government pension funds which exists to promote and maximise investment interests of Funds.

The Fund could potentially allow managers to exercise votes on its behalf at company meetings, however in order to ensure a consistent approach to voting, it has for the past few years engaged PIRC to undertake this service through its Proxy Voting facility.

During 2013/14, PIRC voted at 135 company meetings with 1371 votes being cast in favour of resolutions, 362 being opposed and 155 being cases of abstentions. Areas where negative votes were cast related predominantly to companies remuneration policies though PIRC also took an active role in challenging policies on gender balance on boards, conflicts of interest, and auditor independence.

PIRC generally attend one Panel and one Committee meeting each year in order to brief members about the latest developments in corporate governance. An update on corporate governance matters is given to members at the quarterly Panel and Committee meetings.

The Fund's corporate governance responsibilities should also be considered within the context of the UK Stewardship Code. The Code comprises of seven principles which seek to improve the quality of engagement between institutional investors and investee companies. Under the seven principles, companies are required to:

1. publicly disclose their policy on how they will discharge their stewardship responsibilities.
2. have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed.
3. monitor their investee companies.
4. establish clear guidelines on when and how they will escalate their stewardship activities.
5. be willing to act collectively with other investors where appropriate.
6. have a clear policy on voting and disclosure of voting activity.
7. report periodically on their stewardship and voting activities.

Consistent with Code requirements, asset managers must produce a statement of their commitment or explain their alternative approach to company engagement. It is pleasing to note that each of the Fund's investment managers has expressed their commitment to the Code.

PENSION FUND ACCOUNT

This statement shows the revenue account of the Pension Fund and separates those transactions which are related to dealings with members from those transactions which are a consequence of investment.

2012/13 £'000	CONTRIBUTIONS AND BENEFITS	2013/14 £'000	Note
	Dealings with members, employers and others directly involved in the fund		
69,130	Contributions	76,433	8
4,383	Transfers from Other Pension Funds	3,316	9
73,513		79,749	
(52,729)	Benefits	(56,485)	10
(4,058)	Payments to and on account of leavers	(4,655)	11
(375)	Administrative and Other Expenses	(430)	12
(57,162)		(61,570)	
16,351	**Net Additions from dealing with Members**	18,179	
	RETURNS ON INVESTMENTS		
21,607	Investment Income	26,484	13
(229)	Taxes on Income	(268)	14
179,033	Profit and losses on disposal of investments and changes in market value of investments	75,301	16
(5,676)	Investment Management Expenses	(6,090)	15
194,735	**Net Return on Investments**	95,427	
211,086	**Net Increase/(Decrease) in the net assets available for benefits during the year**	113,606	
1,251,989	**Opening Net Assets as at 1 April 2013**	1,463,075	
1,463,075	**Closing Net Assets as at 31 March 2014**	1,576,681	

PENSION FUND NET ASSETS STATEMENT

This statement discloses the size and type of the net assets of the Fund at the end of the financial year.

2012/13 £'000		2013/14 £'000	Note
1,445,385	**INVESTMENT ASSETS**	1,575,496	16
(341)	**INVESTMENT LIABILITIES**	(7,601)	16
1,445,044		1,567,895	
	NON-CURRENT ASSETS		
1,611	Long Term Debtors	816	26
	CURRENT ASSETS		
12,419	Cash Balances	4,228	27
6,878	Debtors	6,735	28
	CURRENT LIABILITIES		
(2,877)	Creditors	(2,993)	29
1,463,075	**NET ASSETS OF THE FUND AVAILABLE TO FUND BENEFITS AT THE PERIOD END**	1,576,681	

The Fund's financial statements do not take account of liabilities to pay pensions and other benefits after the period end. The actuarial present value of promised retirement benefits is disclosed in Note 25.

The unaudited accounts were issued on 30 June 2014 and the audited accounts were authorised for issue by Bryan Smail, Chief Finance Officer on xx September 2014. The Statement of Accounts presents a true and fair view of the financial position of the Pension Fund as at 31 March 2014 and their income and expenditure for the year ended 31 March 2014.

Bryan Smail, CPFA MBA
Chief Finance Officer

NOTES TO THE ACCOUNTS

1. Fund and Scheme Overview

Introduction

As part of its statutory obligations, Falkirk Council is required to operate the terms of the Local Government Pension Scheme (LGPS), including the maintenance and administration of a pension fund.

The LGPS is a public sector statutory scheme which provides defined benefits on a final salary basis. The Scheme was established under the Superannuation Act 1972. It is also contracted-out of the State Second Pension and is registered with HM Revenue and Customs as a UK pension scheme.

The scheme rules are made by the Scottish Ministers through the office of the Scottish Public Pensions Agency and are primarily set out in the following statutory instruments:

- the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008;
- the Local Government Pension Scheme (Benefits, Membership and Contributions) (Scotland) Regulations 2008; and
- the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2010.

Administration of the Fund is undertaken by an in-house team who oversee the benefits of contributors, deferred members and pensioners on behalf of Clackmannanshire, Falkirk and Stirling Councils, as well as for around 35 other employers. Teachers, Police and Firefighters do not come within the scope of the LGPS as they have their own national pension arrangements. A full list of employers who participate in the Falkirk Council Pension Fund is included in this report on Page 55.

The investments of the Fund are overseen by a small in-house team and managed by external Fund Managers within the overall policy direction of the Council's Pensions Committee and advisory Pensions Panel. Support on investment matters is also provided through a service level agreement with the City of Edinburgh Council.

Membership

Membership of the LGPS is voluntary and, although employees may have been enrolled in the scheme automatically (either as a result of auto enrolment legislation or the Scheme's own contractual enrolment provisions), employees are free to choose whether to remain in the scheme or, having opted out, join it at a later date.

Organisations participating in the Scheme fall into two categories, namely:

Scheduled Bodies - organisations such as local authorities that are statutorily required to offer the Scheme to their employees; and

Admission Bodies - mainly charitable, non-profit making bodies that have reached an agreement with an Administering Authority to participate in the Scheme.

Around 40 employing bodies participate in the Falkirk Council Pension Fund. Full details of membership numbers are contained on Page 18 of the Annual Report.

Funding

Benefits are funded by contributions and returns on investments. Contributions are made by active members of the fund in accordance with the LGPS (Benefits, Membership and Contributions) (Scotland) Regulations 2008. The rate of employee contribution varies depending on a member's full time equivalent pensionable pay with designated pay bands attracting rates of between 5.5% and 12%.

Employee Contributions are matched by employer contributions which are based on the results of the three yearly actuarial funding valuation. The last such valuation was at 31st March, 2011. For the majority of fund employers in 2013/14, contribution rates were in the range 17% – 22% of pensionable pay. Full details of employer contribution rates can be found in the Valuation Report at www.falkirkpensionfund.org.

Benefits

Benefits under the LGPS are based on final pensionable pay and length of pensionable service, and are summarised below:

	Service pre 1 April 2009	Service post 31 March 2009
Pension	Each year worked is worth 1/80th x final pensionable salary	Each year worked is worth 1/60th x final pensionable salary
Lump Sum	Automatic lump sum of 3 x annual pension In addition, part of the pension may be exchanged for a lump sum. The conversion rate is £12 of lump sum for each £1 surrendered.	No automatic lump sum Part of the pension may be exchanged for a lump sum. The conversion rate is £12 of lump sum for each £1 surrendered.
	The lump sum cannot be greater than 25% of the capital value of the pre 2009 and post 2009 pension rights.	

Additionally, the Scheme provides a range of inflation proofed benefits including early payment of pension and lump sum on ill health or redundancy grounds, as well as death and survivor benefits.

The measure of inflation currently used by the Scheme in determining annual increases is the Consumer Price Index. Prior to April, 2010, the measure used was the Retail Price Index.

More information about scheme benefits can be found in the Member's Handbook which is accessible at www.falkirkpensionfund.org.

LGPS 2015

The Public Service Pensions Act 2013 requires that certain changes are made to public sector pension schemes by 1st April, 2015. The main changes affecting the LGPS are as follows:

- Scheme will operate on Career Average Re-valued Earnings (CARE) basis;
- Normal Retirement Age will be aligned with each member's own State Pension Age;
- Membership rights up to 31st March, 2015 will be protected on Final Salary basis;
- Transitional protection will exist for those closest to retirement; and
- The Scheme will have a national Advisory Board and local Pension Boards.

New regulations setting out details of LGPS 2015 were laid in June, 2014. Transitional and Governance regulations are expected to follow later in 2014.

2. Prior Year Adjustment

During the year, the Fund has changed its accounting policy in two areas such that a restatement of the 2012/13 results is required.

The first policy change relates to the treatment of balances due to brokers at year end. Previously a net figure was used and recognised within Other Investment balances. The new treatment recognises balances to/from brokers and this has impacted on both the Fund's assets and liabilities.

	2012/13 Restated Balance	Adjustment
	£'000	£'000
Investment Assets	1,445,385	283
Investment Liabilities	(341)	(283)

The second policy change relates to the treatment of direct management expenses arising from the Fund's Alternative investments. Previously due to the complex nature of Private Equity and Infrastructure investments, management fees were rolled up within the investment and so would flow through as a loss on investment. The accounting treatment has been revised to recognise direct expenses relating to the management of these funds and include them within Investment Management Expenses. This has increased the Fund's Profit and loss on disposal as well as its Investment Management Expenses.

	2012/13 Restated Balance	Adjustment
	£'000	£'000
Profit and losses on disposal of investments and changes in market value of investments	179,033	1,558
Investment management expenses	(5,676)	(1,558)

3. Basis of Preparation

The Statement of Accounts summarises the Fund's transactions for the 2013/14 financial year and its financial position as at the year end of 31 March 2014. The accounts also report on the net assets available to pay pension benefits.

The accounts have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 which is based upon International Financial Reporting Standards (IFRS), as amended for the UK public sector.

The accounts do not take account of obligations to pay pensions and benefits which fall due after the end of the financial year. The actuarial present value of promised retirement benefits, valued on an International Accounting Standard (IAS) 19 basis is disclosed at Note 25 of these accounts.

Amendments to accounting standard IAS 32 came into effect in January 2014 and changes to IFRS 13 come into effect in July 2014. Neither will have any effect on the Fund as it is already in compliance with the requirements.

4. Summary of Significant Accounting Policies

Fund account - revenue recognition

a) Contribution income

Normal contributions, both from the members and from employers, are accounted for on an accruals basis. Employer contributions are made at the percentage rate recommended by the Fund Actuary in the payroll period to which they relate. Employee contributions are made in accordance with the rates specified in the Scheme rules.

Employers’ augmentation contributions and pension strain contributions are accounted for in the period in which the liability arises.

Any amount due in year but unpaid will be classed as a current financial asset. Amounts not due to be paid until future years are classed as long-term financial assets.

b) Transfers to and from other schemes

Transfer values represent the amounts received and paid during the year for members who have either joined or left the fund and are calculated in accordance with guidance from the Government Actuary. Individual transfers in/out are accounted for when received/paid, which is normally when the member liability is accepted or discharged.

Transfers in from members wishing to use the proceeds of their additional voluntary contributions to purchase scheme benefits are accounted for on a receipts basis and are included in Transfers In.

c) Investment income

i) Interest income

Interest income is recognised in the fund account as it accrues, using the effective interest rate of the financial instrument as at the date of acquisition or origination. Income includes the amortisation of any discount or premium, transaction costs or other differences between the initial carrying amount of the instrument and its amount at maturity calculated on an effective interest rate basis.

ii) Dividend income

Dividend income is recognised on the date the shares are quoted ex-dividend. Any amount not received by the end of the reporting period is disclosed in the net assets statement as a current financial asset.

iii) Distributions from pooled funds

Distributions from pooled funds are recognised at the date of issue. Any amount not received by the end of the reporting period is disclosed in the net assets statement as a current financial asset.

iv) Property related income

Property-related income consists primarily of rental income.

Rental income from operating leases on properties owned by the fund is recognised on a straight-line basis over the term of the lease. Any lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

Contingent rents based on the future amount of a factor that changes other than with the passage of time, such as turnover rents, are only recognised when contractually due.

v) Movement in the net market value of investments

Changes in the net market value of investments (including investment properties) are recognised as income and comprise all realised and unrealised profits/losses during the year.

Fund account - expense items

d) Benefits payable

Pensions and lump sum benefits payable include all amounts known to be due as at the end of the financial year. Any amounts due but unpaid are disclosed in the net assets statement as current liabilities.

e) 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 is accounted for as a fund expense as it arises.

f) Administrative expenses

All administration expenses are accounted for on an accruals basis. Costs directly related to Fund activities are being charged to the Fund during the financial year. Costs which relate to both Fund and Non-Fund activities are apportioned between the Fund and the sponsors of the other pension arrangements administered by the Pensions Section. Any apportionment is carried out on the basis of share of aggregate membership numbers.

g) Investment management expenses

All investment management expenses are accounted for on an accruals basis.

Fees of the external investment managers and custodian are agreed in the respective mandates governing their appointments. Broadly, these are based on the market value of the investments under their management and therefore increase or reduce as the value of these investments change.

The cost of obtaining external investment advice and the fee in respect of the shared service agreement with City of Edinburgh Council (Lothian Pension Fund) is included in investment management charges.

The costs of the in-house investment administration team are charged to the Fund. The basis of allocation is as per the administration expenses described above.

Net assets statement

h) Financial assets

Financial assets are included in the net assets statement on a fair value basis as at the reporting date. A financial asset is recognised in the net assets statement on the date the fund becomes party to the contractual acquisition of the asset. From this date any gains or losses arising from changes in the fair value of asset are recognised by the fund.

The values of investments as shown in the net assets statement have been determined as follows:

i) Market quoted investments

The value of an investment for which there is a readily available market price is determined by the bid market price ruling on the final day of the accounting period.

ii) Unquoted investments

The fair value of investments for which market quotations are not readily available is determined as follows:

- valuations of delisted securities are based on the last sale price prior to delisting, or where subject to liquidation, the amount the Council expects to receive on wind-up, less estimated realisation costs
- securities subject to takeover offer – the value of the consideration offered under the offer, less estimated realisation costs
- directly held investments include investments in limited partnerships, shares in unlisted companies, trusts and bonds. Other unquoted securities typically include pooled investments in property, infrastructure, debt securities and private equity. The valuation of these pools or directly held securities is undertaken by the investment manager or responsible entity and advised as a unit or security price. The valuation standards followed in these valuations adhere to industry guidelines or to standards set by the constituent documents of the pool or the management agreement.
- investments in unquoted property and infrastructure pooled funds are valued at the net asset value or a single price advised by the fund manager
- the values of the investments in unlisted private equity and infrastructure are based on valuations provided by the general partners to the funds in which the Fund has invested. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of IFRS. The valuations are usually undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

iii) Pooled investment vehicles

Pooled investment vehicles are valued at closing bid price if both bid and offer prices are published; or if single priced, at the closing single price. In the case of pooled investment vehicles that are accumulation funds, change in market value also includes income which is reinvested in the fund, net of applicable withholding tax.

iv) Freehold and leasehold properties
The Fund's direct property holding was valued at 31 March 2014 by DM Hall LLP, Chartered Surveyors, in accordance with the requirements of the RICS Valuation Standards 6th edition. This valuation is completed every 3 years, with the next due 31 March 2017. The valuer's opinion of market value and existing use value was primarily derived using comparable recent market transactions on arms-length terms at the time of the valuation.

i) Foreign currency transactions and balances

Dividends, interest and purchases and sales of investments in foreign currencies have been accounted for at the spot market rates at the date of transaction. End-of-year spot market exchange rates are used to value a) cash balances held in foreign currency bank accounts, b) market values of overseas investments and c) purchases and sales outstanding at the end of the reporting period.

j) Derivatives

Derivative contract assets are fair valued at bid prices. Derivative contract liabilities are fair valued at offer prices. Changes in the fair value of derivative contracts are reflected within the change in market value in the net assets statements.

The value of futures contracts is determined using exchange prices at the reporting date. Amounts due from or owed to the broker are the amounts outstanding in respect of the initial margin and variation margin.

The future value of forward currency contracts is based on market forward exchange rates at the year-end date and determined as the gain or loss that would arise if the outstanding contract were matched at the year-end with an equal and opposite contract.

k) 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 and that are subject to minimal risk of changes in value.

l) 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.

m) Actuarial present value of promised retirement benefits

The actuarial present value of promised retirement benefits of the Fund is assessed on an annual basis by the Fund Actuary in accordance with the requirements of IAS 19 and relevant actuarial standards. As permitted under IAS 26, the Fund has opted to disclose the actuarial present value of promised retirement benefits by way of a note to the net assets statements.

n) Additional voluntary contributions

The Fund provides an additional voluntary contributions (AVC) scheme for its members, the assets of which are invested separately from those of the Fund. The Fund has appointed Standard Life as its AVC provider. AVCs are paid to Standard Life by employers and are specifically for providing additional benefits for individual contributors. Each AVC contributor receives an annual statement showing the amount held in their account and the movements in the year. (n.b. Prudential have been appointed as joint AVC providers with Standard Life from June 2014).

In accordance with regulation 4(2)(b) of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010, AVCs are not included in the pension fund financial statements. Details of contributions paid and the total value of funds invested are disclosed in Note 30 on page 51.

5. Critical Judgement in Applying Accounting Policies

In applying its accounting policies, the Fund has had to make certain judgements about complex transactions or those involving uncertainty about future events. The critical judgements made in the statement of accounts are:

i) Unquoted Investments

It should be recognised that determining the fair value of private equity and infrastructure investments is highly subjective. Inherently, valuations are based on forward-looking estimates and judgements made on a variety of factors. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of IFRS.

At 31 March 2014 the Fund had a value of £117.1m (2013 £113.8m) invested in unquoted private equity and infrastructure funds.

(ii) Actuarial present value of promised retirement benefits

Each Fund is required to disclose the estimated actuarial present value of promised retirement benefits as at the end of the financial year. These estimates are prepared by the Fund's Actuary. Values are calculated in line with IAS19 assumptions and comply with the requirements of IAS26. However, the results are subject to significant variances based on changes to the underlying assumptions.

6. Assumptions made about the future and other major sources of estimation uncertainty

The Statement of Accounts contains estimated figures that are based on assumptions about the future or circumstances that are otherwise uncertain. The assumptions are made by the Council, by private equity and infrastructure managers, by the Fund Actuary and by other financial information providers. Estimates are made taking into account historical experience, current trends and other relevant factors. However, because balances cannot be determined with certainty, actual results could be materially different from the assumptions and estimates.

(i) Unquoted Investments

The Fund’s asset allocation to Private Equity and Infrastructure exposes it to investments that are not publicly listed. Valuations for these assets will contain an element of estimation in their production.

There is a risk that these investments may be under or overstated in the accounts.

(ii) Actuarial present value of promised retirement benefits

Estimation of the net liability to pay pensions depends on a number of complex judgements relating to the discount rate used, the rate at which salaries are projected to increase, changes in inflation, retirement ages, mortality rates and expected returns on pension fund assets. The Fund’s actuary provides expert advice on the assumptions used to produce the estimated valuation presented in the Notes to the Accounts.

The table below highlights the approximate impact that a small change in the assumptions used would have on the liability of the Fund.

Change in assumptions at year ended 31 March 2014	Approximate % increase to liabilities	Approximate monetary amount (£m)
0.5% decrease in Real Discount Rate	10%	228
1 year increase in member life expectancy	3%	68
0.5% increase in the Salary Increase Rate	3%	68
0.5% increase in the Pension Increase Rate	7%	160

7. Events after the Balance Sheet Date

The unaudited Statement of Accounts were issued by the Chief Finance Officer on 30 June 2014 and the audited Statement of Accounts were authorised for issue on xx September 2014. Events taking place after this date are not reflected in the financial statements or notes. There have been no material events since the date of the Net Asset Statement which have required the figures in the financial statements and notes to be adjusted.

8. Contribution Receivable

By Category

2012/13 £'000		2013/14 £'000
50,063	Employers – Normal/deficit Contributions	54,432
2,481	Employers – Strain Contributions	4,552
16,586	Members	17,449
69,130	TOTAL	76,433

By Authority

2012/13			2013/14	
Members £'000	Employers £'000		Members £'000	Employers £'000
5,442	17,650	Administering Authority	5,978	19,690
9,447	29,270	Other Scheduled Bodies	9,721	33,195
1,697	5,624	Admission Bodies	1,750	6,099
16,586	52,544	TOTAL	17,449	58,984

9. Transfers from Other Pension Funds

All transfers during the year related to individual transfer payments and not to bulk transfer payments.

10. Benefits Payable

By Category

2012/13 £'000		2013/14 £'000
(39,651)	Pensions	(42,038)
(10,915)	Commutation and lump sum retirement benefits	(12,919)
(2,163)	Lump sum death benefits	(1,528)
(52,729)	TOTAL	(56,485)

By Authority

2012/13			2013/14	
Pensions £'000	Lump Sum* £'000		Pensions £'000	Lump Sum* £'000
(13,555)	(4,655)	Administering Authority	(15,452)	(4,343)
(24,263)	(7,324)	Other Scheduled Bodies	(23,272)	(9,359)
(1,833)	(1,099)	Admission Bodies	(3,314)	(745)
(39,651)	(13,078)	TOTAL	(42,038)	(14,447)

* Lump Sum includes Death Benefits

11. Payments to and on account of leavers

2012/13 £'000		2013/14 £'000
(137)	Refunds to members leaving service	(151)
(3,921)	Individual transfers	(4,504)
(4,058)	TOTAL	(4,655)

12. Administration Expenses

2012/13 £'000		2013/14 £'000
(319)	Administration Costs	(351)
(23)	Actuarial Fees	(55)
(22)	External Audit	(22)
(11)	Fees and Subscriptions	(2)
(375)	TOTAL	(430)

13. Investment Income

2012/13 £'000		2013/14 £'000
9,764	UK Equities	11,293
125	UK Pooled Equities	180
3,037	UK Managed Funds – Property	3,357
7,841	Overseas Equities	8,206
187	Overseas Managed Funds – Property	372
-	UK Private Equity	1,551
351	Overseas Private Equity	1,215
-	Overseas Infrastructure	21
206	UK Property	183
96	Cash & Other Income	106
21,607	TOTAL	26,484

14. Taxes on Income

All tax withheld on income for the Fund relates to equity investments.

15. Investment Management Expenses

2012/13 £'000		2013/14 £'000
(5,433)	External Investment Management Services	(5,757)
(98)	Custodian	(97)
(98)	Internal Administration	(99)
(11)	Performance Monitoring	(14)
(36)	Actuarial Fees – Investment Consultancy	(123)
(5,676)	TOTAL	(6,090)

These expenses cover all investment fees directly chargeable to the Fund. The Fund is exposed to a dual layer of fees in some of its more complex investments. These indirect fees are estimated to be £3.1m (£3.0m 2012/13) and are not included in the above figures.

16. Investments

Market Value 31/03/13 £'000	INVESTMENT ASSETS	Market Value 31/03/14 £'000
	Listed Investments	
599,593	Equities	613,587
578,486	Pooled Investments	665,055
92,734	Managed Property Funds	109,735
113,762	Private Equity/Infrastructure	117,095
2,300	Property (West Mains)	2,300
243	Derivatives – Forward Foreign Exchange	-
-	- Futures Contract	33
	Cash Deposits	
8,376	Other Balances	16,164
46,536	Deposits	41,576
	Other Investment Balances	
3,296	Debtors – Investment Income Due	2,962
59	– Due from Broker	6,989
1,445,385	**Total Investment Assets**	**1,575,496**
	INVESTMENT LIABILITIES	
(58)	Derivatives – Forward Foreign Exchange	(44)
(283)	Creditor – Due to Broker	(7,557)
(341)	**Total Investment Liabilities**	(7,601)
1,445,044	**NET INVESTMENT ASSETS**	**1,567,895**

16b. Analysis of Investments (excluding derivative contracts)

31/03/13 £'000		31/03/14 £'000
	Equities	
262,331	UK	270,001
337,262	Overseas	343,586
599,593		**613,587**
	Pooled Funds	
120,886	Equities – UK	131,425
193,999	- Overseas	209,037
136,088	Bonds - UK	124,154
-	- Overseas	10,943
127,513	Diversified Growth	189,496
578,486		**665,055**
	Property	
83,821	Managed Fund – UK	102,554
8,913	- Overseas	7,181
2,300	Direct UK (West Mains)	2,300
95,034		**112,035**
	Private Equity	
55,458	UK	56,558
29,970	Overseas	26,729
85,428		**83,287**
	Infrastructure	
28,334	Overseas	33,808
1,386,875		**1,507,772**

INVESTMENT ASSETS	Market Value 01/04/13 £'000	Purchases at Cost £'000	Sale Proceeds £'000	Change in Market Value £'000	Market Value 31/03/14 £'000
Equities	599,593	173,147	(200,699)	41,546	613,587
Pooled Investments	578,486	67,816	(15,737)	34,490	665,055
Managed Property Funds	92,734	13,367	(1,984)	5,618	109,735
Private Equity/Infrastructure	113,762	20,144	(18,266)	1,455	117,095
Property (West Mains)	2,300	-	-	-	2,300
Derivatives					
- Exchange Traded Futures	-	639	-	(606)	33
- Forward Foreign Exchange	185	429	(299)	(359)	(44)
	1,387,060	275,542	(236,985)	82,144	1,507,761
Other Balances	8,376	65,825	(56,532)	(1,505)	16,164
Deposits	46,536	-	-	(5,338)	41,576
Broker Balance	(224)	-	-	-	(568)
Investment Income Due	3,296	-	-	-	2,962
NET INVESTMENT ASSETS	**1,445,044**	**341,367**	**(293,517)**	**75,301**	**1,567,895**

Transaction costs are included in the cost of purchases and sale proceeds. Transaction costs include costs charged directly to the scheme such as fees, commissions and stamp duty. Transaction costs incurred during 2013/14 amounted to £629,981 (2012/13 £504,609). In addition to the transaction costs disclosed above, indirect costs are incurred through the bid-offer spread on investments within pooled investment vehicles. The amount of indirect costs is not separately provided to the scheme.

INVESTMENT ASSETS	Market Value 01/04/12 £'000	Purchases at Cost £'000	Sale Proceeds £'000	Change in Market Value £'000	Market Value 31/03/13 £'000
Equities	498,232	122,263	(102,472)	81,570	599,593
Pooled Investments	497,165	5,057	(141)	76,405	578,486
Managed Property Funds	94,919	6,225	(6,331)	(2,079)	92,734
Private Equity/Infrastructure	97,199	25,326	(13,875)	5,112	113,762
Property (West Mains)	2,300	-	-	-	2,300
Derivatives					
– Forward Foreign Exchange	251	710	(1,702)	926	185
	1,190,066	159,581	(124,521)	161,934	1,387,060
Other Balances	7,385	47,727	(47,605)	869	8,376
Deposits	32,833	-	-	16,230	46,536
Broker Balance	(711)	-	-	-	(224)
Investment Income Due	2,931	-	-	-	3,296
NET INVESTMENT ASSETS	**1,232,504**	**207,308**	**(172,126)**	**179,033**	**1,445,044**

The Fund holds the following investments in pooled funds, which are in excess of 5% of the value of the Fund.

31 March 2013			31 March 2014	
£'000	%		£'000	%
127,512	8.8	Baillie Gifford Diversified Growth	189,496	12.1
108,895	7.6	L&G – UK Equity Index	118,426	7.6
105,915	7.3	L&G – North American Equity Index	112,624	7.3
82,381	5.7	Baillie Gifford Sterling Aggregate Bonds	82,263	5.3

Regulation 14 of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) 2010 (SSI 2010/233) places limits on the investments LGPS Funds can make. For example, restrictions are placed on the percentage of unlisted securities that the Fund can hold and the percentage that can be invested in one stock (i.e. 10% is the maximum). Although the Fund does hold a stock over 10% of the Fund value, this is allowed under regulation due to it being a unitised trust.

17. Securities Lending

The Fund did not participate in any stock lending programmes managed by its global custodian, Northern Trust.

18. Funds Under Management

MARKET VALUE 31 March 2013			MARKET VALUE 31 March 2014	
£ million	(%)		£ million	(%)
208.6	14.5	Aberdeen Asset Management	212.0	13.5
136.1	9.4	Baillie Gifford Life Ltd.	135.1	8.6
127.5	8.8	Baillie Gifford Life Ltd – Diversified Growth	189.5	12.1
302.8	21.1	Legal and General Investment Management Ltd.	327.5	20.9
213.0	14.8	Newton Investment Management Ltd.	227.5	14.5
226.3	15.7	Schroder Investment Management Ltd.	223.8	14.3
100.2	6.9	Schroder Investment Management Ltd. (Property)	110.5	7.1
43.6	3.0	SL Capital Partners LLP	43.1	2.8
30.0	2.1	Wilshire Private Markets Group	26.7	1.7
12.0	0.8	M&G UK Companies	13.4	0.9
28.3	1.9	Credit Suisse Securities	33.8	2.2
14.4	1.0	In House Cash	22.7	1.4
1,442.8	100.0	TOTAL	1,565.6	100.0

19. Derivatives

The Fund's approach to derivatives is to allow individual managers to decide to participate in derivative contracts subject to any limits set out in their investment management agreements. At present, only Newton chooses to do so, with derivatives making up 0.005% of their portfolio's value.

(a) Derivatives – Exchange Traded Futures Contracts

Summary of Contracts held at 31 March 2014

Contract	Settlement Date	Value of Currency Bought £'000	Market Value £'000
Overseas Equity	Within 1 Month	110	33

(b) Derivatives – Forward Foreign Exchange

Summary of Contracts held at 31 March 2014

Contract	Settlement Date	Value of Currency Bought £'000	Asset £'000	Liability £'000	Net £'000
Various Currency Forwards	Within 1 month	4,826	-	(44)	(44)

Summary of Contracts held at 31 March 2013

Contract	Settlement Date	Value of Currency Bought £'000	Asset £'000	Liability £'000	Net £'000
Various Currency Forwards	Within 1 month	12,832	101	(58)	43
Various Currency Forwards	Within 2 months	5,546	142	-	142

The above contracts are used as hedges reducing the extent to which Newton's portfolio is exposed to currency movement. Three foreign currencies are involved in this hedge and contracts are traded on an over-the-counter basis.

20. 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 fair value amounts of financial assets and liabilities by category and net assets statement heading. No financial assets were reclassified during the accounting period.

All financial instruments are marked to market (at fair value) in the Fund's accounting records, hence there is no difference between the carrying value and fair value.

31 March 2013 Designated as fair value through net asset statement £'000	Loans and receivables £'000	Financial liabilities at amortised cost £'000	FINANCIAL ASSETS	31 March 2014 Designated as fair value through net asset statement £'000	Loans and receivables £'000	Financial liabilities at amortised cost £'000
			Investment assets			
599,593	-	-	Equities	613,587	-	-
578,489	-	-	Pooled investments	665,055	-	-
92,734	-	-	Property	109,735	-	-
113,759	-	-	Private Equity/Infrastructure	117,095	-	-
243	-	-	Derivative contracts	33	-	-
-	54,912	-	Cash		57,740	-
-	3,355		Other investment balances		9,951	-
1,384,818	58,267	-		1,505,505	67,691	-
			Other assets			
-	12,419	-	Cash Balances	-	4,228	-
-	8,489		Debtors	-	7,551	-
-	20,908	-		-	11,779	-
1,384,818	79,175	-	**ASSETS TOTAL**	1,505,505	79,470	-
			FINANCIAL LIABILITIES			
			Investment liabilities			
(58)	-	-	Derivative contracts	(44)	-	-
(283)	-	-	Other Investment balances	(7,557)	-	-
			Other liabilities			
-	-	(2,877)	Creditors	-	-	(2,993)
(341)	-	(2,877)	**LIABILITIES TOTAL**	(7,601)	-	(2,993)
1,384,477	79,175	(2,877)		1,497,904	79,470	(2,993)

31 March 2013		31 March 2014
1,460,775	**Total net financial instruments**	1,574,381
2,300	Amounts not classified as financial instruments	2,300
1,463,075	**Total net assets**	1,576,681

21. Net Gains and Losses on Financial Instruments

31 March 2013 £'000		31 March 2014 £'000
161,934	Designated as fair value through net asset statement	82,144
17,099	Loans and receivables	(6,843)
-	Financial liabilities at amortised cost	-
179,033	Net gains and losses on financial instruments	75,301
-	Gains and losses on directly held freehold property	-
179,033	Change in market value of investments per fund account	75,301

22. Valuation of Financial Instruments Carried at Fair Value

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

Level 1
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 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 equity investments, which are valued using various valuation techniques that require significant judgement in determining appropriate assumptions.

The values of the investments in private equity are based on valuations provided by the general partners to the private equity funds in which the Fund has invested. These valuations are prepared in accordance with the International Private Equity and Venture Capital Valuation Guidelines or similar guidelines provided by the British Venture Capital Association, which follow the valuation principles of IFRS. Valuations are usually undertaken annually at the end of December. Cash flow adjustments are used to roll forward the valuations to 31 March as appropriate.

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

As at 31 March 2014

FINANCIAL ASSETS	Quoted market price Level 1 £'000	Using observable inputs Level 2 £'000	With significant unobservable inputs Level 3 £'000	Total at 31 March 2014 £'000
Designated as fair value through net asset statement	1,143,578	244,835	117,092	1,505,505
Loans and receivables	79,470	-	-	79,470
Total Financial Assets	1,223,048	244,835	117,092	1,584,975
FINANCIAL LIABILITIES				
Designated as fair value through net asset statement	(7,601)	-	-	(7,601)
Financial liabilities at amortised cost	(2,993)	-	-	(2,993)
Total Financial Liabilities	(10,594)	-	-	(10,594)
NET FINANCIAL ASSETS	1,212,454	244,835	117,092	1,574,381

As at 31 March 2013

FINANCIAL ASSETS	Quoted market price Level 1 £'000	Using observable inputs Level 2 £'000	With significant unobservable inputs Level 3 £'000	Total at 31 March 2013 £'000
Designated as fair value through net asset statement	1,042,234	228,825	113,759	1,384,818
Loans and receivables	79,175	-	-	79,175
Total Financial Assets	1,121,409	228,825	113,759	1,463,993
FINANCIAL LIABILITIES				
Designated as fair value through net asset statement	(341)	-	-	(341)
Financial liabilities at amortised cost	(2,877)	-	-	(2,877)
Total Financial Liabilities	(3,218)	-	-	(3,218)
NET FINANCIAL ASSETS	1,118,191	228,825	113,759	1,460,775

23. Nature and Extent of Risks Arising from Financial Instruments

Risk and Risk Management

The Fund's primary long-term risk is that its assets will fall short of its liabilities (i.e. promised benefits payable to members). Therefore the aim of investment risk management is to minimise the risk of an overall reduction in the value of the Fund and to maximise the opportunity for gains across the whole portfolio. The Fund achieves this through asset diversification to reduce market risk (as quantified below) and credit risk to an acceptable level. In addition the Fund manages its liquidity risk to ensure there is sufficient liquidity to meet future cashflows. Responsibility for the Fund's risk management strategy rests with the Pensions Committee. Risk management policies are reviewed on a consistent basis to reflect changes in activity and in market condition.

Types of Investment Risk

Fluctuations in overall price can arise from a variety of sources including market risk, foreign exchange risk, interest rate risk and credit risk. Each of these vary in importance and will not by themselves account for the overall pricing risk faced. To some extent they may offset each other. The Fund's analysis combines these factors when looking at the total market price risk.

(i) **Market Risk**

Market risk is the risk of loss from fluctuations in equity and other asset prices, interest and foreign exchange rates and credit spreads. 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 as it relates to investments is to identify, manage and control market risk exposure within acceptable parameters, whilst optimising the return on assets. Investment risk is considered further in the Fund's Statement of Investment Principles.

In general, excessive volatility in market risk is managed by engaging a range of Fund Managers with differing approaches and philosophies and also through the diversification of the portfolio in terms of geographical and industry sectors and individual securities. To mitigate market risk, the Council and its investment advisors undertake appropriate monitoring of market conditions and benchmark analysis.

The Fund's approach to managing risk can be described in two fundamental ways:

- by maintaining asset class exposures such that risk remains within tolerable levels; and
- by applying maximum exposures to individual investments.

(ii) **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 recognised by the Council and its investment advisors. The Fund monitors the interest rate risk faced and will adjust its strategy in accordance with its Statement of Investment Principles. The Fund's direct exposure to interest rate movement as at the 31 March 2014 is estimated to be around £340m.

(iii) **Currency Risk**

Currency risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Fund is exposed to currency risk on financial instruments that are denominated in any currency other than the functional currency of the Fund (£UK). The Fund holds both monetary and non-monetary assets denominated in currencies other than £UK.

The Fund's currency rate risk is recognised by the Council and its investment advisors. In respect of cash deposits managed internally under the terms of the Cash Management Strategy, it is the Fund's policy to convert all non GBP monies to Sterling at the end of a month to reduce the currency risk faced. In respect of cash held with external Fund Managers, it is left to their discretion as to whether they wish to hedge their currency position or not.

The Fund's currency exposure as at the 31 March 2014 is estimated to be around £792m.

(iv) **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 assets and liabilities (as outlined in Market Risk above).

In essence, the Fund's entire investment portfolio is exposed to some sort of credit risk. However the selection of high quality counterparties, brokers and financial institutions minimises credit risk that may occur through the failure to settle a transaction in a timely manner. The Fund has had no experience of default or uncollected deposits over the past five financial years.

The main area where risk is not reflected in a market price is cash deposits which at 31 March 2014 accounted for 2.9% of fund assets.

Balances at 31 March 2013 £'000		**Moody's Credit Rating**	**Balances at 31 March 2014 £'000**
	Held for Investment Purposes		
17,326	Northern Trust Global Investment Limited – Liquidity Funds	Aaa-mf	12,400
-	Ignis Asset Management Sterling Liquidity Fund	AAAmmf (Fitch)	4,953
29,210	Northern Trust Company – Cash Deposits	A1	14,223
-	Santander UK PLC	A2	5,000
-	Bank of Scotland PLC	A1	5,000
46,536	Total Investment Cash		41,576
	Held for Other Purposes		
8,189	Clydesdale Bank	Baa2	3,927
54,725	Total Cash		45,503

As part of its approach to managing credit risk, the Fund formalised its Treasury operations during 2013/14 through the implementation of a Cash Management Strategy. This details:

- the counterparties with whom the Fund may have dealings;
- the credit ratings that are deemed acceptable; and
- specific limits and conditions attaching to certain types of deposit.

The credit rating used above is Moody's Long Term Outlook.

Despite its credit rating, the Fund (along with Falkirk Council) continues to use the Clydesdale Bank for its day to day transactional banking operations. Balances, are however, closely monitored and minimised to a level of around £3m.

(v) **Liquidity Risk**

Liquidity risk reflects the risk that the Fund will not be able to meet its financial obligations as they fall due. The Council in its capacity as Administering Authority therefore ensures that the Pension Fund has adequate cash and liquid resources to meet its commitments. The Fund currently does not have access to an overdraft facility for short term cash needs. As part of the ongoing monitoring of the Fund's banking arrangements this position may be reviewed and amended accordingly.

A majority of the Fund's investment assets (estimated to be over 85%) could be converted into cash within three months in normal market conditions.

(vi) **Refinancing Risk**

Refinancing risk is the risk that the Fund will be bound to replenish a significant proportion of its Pension Fund financial instruments at a time of unfavourable interest rates. The Fund is not bound by any obligation to replenish its investments. In any event, the Fund does not have any financial instruments that have a refinancing risk as part of its Pension Fund management and investment strategies.

Sensitivity Analysis

The Fund's valuation is sensitive to fluctuations in its Asset prices. The level of these fluctuations is known as "volatility" and will differ between asset classes. By analysing historical data, it is possible to gain an indication of the likely volatility of certain asset classes. In consultation with KPMG and Lothian Pension Fund, the following analysis predicts the likely annual volatility of the Fund's assets.

Asset Type	Potential price movement (+ or -)
Equities – Developed Markets	20.0%
Equities – Emerging Markets	30.0%
Private Equity	30.0%
Commodities	30.0%
Property – Balanced	13.0%
Property – Infrastructure	8.0%
Diversified Credit	10.0%
Fixed Interest Gilts	10.5%
Index-Linked Gilts	8.5%
Cash	1.5%

Volatility is measured as the standard deviation of annual returns. Broadly speaking, in two years out of three, the asset's change in value (which could be a gain or a loss) is expected to be lower than the volatility figure, but in one year out of three, the change in value is expected to be higher than the volatility figure.

Asset classes don't always move in line with each other. The extent to which assets move together is known as their "correlation". A lower correlation means that there is less risk of assets losing value at the same time. The overall Fund benefits from "diversification" because it invests in numerous different asset classes, which don't all move in line with each other. Consequently, the aggregate risk at the Fund level is less than the total risk from all the individual assets in which the Fund invests. The following table shows the risks at the asset class level and the overall Fund level.

Position as at 31 March 2014

Asset Type	Value at 31 March 2014 £'m	Asset Weight	Volatility	Potential Change =/- £'m	Value on increase £'m	Value on decrease £'m
Equities - Developed Markets	951.3	60.7%	20.0%	190.3	1,141.6	761.0
Equities - Emerging Markets	31.1	2.0%	30.0%	9.3	40.4	21.8
Private Equity	75.2	4.8%	30.0%	22.6	97.8	52.6
Commodities	13.1	0.8%	30.0%	3.9	17.0	9.2
Property	116.0	7.4%	13.0%	15.1	131.1	100.9
Infrastructure	41.4	2.6%	8.0%	3.3	44.7	38.1
Diversified Credit	162.7	10.4%	10.0%	16.3	179.0	146.4
Fixed Interest Gilts	63.5	4%	10.5%	6.7	70.2	56.8
Index-Linked Gilts	32.6	2.1%	8.5%	2.8	35.4	29.8
Cash	81.0	5.2%	1.5%	1.2	82.2	n/a
Total Assets (without correlations)	**1,567.9**	**100.0%**	**17.3%**	**271.5**	**1,839.4**	**1,296.4**
Total Assets (including correlations)	**1,567.9**		**14.9%**	**233.0**	**1,800.9**	**1,334.9**
Assets Relative to Liabilities (including correlation)	**1,567.9**		**14.1%**	**221.1**	**n/a**	**n/a**

The "Potential change" column shows the monetary effect of the expected volatility relative to each asset class. The actual annual change in value is expected to be lower than this in two years out of three, but higher in one year out of three. It can also be seen that the risk to the overall Fund assets is lower than the total of the risks to the individual assets.

However, because the purpose of a pension scheme is to make payments to scheme beneficiaries, the true risk of a pension scheme is not measured in absolute terms, but relative to its liabilities. This risk is shown in the bottom row of the above table. The risk is lower than the absolute asset risk, due to the impact of correlation with the discount rate used to value the liabilities.

It should be noted that the asset allocation used for this analysis will differ to that shown in the financial statements earlier. This is due to the Fund reporting its asset allocation in the financial statements according to each Manager's mandate, whilst for this section the most appropriate means is to analyse the mandate according to the underlying elements.

The corresponding/

The corresponding details as at 31 March 2013 are set out in the table below.

Position as at 31 March 2013

Asset Type	Value at 31 March 2013 £'m	Asset Weight	Volatility	Potential Change =/- £'m	Value on increase £'m	Value on decrease £'m
Equities - Developed Markets	884.8	61.2%	20.0%	177.0	1,061.8	707.8
Equities - Emerging Markets	53.0	3.7%	30.0%	15.9	68.9	37.1
Private Equity	78.9	5.5%	30.0%	23.7	102.6	55.2
Commodities	6.2	0.4%	30.0%	1.9	8.1	4.3
Property	95.8	6.6%	13.0%	12.5	108.3	83.3
Infrastructure	33.2	2.3%	8.0%	2.7	35.9	30.5
Diversified Credit	135.7	9.4%	10.0%	13.6	149.3	122.1
Fixed Interest Gilts	54.2	3.7%	9.0%	4.9	59.1	49.3
Index-Linked Gilts	32.9	2.3%	7.0%	2.3	35.2	30.6
Cash	70.3	4.9%	1.6%	1.1	71.4	n/a
Total Assets (without correlations)	**1,445.0**	**100%**	**17.7%**	**255.6**	**1,700.6**	**1,189.4**
Total Assets (including correlations)	**1,445.0**		**15.3%**	**221.1**	**1,666.1**	**1,223.9**

24. Actuarial Valuation as at 31 March 2011

The most recent actuarial valuation, carried out under Regulation 32 of the Local Government Pension Scheme (Administration) (Scotland) Regulations 2008, was undertaken as at 31 March 2011. This disclosed that the Fund's assets were sufficient to meet 86% of its liabilities.

In determining the employer contribution rates, the actuary took into account the funding policy as set out in the Funding Strategy Statement. The policy of the Administering Authority is to pursue a funding level of 100% and to generally allow employers (notably the scheduled bodies) to recover from their deficit position over a period of 20 years.

Full details of the methods and assumptions used in the 2011 valuation are set out in the actuary's valuation report dated 30 March 2012.

Copies of the Valuation report and the Funding Strategy Statement can be found at www.falkirkpensionfund.org

The Actuary has provided a statement describing the funding arrangements of the Fund during 2013/14. This can be found in a separate section later in this report (page 53).

25. Actuarial Present Value of Promised Retirement Benefits

The actuarial value of promised retirement benefits at the accounting date, based on a roll forward of the 31 March 2011 valuation and assumptions consistent with IAS19 (International Accounting Standard), has been estimated by the Fund Actuary as £2,281m (£2,011m at 31 March 2013). This figure is used by the Pension Fund for statutory accounting purposes and complies with the requirements of IAS26. The assumptions underlying the figure match those adopted for the Administering Authority's FRS17/IAS19 reports at each year end. The figure is only prepared for the purposes of IAS26 and has no validity in other circumstances. In particular, it is not relevant for calculations undertaken for funding purposes and setting contributions payable to the Fund.

The key assumptions relied upon by the actuary in deriving the actuarial present value of promised retirement benefits are as follows:

Financial Assumptions	**31 March 2013 % p.a.**	**31 March 2014 %p.a.**
Discount rate	4.5	4.3
Pay increase *	5.1	5.1
Price inflation/Pensions increases	2.8	2.8

* Pay increases are 1% p.a. nominal until 31 March 2015 reverting to long term rate thereafter.

Longevity Assumptions

The life expectancy assumption is based on standard SAPS tables with improvements in line with the Medium Cohort and a 1% p.a. underpin from 2008. Based on these assumptions, the average future life expectancies at age 65 are summarised below:

	Males	**Females**
Current pensioners	23.0 years	25.8 years
Future pensioners (assumed to be currently 45)	24.9 years	27.7 years

Commutation Assumptions

An allowance is made for future retirees to take 50% of the maximum additional tax-free cash up to HMRC limits for pre-April 2009 service and 75% of the maximum tax-free cash for post-April 2009 service.

26. Non Current Assets

Long Term Debtors

31 March 2013 £'000		31 March 2014 £'000
1,611	Strain on Fund Contributions (Due in over 1 year)	816

Analysis of Long Term Debtors

31 March 2013 £'000		31 March 2014 £'000
-	Central government bodies	-
1,401	Other local authorities	702
-	NHS bodies	-
-	Public corporations and trading funds	-
210	Other entities and individuals	114
1,611	TOTAL	816

27. Cash Balances

31 March 2013 £'000		31 March 2014 £'000
8,189	Bank Account	3,927
4,230	Balance held by Falkirk Council	301
12,419	TOTAL	4,228

As stipulated by the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 (SSI 2010 No. 233), all Local Authority Pension Funds have been required to operate their own bank account from 1 April 2011. From 1 April 2011 all payments made to the Fund are paid directly into the Fund's separate bank account.

Due to the Fund using Falkirk Council's financial management systems to effect transactions, there is a small working balance at year end, mainly due to timing issues.

28. Debtors

By Category

31 March 2013 £'000		31 March 2014 £'000
4,187	Contributions due – employers	3,917
1,387	Contributions due – members	1,228
1,150	Strain on Fund Contribution (Due within 1 year)	1,508
17	Benefits Paid in Advance	12
137	Sundry Debtors	70
6,878	TOTAL	6,735

Analysis of Debtors

31 March 2013 £'000		31 March 2014 £'000
974	Central government bodies	430
4,976	Other local authorities	5,486
-	NHS bodies	2
-	Public corporations and trading funds	4
928	Other entities and individuals	813
6,878	TOTAL	6,735

29. Creditors

31 March 2013 £'000		31 March 2014 £'000
(1,737)	Benefits Payable	(1,740)
(1,140)	Miscellaneous Creditors and Accrued Expenses	(1,253)
(2,877)	TOTAL	(2,993)

Analysis of Creditors

31 March 2013 £'000		31 March 2014 £'000
(28)	Central government bodies	(15)
(8)	Other local authorities	(14)
-	NHS bodies	-
(1,049)	Public corporations and trading funds	(1,126)
(1,792)	Other entities and individuals	(1,838)
(2,877)	TOTAL	(2,993)

30. Additional Voluntary Contributions

The Fund is required to offer an Additional Voluntary Contributions (AVC) facility to its Scheme Members. The arrangement operates on a money purchase basis with members' contributions being invested by Standard Life who are the Council's chosen AVC provider. (n.b. Prudential have been appointed joint AVC providers with Standard Life from June, 2014).

The AVC contributions are sent directly to the AVC provider by employers and as a result, they do not form part of the contribution income of the Fund.

The net asset value of the AVC policy with Standard Life at 5 April 2014 was £2.48 million (£2.54 million at 5 April 2013). Contributions made by members during the year to 5 April 2014 were £0.27 million. Expenditure from the policy during the same period (including the purchase of member annuities) amounted to £0.55 million. These amounts are not included in the Pension Fund Accounts in accordance with regulation 4 of the Local Government Pension Scheme (Management and Investment of Funds)(Scotland) Regulations 2010 (SSI 2010 No. 233).

31. Related Party Transactions

Falkirk Council

Falkirk Council Pension Fund is administered by Falkirk Council. Consequently, there is a strong relationship between the Council, in its capacity as an employing body, and the Pension Fund.

The Council incurred costs of £505k (2012/13: £473k) in relation to the administration of the Fund and was subsequently reimbursed by the Fund for these expenses. The Council is also the single largest employer of members of the Pension Fund and contributed £19.7m to the fund in 2013/14 (2012/13: £17.7m). All monies owing to and due from the fund were paid in year.

Transactions between the Council and the Fund are monitored by the Creditors section within Corporate Finance with the aim of any balances being settled as soon as reasonably practicable. The balance at 31 March 2014 was £301k (£4.2m 2013).

Key Management Personnel

The following senior officers at Falkirk Council held key positions in the financial management of the Fund during the year:-

Accrued CETV 31 March 2013 (£'000)	Role	Salary (£'000)	Service	Accrued CETV 31 March 2014 (£'000)
716	Chief Finance Officer	86	29 years	767
348	Pensions Manager	49	31 years	368

"CETV" means Cash Equivalent Transfer Value.

32. Contractual Commitments

Outstanding capital commitments (investments) at 31 March 2014 totalled £63m (31 March 2013 : £66m).

These commitments relate to outstanding call payments due to unquoted limited partnership funds held in the private equity and infrastructure segments of the portfolio. The amounts "called" by these funds are irregular in both size and timing over the life of the investment.

33. Contingent Assets/Liabilities

The Fund has no material contingent assets or liabilities at the period end and there were no material non-adjusting events occurring subsequent to the period end.

ACTUARIAL STATEMENT FOR 2013/14

This statement has been prepared in accordance with Regulation 31A(1)(d) of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008, and Chapter 6 of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the UK 2013/14.

Description of Funding Policy

The funding policy is set out in the Falkirk Council Funding Strategy Statement ("FSS"), dated December 2011. In summary, the key funding principles are as follows:

- To ensure the long term solvency of the Fund;
- To ensure that sufficient funds are available to meet all benefits as they fall due for payment;
- To enable employer contribution rates to be kept as nearly constant as possible and at a reasonable cost to the participating employers and to the taxpayers;
- To manage employers' liabilities effectively;
- To use reasonable measures to reduce the risk to scheme employers, and ultimately the taxpayers, from an employer defaulting on its pension obligations;
- To maximise the income from investments within reasonable risk parameters; and
- To address the different characteristics of the various employers to the extent that this is practical and cost effective.

The FSS sets out how the Administering Authority seeks to balance the conflicting aims of securing the solvency of the Fund and keeping employer contributions stable. The funding objective is to pursue a funding level of 100% (i.e. fund assets are 100% of the liabilities). Where an employer is in a deficit position, the funding strategy is generally to allow the deficit to be recovered over a period of 20 years. However, for employers whose covenant was considered by the Administering Authority to be sufficiently strong, contributions have been stabilised below the theoretical rate required to return their portion of the Fund to full funding over 20 years if the valuation assumptions are borne out. Asset-liability modelling has been carried out which demonstrate that if these contribution rates are paid and future contribution changes are constrained as set out in the FSS, there is still a better than 50% chance that the Fund will return to full funding over 20 years.

Funding Position as at the last formal funding valuation

The most recent actuarial valuation carried out under Regulation 32 of the Local Government Pension Scheme (Scotland) (Administration) Regulations 2008 was as at 31 March 2011. This valuation revealed that the Fund's assets, which at 31 March 2011 were valued at £1,199 million, were sufficient to meet 86% of the liabilities (i.e. the present value of promised retirement benefits) accrued up to that date. The resulting deficit at the 2011 valuation was £194 million.

Individual employers' contributions for the period 1 April 2012 to 31 March 2015 were set in accordance with the Fund's funding policy as set out in its FSS.

Principal Actuarial Assumptions and Method used to value the liabilities
Full details of the methods and assumptions used are described in my valuation report dated 30 March 2012.

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

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

The key financial assumptions adopted for the 2011 valuation were as follows:

Financial assumptions	**31 March 2011**	
	% p.a. Nominal	**% p.a. Real**
Discount rate	5.9%	3.1%
Pay increases *	5.1%	2.3%
Price inflation/Pension increases	2.8%	-

*plus an allowance for promotional pay increases. Short term pay growth was assumed to be 1% p.a. for 2011/12 and 2012/13, reverting to 5.1% p.a. thereafter.

The key demographic assumption was the allowance made for longevity. As described in the 2011 valuation report, life expectancy is based on the SAPS year of birth tables with improvements from 2008 in line with the Medium Cohort and a 1% p.a. underpin. Based on these assumptions, the average future life expectancies at age 65 are as follows (future pensioners are assumed to be aged 45 at 31 March 2011):

	Males	**Females**
Current Pensioners	23.0 years	25.8 years
Future Pensioners	24.9 years	27.7 years

Copies of the 2011 valuation report and Funding Strategy Statement are available on request from Falkirk Council, administering authority to the Fund.

Experience over the period since April 2013
Over the last year we expect that the funding level (excluding the effect of any membership movements) has improved due to stronger than expected investment performance over the period and a rise in gilt yields.

The next actuarial valuation will be carried out as at 31 March 2014.The Funding Strategy Statement will also be reviewed at that time.

Julie West
Fellow of the Institute and Faculty of Actuaries
For and on behalf of Hymans Robertson LLP
15 September 2014

SCHEDULED AND ADMISSION BODIES AS AT 31 MARCH 2014

Scheduled Bodies

Central Scotland Joint Valuation Board
Clackmannanshire Council
Falkirk Council
Forth Valley College
Scottish Children's Reporter Administration (SCRA)
Scottish Environment Protection Agency (SEPA)
Scottish Fire and Rescue Service (ex Central Scotland Fire & Rescue Service)
Scottish Police Authority (ex Central Scotland Police)
Stirling Council
Visit Scotland (Ex-Argyll, The Isles, Stirling, Loch Lomond and Trossachs Tourist Board)

Admission Bodies

Active Stirling
Alsorts
Amey (Clackmannanshire Schools Project) *
Association of Scottish Colleges
Ballikinrain School
Central Scotland Council for Racial Equality
Central Carers Association
Ceteris
Cowane's Hospital
Dollar Academy Trust
Falkirk Community Trust Ltd
Forth and Oban Ltd (Falkirk Schools Project)
Forth and Oban Ltd (Stirling Schools Project)
McLaren Community Leisure Centre
Open Secret
Plus
Scottish Autism
Seamab School
Smith Art Gallery
Snowdon School Ltd
Stirling District Tourism Ltd
Stirling Enterprise Park Limited (STEP)
Stirling University *
Strathcarron Hospice
Thinkwhere Ltd. (formerly Forth Valley GIS Ltd)
Valad Management (UK) Ltd *
Water Industry Commission for Scotland
Waterwatch Scotland *

* Closed to new members

Independent auditor's report to the members of Falkirk Council as administering body for Falkirk Council and the Accounts Commission for Scotland

I certify that I have audited the financial statements of Falkirk Council Pension Fund for the year ended 31 March 2014 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the fund account, the net assets statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 (the 2013/14 Code).

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Accounts Commission for Scotland, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

Respective responsibilities of the Responsible Financial Officer and auditor

As explained more fully in the Statement of Responsibilities, the Chief Finance Officer is responsible for the preparation of financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Chief Finance Officer; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the financial statements:

- give a true and fair view in accordance with applicable law and the 2013/14 Code of the financial transactions of the fund during the year ended 31 March 2014, and of the amount and disposition at that date of its assets and liabilities
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2013/14 Code
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973 and the Local Government in Scotland Act 2003.

Opinion on other prescribed matter

In my opinion the information given in the Explanatory Foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I am required to report by exception

I am required to report to you if, in my opinion:

- adequate accounting records have not been kept
- the financial statements are not in agreement with the accounting records
- I have not received all the information and explanations I require for my audit
- the Governance Compliance Statement does not comply with guidance from the Scottish Ministers.

I have nothing to report in respect of these matters.

Fiona Mitchell-Knight FCA
Assistant Director (Audit Services)
Audit Scotland
4th Floor, South Suite
Athenaeum building
8 Nelson Mandela Place
Glasgow
G2 1BT

25 September 2014

ADDITIONAL INFORMATION

Key Documents Online

You can find further information on what we do and how we do it on our website www.falkirkpensionfund.org. The following documents are on the website:

- Actuarial Valuation Report
- Funding Strategy Statement
- Annual Report and Accounts
- Governance Policy Statement
- Statement of Investment Principles

Fund Key Contacts

Actuaries:	Hymans Robertson LLP
Bankers:	Clydesdale Bank
Investment Custodians:	The Northern Trust Company
Investment Managers:	Details can be found in the notes to the accounts
Additional Voluntary Contributions (AVC) Managers:	Standard Life, Prudential
Solicitors:	Falkirk Council - Legal Services McLay, Murray and Spens

Contact Details

If you would like further information about Falkirk Council Pension Fund, please contact us.

Address:	Pensions Section PO Box 14882 Falkirk Council Municipal Buildings, West Bridge Street Falkirk, FK1 5ZF
Telephone:	01324 506338 (Accounting & Investment)
Telephone:	01324 506316 (Administration)
Fax	01324 506303
E-Mail	pensions@falkirk.gov.uk or investments@falkirk.gov.uk
Web	www.falkirkpensionfund.org

Independent Auditor

The Auditor appointed by the Accounts Commission for Scotland for the purpose of auditing the annual report and accounts is:

Audit Scotland
4th Floor, South Suite
The Athenaeum Building
8 Nelson Mandela Place
Glasgow
G2 1BT

AGENDA ITEM 6

FALKIRK COUNCIL

Subject: **CLUB VITA - LONGEVITY ANALYSIS**
Meeting: **PENSIONS COMMITTEE**
Date: **25 SEPTEMBER 2014**
Author: **CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 This report updates the Committee with initial findings from the Pension Fund's participation in the Club Vita longevity analysis.

2. BACKGROUND

2.1 One of the key risks faced by a pension fund is where life expectancy.increases more rapidly than has been envisaged and that, as a result, funding pressure is created.

2.2 Longevity risk is taken into account by the Actuary when setting employer contribution rates at the three yearly valuation. Until now, however, the actuary has used longevity assumptions based on national UK demographic data rather than data that is specific to the Falkirk Fund.

2.3 In order to gain a better understanding of the Fund's longevity profile, the Pensions Committee at its meeting of 12th December, 2013 agreed that the Fund should take part in Club Vita. It was highlighted at the time that other LGPS Funds who had participated in Club Vita had generally been able to adopt less stringent longevity assumptions and had thus seen a reduction in overall liabilities.

2.4 The availability of more accurate longevity data means that Fund calculations, such as cessation valuations, bulk transfers and funding assessments will be of a more reliable nature. Having robust evidence based longevity assumptions is also consistent with the Pension Regulator's view that Schemes should pay due attention to longevity risk.

2.5 Club Vita is an established provider of longevity research for pension funds and operates in conjunction with the Fund's actuaries, Hymans Robertson. Results are obtained by comparing Fund experience with the Club Vita dataset of 2 million scheme members and 700,000 deceased pensioners. Factors taken into account in establishing longevity trends include postcode, salary at cessation and occupation at retirement.

3. CLUB VITA OUTCOME

3.1 The Club Vita analysis indicates that the longevity assumption used in the 2011 actuarial valuation over-estimated the life expectancy of the Fund's pensioners. Applying the assumptions implied by the recent Club Vita analysis will result in a reduction in the Fund's liabilities of around £130m. This will clearly be of beneficial effect for employers when the actuary comes to set contributions rates for the three years starting from April, 2015, however other factors such as the discount rate and pending scheme changes will also have a significant part to play.

3.2 Catherine McFadyen, Fund Actuary with Hymans Robertson will give a short presentation highlighting the Club Vita process and summarising the key points of the findings.

3.3 More detailed analysis is attached at Appendix 1 of the report.

4. CONCLUSION

4.1 The Club Vita analysis has revealed that less stringent longevity assumptions can be justified for the Fund.

4.2 Continued participation in Club Vita will ensure that the Fund's longevity assumptions are more closely aligned with actual experience.

5. RECOMMENDATION

5.1 The Committee is asked to note the findings of the Club Vita analysis and invited to comment as appropriate.

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

<u>LIST OF BACKGROUND PAPERS</u>

NIL

Longevity Risk

Addressee and Scope

This paper is addressed to Falkirk Council, as the administering authority to the Falkirk Council Pension Fund, ("the Fund") for the purpose of sharing with the Pension Fund Panel and Committee. This paper summarises some of the information provided in the recent Club Vita reports addressed to the Fund and is written to assist the Committee and Panel in understanding the Fund's longevity risk. For more detail please refer to your full set of reports (which are compliant with relevant Technical Actuarial Standards). The contents of this report are reliant on the data supplied to us on your behalf including administration data provided by David Cunningham of the Falkirk Pensions Team on 7 May 2014.

This paper must not be released or otherwise disclosed to any third party (in whole or in part) except as required by law, regulatory obligation. Third parties placing reliance on this report do so at their own risk and neither Hymans Robertson LLP nor Club Vita accepts liability in relation to any such reliance.

No decisions are required based on the information in this paper. Decisions regarding the Fund's approach to managing longevity risk will be made later in the year as part of the formal funding valuation.

Club Vita

Club Vita aims to provide greater insight into the longevity characteristics in occupational pension schemes by bringing like-minded schemes together in a community where longevity experience data is pooled. By combining the data from individual schemes a clearer picture of the underlying patterns emerges.

Falkirk Council Pension Fund became a member of Club Vita in December 2013 with the aim of gaining a better understanding of the longevity characteristics of the Fund's membership. This impacts directly on the cost of pension provision and is therefore a key funding risk to manage. The cost of membership was £10,000 p.a. for an initial period of 3 years.

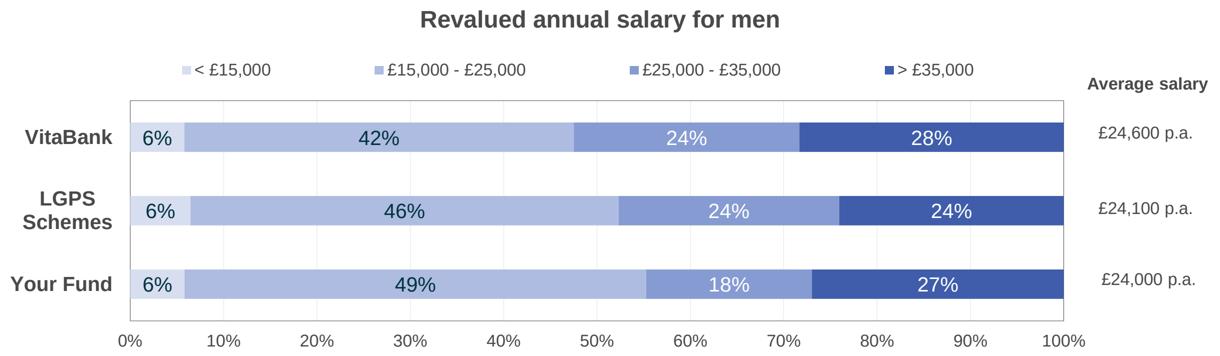
The Fund's membership data was submitted to Club Vita in May 2014. Club Vita carried out a full data cleansing exercise and analysed the data for the availability and the consistency of key membership statistics required to perform the comprehensive review of the Fund's longevity experience. The quality of the Fund's data was found to compare well to other Fund's in the LGPS peer group (all LGPS Funds participating in Club Vita) and Club Vita was able to proceed with detailed analysis, the results of which were recently reported back to the Fund. This paper summarises some of the key results.

Longevity 'DNA'

Club Vita uses a dataset ("VitaBank") of pension scheme mortality experience of c2m pensioners and c0.7m deaths to analyse the death rates of pensioners. The availability of such a large data set enables statisticians and actuaries to identify particular characteristics of individual members, specifically, **affluence**, **lifestyle**, **retirement**, **health** and **occupation** which are predictors of individual life expectancy. Your fund's demographic 'DNA' can be considered to be the 'DNA' of your fund in terms of its longevity characteristics. Just as every individual is unique in terms of his or her DNA, every fund is a unique collection of individuals, each of whom will have very different characteristics which will define their longevity prospects. Your fund's demographic 'DNA' considers the Fund's membership profile in terms of the concentrations (or sparcity) of these particular characteristics, each of which, are crucial to understanding your fund's longevity risk.

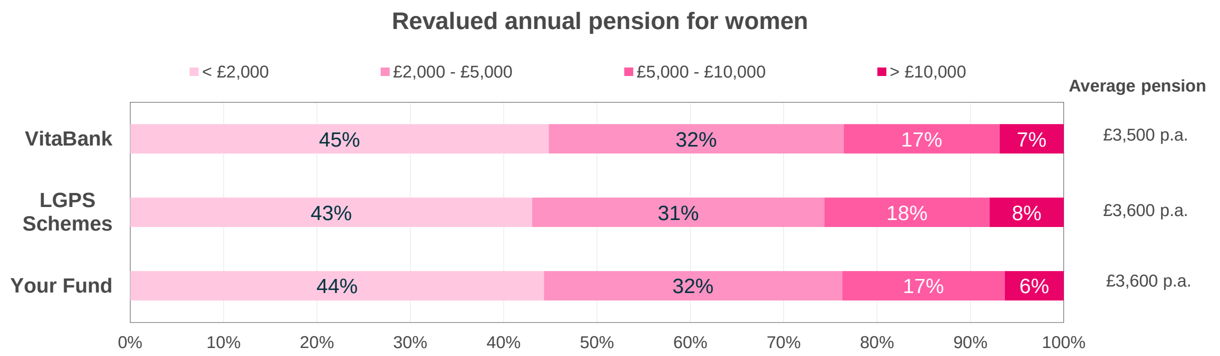
Your affluence 'DNA'

The relative affluence of your fund is pensioner membership was analysed, using revalued final salary as the affluence indicator for men and pension as the affluence indicator for women.



The male pensioners in your fund have:

- a lower average salary at exit/retirement (revalued to current terms) than the average for VitaBank as a whole; and
- a slightly lower average salary at exit/retirement (revalued to current terms) than the average for your LGPS peer group.



The female pensioners in your fund have:

- a higher average pension than the average for VitaBank as a whole; and
- a similar average pension to the average for your LGPS peer group.

All else being equal, we would expect members of funds with lower affluence measures to have a lower average life expectancy than those in occupational pension schemes in general.

Similar analysis is carried out for active and deferred members.

Your lifestyle 'DNA'

In determining life expectancy, it is not just how much income an individual has, but how they spend it which is important. Having information on the postcode of the individuals in VitaBank means that we are able to explore how lifestyle varies between different individuals. The members' postcodes enable us to enrich the database with geo-demographic information available in a variety of marketing databases purchased from third party providers.

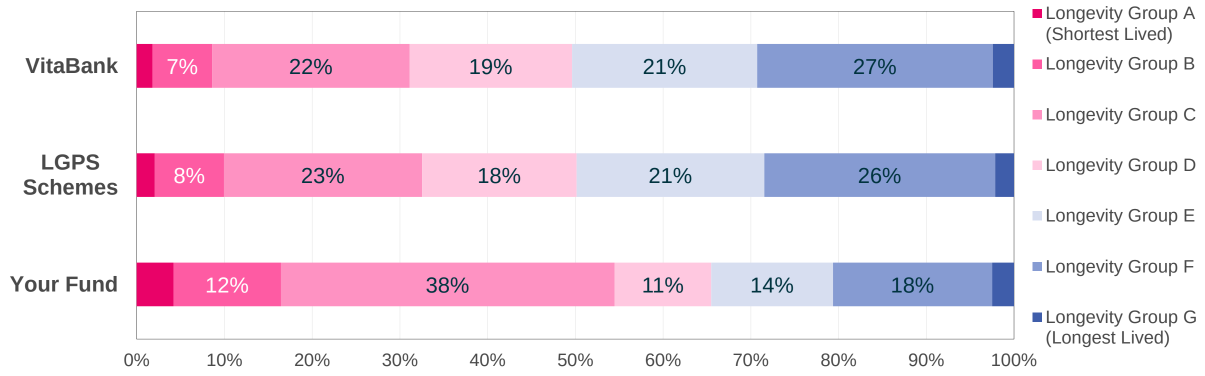
For example, one particular market research database classifies each of the UK's 1.7m postcodes into 57 different geo-demographic categories based upon information such as:

- type of property, (e.g. Urban terraced house);
- lifestyle information on the residents including:
  - which newspaper an individual is most likely to read
  - most likely hobbies, holiday habits etc.
  - financial sophistication

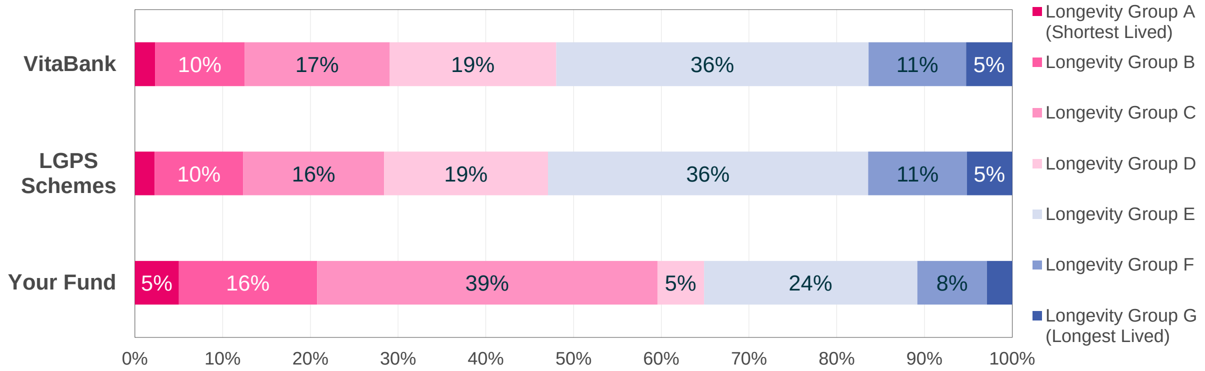
Owing to the considerable volumes of data within VitaBank we are then able to see how life expectancy varies between these different geo-demographic types. We have combined this information to create 7 lifestyle longevity groups. On average there is a difference of around 6.0 years between the shortest and longest lived group. However, not all of this difference will be due purely to lifestyle differences as some of the characteristics used to identify the varieties of geo-demographic types relate to affluence (for example, type of property). We are able to use powerful statistical techniques, known as multi-variate analysis, to isolate the individual effects of different characteristics such as geo-demographics and affluence.

The charts below consider the split of your membership, between the 7 longevity groups for those pensioners and dependants for whom you have supplied postcodes (99%).

Men



Women



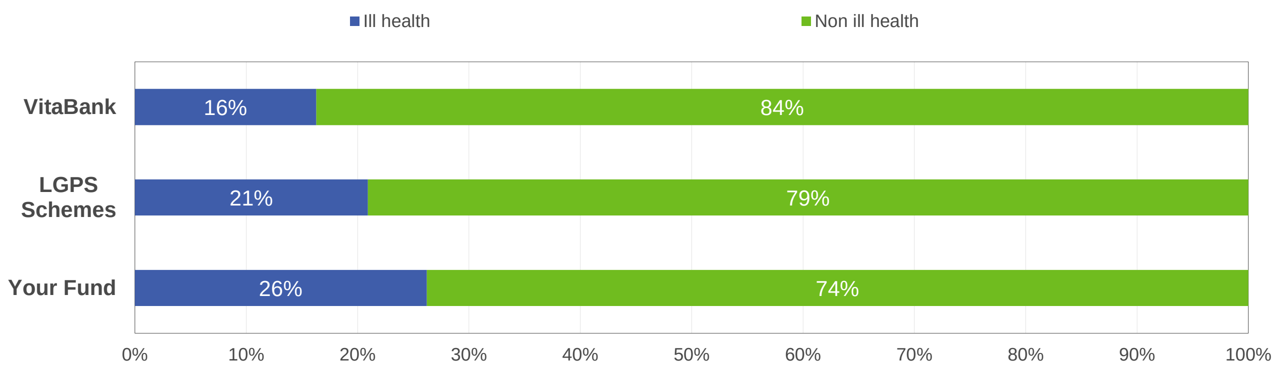
We see that, amongst those members for whom postcodes are known, your:

- men and women live, on average, in postcodes associated with shorter life expectancy than typically seen within VitaBank; and
- men and women live, on average, in postcodes associated with shorter life expectancy than typically seen within LGPS Schemes.

Your retirement health 'DNA'

Intuitively, you might expect that life expectancy is greater for those who retire in normal health in comparison with those who retire on grounds of ill-health. Evidence based on analysis of VitaBank deaths supports this, although in recent history the 'gap' between the 'sick' and 'healthy' appears to be closing.

The chart below considers the split of your pensioner membership, excluding widow(er)s, between those who retired on grounds of ill-health or in 'normal' health where this information has been provided

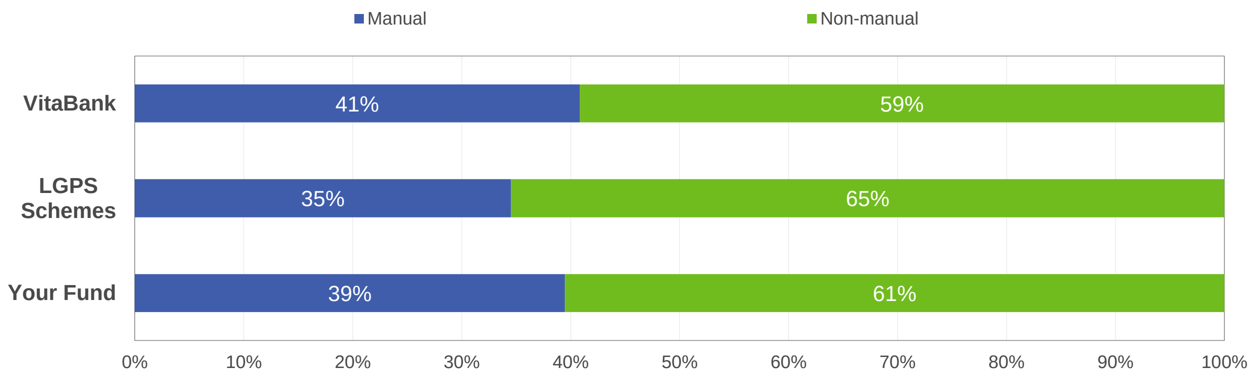


We can see that within your fund:

- there is (amongst those for whom retirement type is known) a higher proportion of ill health retirees than within VitaBank; and
- there is a higher proportion of ill health retirees than within your LGPS peer group.

Your occupational 'DNA'

The chart below considers the split of your pensioner membership, including ill health retirees but excluding widow(er)s, between those formerly employed in manual roles and those formerly employed on non-manual roles, known for all members.



We can see that within your fund:

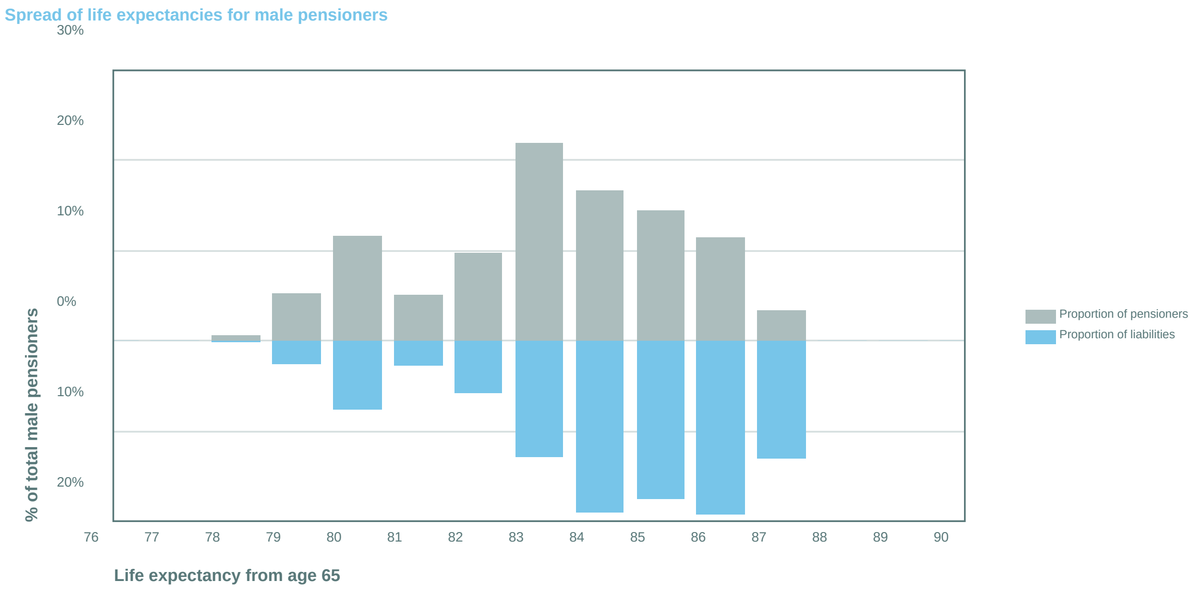
- there is (amongst those for whom former employment type is known) a slightly lower proportion of former manual employees than within VitaBank; and
- there is a higher proportion of former manual employees than within your LGPS peer group.

All else being equal, we would expect members of funds with a higher proportion of former manual employees to have a lower average life expectancy than those in occupational pension schemes in general.

Concentration of Longevity Risk

This 'DNA' analysis was applied to the membership of the Fund which identified a 9 year difference in life expectancy between the shortest and longest lived male pensioners (at age 65). Club Vita have used this analysis to pin-point the 'best estimate' mortality assumption for each member of the Fund which can then be relied on for funding purposes.

The chart below (focusing on male pensioners) shows the wide range of life expectancies predicted by your Club Vita analysis. The top half shows the spread of expectancies from 65 (to the nearest year) for male pensioners. Put simply, certain types of member are expected to live much longer than others.



It is clear that the traditional approach of using a single assumption simply does not reflect the reality of your fund, and is a huge oversimplification for many purposes.

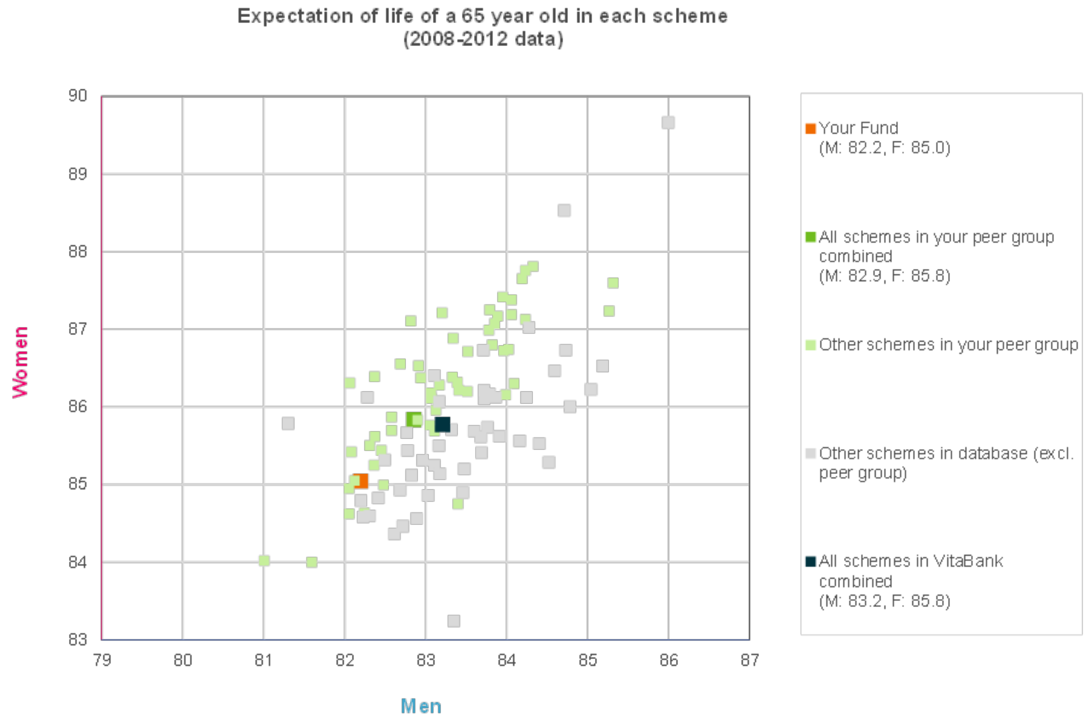
The bottom half of the chart weights the results by each member's liability – hence the larger bars for high life expectancies, which relate to more affluent individuals with larger pensions. In fact, across the whole fund:

- 50% of the liabilities are concentrated on 12.9% of members;
- 10% of liabilities are concentrated on just 1.2% of members (i.e. 353 individuals);
- The "bottom" 50% of members account for less than 9.2% of liabilities.

This means that the survivorship of the members with highest lifespans will have a disproportionate effect on the finances of the fund.

Summary

The graph below shows how the life expectancy of Falkirk Council Pension Fund members compares to the other LGPS Funds subscribing to Club Vita, labelled as “your peer group” in the graph below.



Implications for Funding

The Club Vita analysis has revealed that the assumption made for current longevity (before making any allowance for how longevity might change in the future) at the 2011 actuarial valuation, over-estimated how long the Fund’s pensioners were likely to live for. In numerical terms, if we adopted the assumptions for current longevity based on Club Vita’s detailed analysis of our specific member population, your funding level would improve by c6% and the deficit would reduce by c£130m. This information will be incorporated into the 2014 funding valuation which is currently underway.

Future Longevity Uncertainty

Club Vita’s reports also highlighted the uncertainty around the assumption that the Fund makes for how longevity will change in the future. They illustrated a not unreasonable scenario that would result in a reduction in your funding level. How long pensioners live for is not a static number – as experience data becomes available some uncertainty is removed. Annual reports from Club Vita and will help the Fund understand how the longevity of the Fund pensioners is changing and the impact on funding level and other aspects of managing the Fund.

Catherine McFadyen

Catherine McFadyen, FFA

For and on behalf of Hymans Robertson LLP

3 September 2014

AGENDA ITEM 7

FALKIRK COUNCIL

Subject: LOCAL GOVERNMENT PENSION SCHEME - NEW SCHEME DEVELOPMENTS
Meeting: PENSIONS COMMITTEE
Date: 25 SEPTEMBER 2014
Author: CHIEF FINANCE OFFICER

1. INTRODUCTION

1.1 This report updates the Pensions Committee on latest developments regarding the implementation of the new Local Government Pension Scheme (LGPS) from 1st April, 2015.

2. BACKGROUND

2.1 The LGPS is being updated to meet the requirements of the Public Service Pensions Act 2013 ("the 2013 Act"). This involves the Scheme becoming a Career Average (CARE) arrangement with each member's Normal Pension Age becoming equivalent to their State Pension Age (i.e. between age 65 and 68). Members will still be able to retire at any age between 60 and 75, however the penalty for taking benefits at age 60 will generally be greater than at present due to the linkage with State Pension Age.

2.2 Other significant features of the new scheme are:

- accrual rate of 49ths
- revaluation of benefits in line with the Consumer Price Index (CPI)
- protection of pre-April 2015 rights on final salary basis
- additional protection for those born before April, 1957
- cost management regime
- new governance regime

2.3 Two Heads of Agreement – one on scheme design and the other on governance matters - have been reached between COSLA, the Trade Unions and the Scottish Government.

3. REGULATORY POSITION

3.1 A number of statutory regulations require to be in place so that the new scheme can be implemented on 1st April, 2015. These are as follows:

Main Scheme Regulations
These regulations have been made and describe how benefits and contributions will be determined under the CARE arrangements. A number of defects have been identified in the Regulations and a set of amendments is awaited.

Transitional Regulations
These are about to be made and describe out how existing members' accrued rights will be treated in the new scheme.

Governance Regulations
These are not expected to be made until January, 2015 although a first draft will be available in October, 2014. These will specify how the governance requirements of the 2013 Act are to be applied in the LGPS

.

3.2 The work that is still needed on the Main Scheme and Transitional Regulations is primarily of a non-critical nature and unlikely to impede software development or Fund implementation plans. However, the timetable for Governance regulations being produced means that, in order to comply with the April, 2015 deadline, Funds will have to undertake their Governance reviews in advance of final regulations being available.

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3.3 The Governance implications of the 2013 Act are the subject of a separate report on today's Committee agenda.

4. EMPLOYER TRAINING

4.1 Fund employers have been invited to attend training events on either September 18th or October 2nd. These are aimed mainly at Payroll and HR practitioners. Around 35 employer delegates have signed up for each event.

4.2 A further resource for employers is www.lgpsregs.org at which the actual scheme rules and explanatory guides can be found.

5. EMPLOYEE INFORMATION

5.1 The Member's website www.scotlgps2015.org can be now be accessed. Fund employers have been asked to bring the website to the attention of their employees. The site is still being refined but already has substantial information about the new scheme, including FAQs and worked examples. Member briefings and a video are close to completion and will be uploaded shortly.

6. NEW PENSIONS ADMINISTRATION SYSTEM

6.1 The new local government pensions environment with its melding of pre-2015 Final Salary benefits and post-2015 CARE benefits has necessitated the purchase of a new computerised pensions administration system to replace the existing in-house system. Following a procurement exercise, the system selected is Heywood's "Altair" product, which is used by the majority of Scottish and English/Welsh LGPS Funds.

6.2 The total project costs are estimated at £1.5 million for a contract lasting 4.5 years. It is estimated that once the initial migration exercise has been completed using Altair will increase administration costs from around £16 per member per year to £22 per member. The additional costs should be viewed in the context of the increasingly complicated pension landscape where the demands of the new scheme have been increased by initiatives such as Auto Enrolment and Contracting Out abolition. Despite the additional cost, comfort can be taken that Altair is an

LGPS 2015 compliant product that will offer an array of new functionality to members and employers, including member self-service and employer transmission of electronic data. There are therefore opportunities for improved member service and longer term efficiencies.

6.3 The exercise to migrate data securely from the in house system to Altair is underway. The aim is to have data transferred to both the basic Altair system and the Altair payroll module by February, 2015.

6.4 Approval for the procurement of a replacement pensions administration system was given at the Pensions Committee meeting of 12 December 2013. Procurement of the Altair system has been undertaken in accordance with the Council's Contract Standing Orders.

7. CONCLUSION

7.1 Various workstreams are moving forward with a view to the implementation deadline of 1st April, 2015 being met.

7.2 With around 6 months left before the new scheme comes into operation, some gaps remain in the regulatory framework. The most significant void relates to the Governance arrangements. In view of the tight timescale, Funds will have no alternative but to press forward with their governance reviews. Proposals relating to this matter will be brought forward to the next round of Panel and Committee meetings.

7.3 Arrangements are in place to brief employers about the new scheme at Fund organised training events. Employees now have access to a website focusing exclusively on the new scheme provisions. Further publicity will be made available in the coming months

7.4 Procurement of a new administration system has been completed and engagement is taking place with the supplier to ensure the smooth and accurate transferral of data.

8. RECOMMENDATION

8.1 The Committee is asked to note the developments taking place towards the implementation of the LGPS (Scotland) 2015.

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

<u>LIST OF BACKGROUND PAPERS</u>

NIL

AGENDA ITEM 8

FALKIRK COUNCIL

Subject: LOCAL GOVERNMENT PENSION SCHEME – GOVERNANCE ISSUES
Meeting: PENSIONS COMMITTEE
Date: 25 SEPTEMBER 2014
Author: CHIEF FINANCE OFFICER

1. INTRODUCTION

1.1 This report provides the Pensions Committee with information regarding the governance arrangements that require to be put in place as a result of the Public Service Pensions Act 2013.

2. CURRENT DEVELOPMENTS

2.1 The Committee will be aware that the current round of pension reform began in 2011 with the publication of the Hutton report. This set out proposals for the establishment of a common UK-wide framework for public sector pensions in a bid to ensure that going forward the schemes were affordable, sustainable, fair and transparent. These proposals were carried forward in the Public Service Pensions Act 2013 ("the 2013 Act").

2.2 The governance framework set out in the 2013 Act introduces some new concepts and terminology. For example,

- the Administering Authority (or its Pensions Committee) becomes the "Scheme Manager"
- there is an expanded role for the Pensions Regulator
- there will be a national Scheme Advisory Board for LGPS (Scotland) and a Pension Board for each Fund.

2.3 A Heads of Agreement on governance matters has been reached during the summer between COSLA and the Trade Unions. However, the statutory regulations underpinning the governance rules will not be available until early 2015. The key milestones in the production of regulations by the Scottish Public Pensions Agency (SPPA) are as follows:

Key Event	**From**	**To**
Consultation on Draft Regulations	16 October 2014	27 November 2014
SPPA review consultation comments	28 November 2014	19 December 2014
Final Drafting	5 January 2015	16 January 2015
Ministerial Sign off		27 January 2015

2.4 Given the regulatory timetable above, it is apparent that any consultation on the new arrangements will have to be undertaken in advance of final regulations being made. Whilst it is not ideal to undertake a governance review in advance of the statutory guidance, the strong expectation is that the final regulations will closely follow the terms of the Heads of Agreement.

2.5 A copy of the Heads of Agreement is attached at Appendix A.

3. ROLE AND REQUIREMENTS OF THE PENSION BOARD

3.1 Under the terms of the 2013 Act, the role of the Pension Board is to assist the Scheme Manager to:

- secure compliance with the scheme regulations and other legislation relating to the governance and administration of the scheme;
- secure compliance with requirements imposed by the Pensions Regulator; and
- undertake any such other matters as the scheme regulations may specify.

3.2 The 2013 Act also requires that:

- the Board has an equal number of employer and member representatives;
- the scheme manager is satisfied that a person to be appointed to the board does not have a conflict of interest; and that
- the scheme manager is satisfied from time to time that none of the members of the board has a conflict of interest.

3.3 The Heads of Agreement provides that the Pension Board will:

- have a minimum of 4 trade union and 4 employer representatives;
- meet concurrently with the Pensions Committee;
- have a constituency that reflects broad scheme membership numbers; and
- rotate the Chair of the Board annually between Union and Employer (which implies that the Board may choose to meet separately on occasion).

3.4 The fact that the Pension Board has a specific statutory role means that it is unlikely individuals will be able to be members of both the Pension Board and Pensions Committee. This has implications for the three co-opted members who currently sit on both the Panel and the Committee.

4. CONSULTATION PROPOSAL

4.1 The key governance objective for the Fund in the coming months will be to establish its new pension board. This is a major undertaking for the Fund and will affect how Fund business is conducted in future. It is proposed, therefore, subject to the approval of the Pensions Committee, to consult Fund Employers and Trade Unions for their views as to how the new arrangements could best operate.

4.2 Whilst further questions may emerge, it would seem that any consultation should cover the following points:

- How many employer and trade union representatives should sit on the Board?
- How will employer and union representatives be selected
- What will the term of appointment be for Board members?

- How will the Board Chair be appointed (if there are equal member numbers)
- Should substitute Board members be permitted?
- Should non-Falkirk Council elected members continue to sit on the Pensions Committee? If so, is the current configuration of one employer, one union and one pensioner representative appropriate?
- Should an independent specialist be formally invited to sit on the Committee (such persons can only have observer status on the Board)

4.3 According to the Heads of Agreement, a model constitution setting out the administrative arrangements for Pension Boards is being drafted and is expected to be agreed during September, 2014.

5. PROPOSED CONSULTATION ACTION PLAN

5.1 It is proposed that the Fund's own consultation exercise should proceed broadly as follows:

Step	Activity	Lead	Provisional Target Dates
1	Await Pension Board model constitution	COSLA/ Unions	15 September 2014
2	Await first draft of governance regulations	SPPA	15 October 2014
3	Prepare and circulate consultation paper with draft Pension Board constitution	Falkirk	31 October 2014
4	Consultation period	Fund Employer/ Unions	1 November 2014 to 30 November 2014
5	Consultation comments to be considered and governance arrangements provisionally agreed at Joint meeting of Panel and Committee	Falkirk	11 December 2014
6	Await final governance regulations and check if provisional governance proposals meet regulatory requirements	SPPA	27 January 2015
7	Conduct selection process for Pension Board members	Falkirk/ Unions	1 February 2015 to 28 February 2015
8	Final ratification of arrangements at Pensions Committee	Falkirk	12 March 2015
9	Pension Boards formally set up	Falkirk	31 March 2015
10	First Board/Committee meeting	Falkirk	4 June 2015

6. SCHEME ADVISORY BOARD

6.1 A résumé of the new governance landscape would not be complete without mention of the national Scheme Advisory Board whose statutory role under the 2013 Act is to provide advice to the Scottish Ministers on the desirability of changes to the LGPS.

6.2 The Board may also be called upon to provide advice to the scheme managers or the pension boards in relation to the effective and efficient administration and management of the Scheme or its Funds.

6.3. In Scotland, the Scheme Advisory Board is expected to be based on the existing Scottish Local Government Pensions Advisory Group (SLOGPAG), except that, unlike SLOGPAG, which has Scottish Government representation, the Scheme Advisory Board will be a bipartite entity with representation from local government and trade unions only. The Scottish Government will however have observer status.

6.4 The Advisory Board is expected to have a key role in shaping the cost management arrangements to apply to the Scheme in Scotland.

7. CONCLUSION

7.1 The Public Sector Pensions Act 2013 requires the pension fund to adopt new governance arrangements from 1st April, 2015. These have been expanded upon in a COSLA/Trade Union Heads of Agreement and will be incorporated within LGPS governance regulations to be made in January, 2015.

7.2 Consent is being sought from the Pensions Committee to conduct a consultation exercise with fund stakeholders in the coming months to ensure that a pensions board is established for 1st April, 2015 and that the fund is compliant with the relevant legislation.

8. RECOMMENDATION

8.1 The Pensions Committee is invited:

i) to note the revised governance arrangements that require to be established by 1 April 2015;
ii) to agree to the proposed consultation arrangements; and
iii) to comment on any other matters raised in the report.

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

<u>LIST OF BACKGROUND PAPERS</u>

NIL

APPENDIX A

HEADS OF AGREEMENT

Introduction

The UK Public Service Pensions Act sets out new governance requirements for pension funds across the UK, implementing the Hutton recommendations. The SPPA has recently consulted on new arrangements and SLOGPAG has considered the responses and the views of key stakeholders. This paper sets out the Heads of Agreement for a new governance structure in Scotland.

It is recognised that governance arrangements will be subject to on-going review to reflect changes in, or interpretation of, legislation and best practice. For example, interpretation of the current legal requirements of the Institutions for Occupational Retirement Provision (IORP) Directive and any changes as a result of the new proposed IORP Directive. The Heads of Agreement for the new scheme (agreed in December 2013) also sets out the process for a wider review of structures which could impact future governance arrangements.

It is also recognised that these arrangements will be subject to the views and agreement of Scottish Ministers.

Scheme Advisory Board

The Scheme Advisory Board is the body responsible for providing advice to the Responsible Authority (Scottish Ministers), on the desirability of changes to the scheme. The Scheme Advisory Board also provides advice to the Scheme Managers and Pension Boards in relation to the effective and efficient administration and management of the scheme.

The new scheme advisory board is not a big change in Scotland as we have had a similar body in SLOGPAG for many years. The main elements of the Scheme Advisory Board should be as follows:

- It will be a bipartite body with representatives from local government employers and trade unions. The Scottish Government will be present as observers.
- There will be 7 employer and 7 trade union representatives. Substitute representatives will be available and will have undergone the requisite training and development to inform their role.
- The Chair will be rotated on an annual basis or an independent Chair may be appointed by Scottish Ministers.
- The secretariat will be provided by two Joint Secretaries, appointed from COSLA and the Trade Unions.
- Advisors e.g. Directors of Finance will also attend the Board but will not have membership status.
- Observers e.g. Scottish Government will also attend the Board but will not have membership status.

Pension Boards

Pension Boards will be established covering each fund in Scotland and will be the body responsible for assisting the Scheme Manager in relation to compliance with scheme regulations and the requirements of the Pensions Regulator.

The consultation process indicated a difference between the employer and trade union views on having pension boards in addition to the current structure or merging them into one board. A hybrid solution has therefore been agreed that would retain the pension committee of the administering authority with membership appointed under current arrangements and responsibility for fund management.

While the roles and function of pension committees and pensions boards will be set out in the regulations, the normal practice would be that both bodies would meet at the same time to consider the same agenda, with the Chair of the pension committee chairing the concurrent meeting. This innovation will result in a positive and proactive partnership culture where in practice the two bodies act as one.

New pension boards would also be established as follows:

- Membership would consist of equal numbers of trade union representatives and employers drawn from other councils and scheduled or admitted bodies in membership of that fund.
- As a minimum there will be 4 trade union and 4 employer representatives with the expectation that larger funds will require greater numbers. Numbers from organisations on either side will broadly reflect respective membership in the scheme.
- The Chair will be rotated on an annual basis.
- The secretariat will be provided jointly from the pension fund and the local trade union representatives.
- Advisors and observers will also attend the Board but will not have membership status

There will be a model constitution setting out the administrative arrangements for pension boards. Representatives of employers and trade unions will define the local parameters in addition to the model constitution. If there is difficulty in agreeing those local parameters, the Scheme Advisory Board can act as a point of resolution.

The pension board will determine the areas they wish to consider including, amongst others:

- Reports produced for the pensions committee
- Requisition reports from the scheme managers on any aspect of the fund
- Monitor investments and the investment principles/strategy/guidance
- The fund annual report
- External voting and engagement provisions
- Fund administrative performance
- Actuarial reports and valuations
- Funding policy
- Any other matters that the pensions board deem appropriate

If the pension committee and pension board cannot reach joint agreement on any matter the process for resolving any differences between the two bodies will be as follows. Whilst this process is undertaken the decision of the pension committee is still competent.

In the first instance, if at least half of the members agree, then the pension board can refer back a decision of the pensions committee for further consideration if any of the following grounds are met:

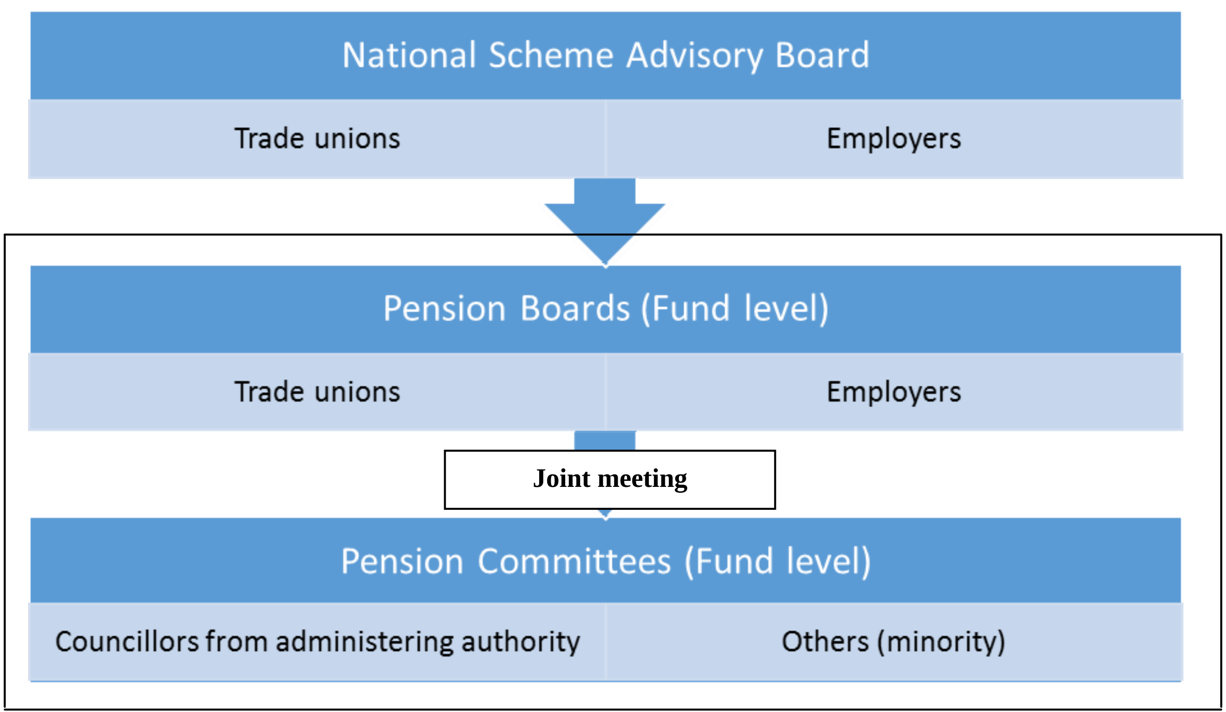
- That there is evidence or information which it is considered needs re-evaluating or new evidence or data which the pensions Committee did not access or was not aware of at the point of decision making and which is considered material to the decision taken;
- That the decision of the pensions Committee could be considered illegal or contrary to regulations;
- That the decision of the pensions Committee is contrary to a relevant Code of Practice published by the Pensions Regulator; or
- That the decision is not in the interest of the continued financial viability of the Scheme or is against the principles of proper and responsible administration of the Scheme

If there is no agreement after the matter has been referred back to the pensions Committee, then the difference in view between the Pension Board and the Pension Committee should be published in the form of a joint secretarial report on the fund website and included in the fund annual report.

It may then be appropriate for the Scheme Advisory Board to consider and take a view on the matter and, if considered appropriate, to provide advice to the Scheme Manager or the pension board in relation to the matter.

There will be an agreed training programme for all members of pension committees and pension boards. All administration costs will be met by the relevant fund.

The structure is shown diagrammatically below.



AGENDA ITEM 9

FALKIRK COUNCIL

Subject: GENERAL GOVERNANCE MATTERS
Meeting: PENSIONS COMMITTEE
Date: 25 SEPTEMBER 2014
Author: CHIEF FINANCE OFFICER

1. INTRODUCTION

1.1 This report updates the Pensions Committee on various matters associated with the business of Falkirk Council Pension Fund.

2. RISK REGISTER

2.1 The Committee has asked officers to provide a regular update on any significant changes in risk. The following items are considered worthy of reporting:

Identified Risk per Risk Register	Reason for Change in Risk Rating
Funding position affected by falling asset values	Rising geopolitical tensions in Ukraine and the Middle East have been impacting on financial markets. This is partly mitigated by the facts that a) the Fund is a long term investor in the assets it holds and has the capacity to "ride out most storms" and b) not all of the Fund's assets are exposed to this risk.
Retention of key staff	The Pension Fund Accountant is moving to a post with City of Edinburgh Council. Discussions are taking place with the Lothian Fund to ascertain whether there is an option for them to provide accounting support.

3. SOCIAL HOUSING

3.1 The legal documentation relating to the Social/Affordable Housing mandate is close to completion. Once concluded, this will enable the initial investment of £15m to be made to the Hearthstone Housing Fund for Scotland. The Committee will recall that the first £15m is to be used to secure a Bond from the Places for People Group /Castle Rock Edinvar to deliver Social Housing. The remaining £15m will be drawn down as opportunities for investment in affordable housing materialise.

3.2 A presentation on mandate developments will be given at today's meeting by Christopher Down, Chief Executive of Hearthstone Investments.

4. LOCAL INFRASTRUCTURE

4.1 At its meeting of 5 June 2014**,** the Pensions Committee took the decision to invest £30m in UK infrastructure projects in conjunction with the Lothian Pension Fund (LPF), using LPF specialist skills to identify potential investments and undertake the necessary due diligence. The final decision as to whether or not the Fund should invest in a particular project has been delegated to the Chief Finance Officer.

4.2 A resourcing agreement, being the vehicle through which LPF staff will be able to provide investment advice to Falkirk without contravening Financial Services regulations, has been drafted and reviewed by an independent firm of Solicitors. This will shortly be available for sign off, at which point the Fund will be in a position to make its first investment.

5. PRUDENTIAL – ADDITIONAL VOLUNTARY CONTRIBUTIONS (AVC)

5.1 Prudential were formally appointed as one of the Fund's AVC Providers during the summer.

5.2 In an effort to promote the AVC facility, Prudential have been delivering a number of information sessions to the scheme members of SEPA, Falkirk and Clackmannanshire Councils. Sessions have covered both AVCs and LGPS benefits generally and have been very well received.

6. LOCAL AUTHORITY PENSION FUND FORUM (LAPFF)

6.1 The LAPFF represents the interests of 58 local authority pension funds with combined assets of around £120 billion. Its mission is to promote the highest standards of corporate responsibility amongst the companies in which member funds invest.

6.2 The LAPFF is supported by PIRC Ltd, who are the Forum's company research and engagement partner. PIRC are also the Falkirk Fund's proxy voting agents and advisers on Environmental, Social and Governance matters. PIRC will be delivering a presentation at today's meeting.

6.3 During the last quarter, LAPFF activity has included:

- attending AGMs of Barclays and Glaxosmithkline to challenge the company over governance and executive remuneration;
- speaking in support of the resolution co-filed at the National Express AGM on human capital management at US operations;
- addressing the BP and Shell Chairs on diversification into low carbon energy and carbon asset risk management; and.
- meeting the Chair of Trinity Mirror over issues of media standards and ethics

7. RECOMMENDATION

7.1 The Pensions Committee is asked to note the contents of this report and invited to comment as appropriate.

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

<u>LIST OF BACKGROUND PAPERS</u>

NIL

AGENDA ITEM 11

FALKIRK COUNCIL

Subject: **FUND MANAGER PERFORMANCE REVIEW**
Meeting: **PENSIONS COMMITTEE**
Date: **25 SEPTEMBER 2014**
Author: **CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 The Local Government Pension Scheme Regulations require that Falkirk Council, as administering authority for the Pension Fund, review the investments of its managers at least once every three months, which includes an analysis of returns and risk. This paper reports on performance for the overall Fund and reviews individual manager performance and developments.

1.2 The rates of return achieved by our fund managers are measured against pre-determined benchmarks. This service is provided by the Fund's custodian, Northern Trust.

1.3 The undernoted benchmarks are in place to measure the performance of each Manager.

Fund Manager	Benchmark
Aberdeen Asset Management (AAM)	MSCI All Countries World Index
Baillie Gifford Bonds (BGB)	Customised benchmark comprising UK Fixed Interest and UK Index Linked Bonds
Baillie Gifford Diversified Growth (BGDG)	UK Bank of England Base Rate
Legal & General (L&G)	Customised benchmark comprising UK and Overseas Equities
Newton Investment Management (NIM)	FTSE All World Index
Schroder Investment Management (SIM) UK Equities	FTSE All Share Index
Schroder Investment Management (SIM) Property	AREF/IPD UK Quarterly Property Fund Indices

1.4 Full details of each Manager's portfolio activity and any engagement with companies on corporate governance issues are recorded in their individual quarterly investment reports, which are enclosed.

2. MARKET REVIEW AND OUTLOOK

2.1 The bull trend in global equity markets continued in the second quarter of 2014, supported by easy monetary policies, positive economic developments and a shortage of compelling investment alternatives given the low yields available in bond markets. The disruptive geopolitical situation, including conflicts in the Middle East, Ukraine and parts of Africa, did not have a durable impact on asset prices.

2.2 US bond and equity markets were underpinned by supportive monetary policy and signs of a recovery in US corporate confidence. There is strong evidence that businesses are shifting from limited shelf-life strategies, such as cost cutting and debt reduction, to ones that involve investing for growth. Although the Fed continues to taper asset purchases, the absence of broad inflationary pressures in the US economy means that bond markets are anticipating an orderly increase in yields in the summer of next year. US economic growth also surprised to the upside after a shocking 2.9% drop in the first quarter, the worst number in five years. In Q2 GDP expanded by 4% versus the consensus expectation of 3%. These trends also caused the US dollar to strengthen against most currencies.

2.3 Globally, the biggest positive economic surprise has been in the UK where GDP growth exceeded expectations to the extent that sterling strengthened, mortgage availability was restricted and investors became increasingly concerned that an increase in interest rates was just around the corner. Some commentators note that growth is unbalanced, and the UK economy is displaying some of the disturbing characteristics last experienced in the late 1980s.

2.4 The much heralded European economic recovery has failed to fully materialise, and fears of more stagnation and disinflation (or even Japanese-style deflation and depression) prompted the ECB to ease monetary policy further. Nevertheless, monetary policy still remains too restrictive for the Continent as a whole, implying that growth and inflation will probably remain weak and the debt overhang excessive.

2.5 And in Japan itself the situation is also rather lacklustre, in part due to the April increase in the consumption tax from 5% to 8%. Abe's growth and restructuring programme has so far under-delivered when judged by tangible results. However, pro-inflationary government policies, gathering reform momentum and resilient business and consumer confidence suggest that second half growth should be relatively robust.

2.6 Growth in the larger emerging economies also continues to be weak, generally due to high inflation rates and restrictive monetary policies. Russian economic problems are exacerbated by an adventurous foreign policy, and China continues to grapple with structural issues and the gradual deflation of its property bubble. However, the overall picture is becoming less bleak, and some emerging countries were actually able to ease monetary policy in Q2, most notably Mexico, Turkey, Thailand and Hungary. There are also rare pockets of outright enthusiasm, for example in the Indian stock market following the election of Modhi based on a programme of reform and restructuring.

2.7 Many equity investors are becoming more cautious, and their concerns are justified. The developed world equity bull market is maturing and valuations are becoming extended: in the US they have reached their most stretched level since the bubble years at the turn of the century. More unsettling, and perhaps the biggest surprise so far in 2014, is the failure of bond yields to rise. This might be signalling problems in the pipeline, maybe in the normalisation of monetary policy in 2015.

3. ANALYSIS OF PERFORMANCE RESULTS

3.1 The total fund and individual external manager returns are shown in the table in Appendix 1. The returns for the quarter ending 30 June 2014 are shown, but this is a very short period to measure performance. It simply reflects the regular reporting cycle. Each manager has been set its own individual investment objective, which depends on the type of mandate awarded. Each active manager is tasked with outperforming their benchmark over either three or five year periods. The table in Appendix 1 incorporates the relevant return and benchmark data and the excess return relative to the manager's benchmark and outperformance objective. More detail on individual manager mandates and objectives can be found in Appendix 2.

3.2 Developed and emerging market equity indices returned +2.6% and +4.0% respectively over the second quarter of 2014. Index-linked gilts managed a +1.0% return while conventional gilts were flat at shorter maturities, but +2.3% at longer (>15 year) maturities. UK commercial property led the pack (+4.3%).

3.3 The overall Fund's return of +2.3% over the quarter was ahead of the benchmark return of 2.1%. Over the 3 year period the Fund benefited from equity market strength and SIM's outperformance in UK equities, rising +8.9% per annum compared with the benchmark return of +7.0% per annum, an excess return of +1.9% per annum. Long term return data shows Fund appreciation of +12.8% per annum over 5 years and +7.2% per annum since September 2001. These long term returns are above the benchmark returns.

3.4 Over the second quarter of 2014, the Fund's three active equity managers all posted positive returns from +0.6% to +2.8%. Only AAM beat its benchmark of global equities while NIM and SIM lagged their equity benchmarks. The Fund's passive equity manager, L&G, produced a return of +2.5%, in line with its benchmark return, and so consistent with its mandate.

The return from BG's bond mandate was +1.9%, ahead of its benchmark by 0.2%. BG's other mandate, the Diversified Growth portfolio, rose 2.4%, ahead of its benchmark by 2.3%.

The property portfolio managed by SIM lagged its benchmark by 0.1%, but rose 4.2% in absolute terms.

3.5 Longer term return data shows that SIM's UK equity portfolio is comfortably ahead of its objective of +1.25% per annum above the benchmark over the 3 year period and since inception.

NIM's global equity mandate stipulates an objective of +3% per annum above the benchmark over 5 year rolling periods. Returns over the past 3 and 5 years and since inception have narrowly beaten the benchmark, but it has not achieved its objective of +3% per annum above the benchmark.

The AAM mandate's objective is +3% per annum outperformance over 3 year rolling periods. After a very poor 2013, performance is lagging the benchmark and objective over 3 years. After an excellent start to the mandate, returns are still ahead of benchmark by 0.7% per annum since inception in May 2010, but lag the objective by 2.4% per annum.

The performance of BG's bond mandate is lagging its benchmark by 0.2% per annum since inception in 2007, but the 3 and 5 year performance have been very strong. The excess return over the benchmark of +1.4% per annum comfortably exceeds the objective of +0.9% per annum over rolling 3 year periods.

SIM's property performance has been disappointing in recent years, and this has reversed positive results in the early years of the mandate. Since inception in 2005, a period of low returns for commercial property owners, the portfolio has performed in line with its benchmark, but has fallen short of the objective by 0.7% per annum.

4. CONCLUSION

4.1 Global equity indices posted solid gains in the quarter aided by some broadly encouraging economic data, continued loosening of monetary policy from the European Central Bank, and in the face of significant geopolitical tensions. In the UK, with the improving labour market and signs of improvements in earnings, the Bank of England's Monetary Policy Committee will be focusing on interest rate rises towards the end of 2014.

4.2 All managers managed to deliver positive returns during the quarter, although only Aberdeen and Baillie Gifford (in both their Bond and Diversified Growth mandates), managed to achieve the benchmark return. The best performing asset class of the quarter was property with a return of 4.3%. The Schroders property mandate, despite the challenges of its Continental European exposure, almost matched the benchmark with a return of 4.2%.

5. RECOMMENDATIONS

5.1 The Committee is asked to note:-

(i) the Managers' performance for the period ending 30 June 2014; and

(ii) the action taken by Managers during the quarter to 30 June 2014 in accordance with their investment policies.

Chief Finance Officer

Date: 25 August 2014

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

1. The Northern Trust Company – Fund Analytics 30 June 2014

Any person wishing to inspect the background papers listed above should telephone Falkirk 01324 506304 and ask for Alastair McGirr

APPENDIX 1 – PERFORMANCE MEASUREMENT (RATES OF RETURN)

Rates of Return by Manager with Excess Returns - 30 June 2014

Manager	Market Value £	Weight	3 months (Returns)	3 year (Returns)	5 year (Returns)	Since inception (Returns)	Inception Date
Aberdeen Portfolio	218,012,365	13.7%	2.8%	8.2%	-	9.4%	May-10
Benchmark			2.6%	8.6%	-	8.8%	
Excess Versus Benchmark			**0.2%**	**-0.4%**	**-**	**0.6%**	
Excess Versus Objective			**-**	-3.4%	**-**	-2.4%	
Baillie Gifford Bond Portfolio	137,768,897	8.7%	1.9%	8.3%	9.8%	6.2%	Mar-07
Benchmark			1.6%	6.9%	7.5%	6.4%	
Excess Versus Benchmark			**0.2%**	**1.4%**	**2.4%**	**-0.2%**	
Excess Versus Objective				**0.5%**	**1.5%**	**-1.1%**	
Baillie Gifford Diversified Growth	194,014,068	12.2%	2.4%	-	-	7.2%	Feb-12
Benchmark			0.1%	-	-	0.5%	
Excess Versus Benchmark			**2.3%**	**-**	**-**	**6.7%**	
Excess Versus Objective *			**-**	**-**	**-**	3.2%	
Legal & General	336,292,146	21.2%	2.5%	9.0%	14.4%	14.5%	Jan-09
Benchmark			2.5%	9.0%	14.3%	14.3%	
Excess Versus Benchmark			**0.0%**	**0.1%**	**0.1%**	**0.1%**	
Excess Versus Objective			**-**	**0.1%**	**0.1%**	**0.1%**	
Newton	231,967,919	14.6%	2.0%	9.0%	14.3%	8.5%	Jun-06
Benchmark			2.7%	8.5%	14.0%	7.5%	
Excess Versus Benchmark			**-0.7%**	**0.5%**	**0.3%**	**0.9%**	
Excess Versus Objective			**-**	**-**	**-2.7%**	**-2.1%**	
Schroders UK Equity	225,286,536	14.2%	0.6%	14.7%	16.9%	9.5%	Sep-01
Benchmark			2.2%	8.9%	14.5%	7.2%	
Excess Versus Benchmark			**-1.6%**	**5.7%**	**2.4%**	**2.4%**	
Excess Versus Objective			**-**	**4.5%**	**1.2%**	**1.1%**	
Schroders Property	116,788,669	7.3%	4.2%	5.7%	7.6%	2.2%	Nov-05
Benchmark			4.3%	6.6%	9.2%	2.1%	
Excess Versus Benchmark			**-0.1%**	**-1.0%**	**-1.6%**	**0.0%**	
Excess Versus Objective			**-**	**-1.7%**	**-2.4%**	**-0.7%**	
Total Fund	1,589,283,871	100.0%	2.3%	8.9%	12.8%	7.2%	Sep-01
Benchmark			2.1%	7.0%	11.5%	6.9%	
Excess Return			**0.2%**	**1.9%**	**1.3%**	**0.3%**	

*** Note that objectives are set over 3 or 5 year periods and Baillie Gifford's Diversified Growth mandate has not been in place for the requisite periods.**

There are small rounding effects in the table above.

APPENDIX 2 - INVESTMENT MANAGER COMMENTS

Aberdeen Global Equity

(13.7% of Total Fund)

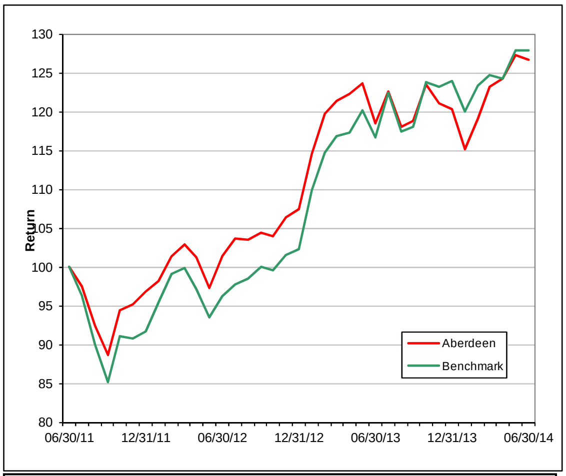
Investment Approach:

High conviction, research-driven house. Only invest in companies they have met. Regional teams produce Global buy list of 330 stocks. Global team carries out comparative analysis and produces model portfolio of 50 stocks from which team must build portfolio. Long-term horizon, trading highly price-sensitive.

Investment Objective:

To outperform the MSCI AC World Index in sterling by 3% per annum, gross of fees, over rolling 3 year periods (inception date 16 May 2010)

3 Year Performance to 30 June 2014



Q2 2014	: +0.2% excess return
3 Years	: -0.4% excess return
Since inception	: +0.6% p.a. excess return

Summary

Mild outperformance this quarter after a good Q1 but terrible 2013. Long term performance is positive, but below target.

Portfolio

The portfolio is genuinely unconstrained, which indicates that it should be able to achieve its objectives. No single investment more than 5% of the portfolio is allowed, but sector and country limits are wide (+/-15% for sectors and +/-35% for countries allowed). Cash currently at 3.9% as 3 stocks were sold in Q2 and just 1 purchased.

The portfolio is more geographically diverse than the benchmark. North America represents >50% of the benchmark, but the portfolio is u/w by 20%. The fund is o/w the UK (+8%), Europe ex-UK (+5%), and LatAm (+6%). By sector, the portfolio remains heavily o/w defensive sectors, such as consumer staples (+6%), energy (+8%) and materials (+3.5%), and has low exposure to cyclical earnings, such as consumer discretionary shares (-10%), I.T. (-3%) and industrials (-2%). Financials are also underrepresented (-5%). Consequently, the portfolio is likely to perform relatively poorly in strong equity markets, but its defensive tilt should help protect it in the event of equity markets falling. Aberdeen's rhetoric and its portfolio positioning remain very cautious.

Performance was ahead of benchmark due mainly to the overweight allocation and stock picking within the Energy sector. Schlumberger, EOG Resources, Petrobras, Petrochina and Royal Dutch Shell all rose by >10%. Outside of Energy, the u/wts in Consumer Discretionary and Financials also helped. Stock picking was strong in Industrials, but there was weakness from I.T., Healthcare, Telecoms and Staples. QBE Insurance, Vodafone and Ericsson were amongst the biggest fallers, although not holding Apple was the biggest detractor from performance as it returned almost 20% in Q2.

Aberdeen continue to follow their process investing in quality companies with lower than average levels of debt and relatively stable earnings and cashflows. In the absence of major price volatility, portfolio activity has been, and can be expected to be, low. Portfolio initiated a position in global payments company Visa and sold its positions in Verizon, QBE Insurance and Quest Diagnostics outright. Otherwise, transactions have involved topping up and top-slicing existing shareholdings largely to reflect shifts in valuations.

Key considerations/developments

Ownership has not changed, but the acquisition of SWIP is very large – it adds £138bn of assets under management taking the Group's assets to £325bn. Integration is proceeding apace – active SWIP portfolios have already been restructured to the Aberdeen shape; perhaps the biggest concern is the **client base**, where instability of flows could be disruptive given the large stakes that Aberdeen holds in some companies – flows were negative in the quarter (-£1554m in Q2 (7%), but 2 net clients won); the **investment process** has not changed/is standardised across equity products. This facilitates cross-fertilisation of ideas and a team-led approach. Stable, well-resourced and experienced **investment team** (6 most senior team members average >19 years in industry and >12 years at Aberdeen), backed up by extensive and experienced regional teams. Andy Brown (senior inv mgr) has transferred from the GEM team on 1 August.

Baillie Gifford Bonds

(8.7% of Total Fund)

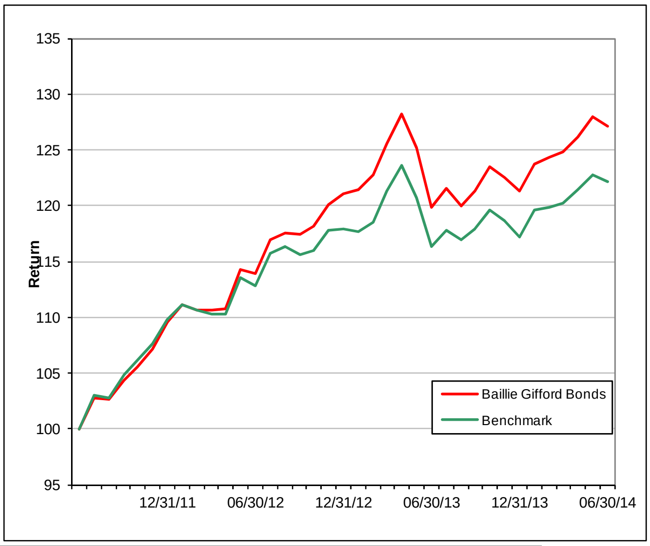
Investment Approach:

Baillie Gifford employs fundamental analysis to identify sustainable trends. It believes that there are inefficiencies that can be exploited in the areas of stock selection and interest rate and currency strategies.

Investment Objective:

To outperform a customised benchmark comprising index-linked gilts, conventional gilts and investment grade bonds by 0.9% per annum net of fees over rolling 3 year periods (inception date 30 March 2007).

3 Year Performance to 30 June 2014



Q2 2014	: + 0.2% excess return
3 Year	: + 1.4% p.a. excess return
Since inception	: - 0.2% p.a. excess return

Summary

	3 year performance is ahead of the objective.

Portfolio

The portfolio has a customised benchmark (20% FT-Actuaries Over 5 Years Index Linked Gilt Index, 30% FT-Actuaries All Gilts, 50% Merrill Lynch Sterling Non-Gilt Index). Baillie Gifford (BG) invests in three BG Funds on a no-fees basis to achieve the appropriate exposure.

Bonds, particularly corporate bonds, had another good quarter as the search for some yield at virtually any price continued. Corporate Bonds returned 2.1% and both conventional and Index Linked Gilts returned 1.1% over the quarter.

The Portfolio had a quarter of modest positive relative performance, returning 1.9% against a benchmark return of 1.6%. Over the quarter asset allocation, and to a lesser extent currency contributed positively to the relative return. However, over a one year period, stock selection remains the dominant factor in the positive relative return generating nearly +1.4% contribution over the year where their positioning in securitized, insurance companies', and lower credit rated bonds have all proved positive.

Looking forward, they have further reduced their weighting in lower credit rated instruments, and are concerned that there is sufficient return relative to the additional risk. They are still looking to add value by stock selection in EM and corporate bonds as well as through the active currency positions, although currency has given a neutral return over the year. They have maintained their biggest currency position relative to the benchmark which is +2.5% overweight USD, as well as some favoured EM Countries such as Mexico. They also continue to be 1% underweight GBP.

There has previously been some discussion around the potential to unwind the change to the Portfolio's benchmark and revert back to the previous one of 20/40/40, thereby reducing the proportion of Investment Grade Credit in the portfolio in favour of UK Government securities. The change has had a beneficial performance effect since it was made, with the spread of corporate bond yield over the equivalent sovereign bond yield reducing significantly. Given the very good run that IG and HY credit have had, supported by BG's views on the market outlook, this may be the time to seriously consider reducing the IG weighting in the benchmark going forward.

Key considerations/developments

Baillie Gifford is a long established, reputable partnership; the client base is stable and the investment process has not changed.

Assets under management in the sterling aggregate product increased from £581m to £613m over the quarter. However, this didn't represent new business to BG, rather a client transferring from separate Gilts and IG Funds. There were no changes to the investment staff in the quarter.

Baillie Gifford Diversified Growth

(12.2% of Total Fund)

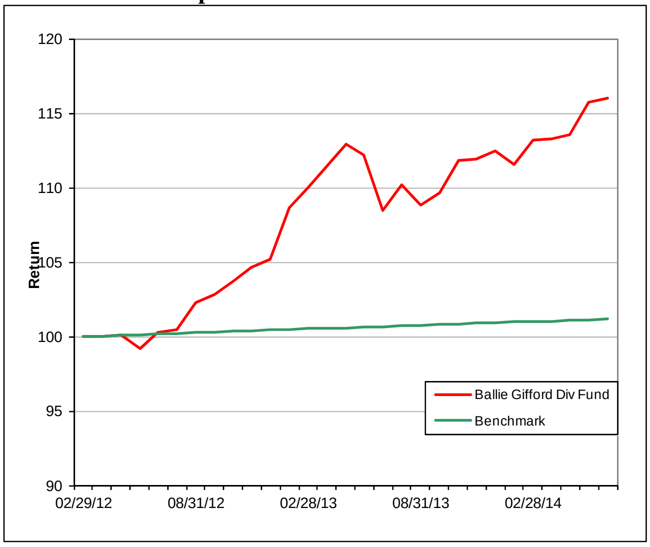
Investment Approach:

Baillie Gifford invests in a broad range of traditional and alternative asset classes, such as equities, bonds, property, private equity, infrastructure, commodities and currencies, adjusting portfolio weightings to reflect the relative attractiveness of the individual assets.

Investment Objective:

Objective: to outperform the UK base rate by at least 3.5% per annum (after fees) over rolling five year periods with an annual volatility of less than 10%. (Inception date 2 February 2012)

Since Inception Performance to 30 June 2014



Q2 2014	: +2.3% relative to base rate
1 Year	: +6.5% relative to base rate
Since inception	: +6.7% relative to base rate

Summary

Since Falkirk invested in Feb 2012, the risk/return is beating the modest fund objectives of (0.5% + 3.5% =) 4% pa net return with less than 10% volatility, by realising 7.2% pa net return with 5.6% delivered volatility.

Portfolio

While net performance beats the modest 4% pa target since inception, it has been falling; over the last 5 years it was 10.6% pa, but over the last 3 years it was 5.2% pa. They say that “we believe that prospective returns are likely to be lower than they have been in the past. Indeed, we are increasingly concerned that volatility, a good measure of the extent to which markets are worried about risks, has recently reached a record low”. Indeed, for Q2 they produced a “Special paper – why we hold cash”.

Including the 5.8% in cash, and a new 3% investment in “Allianz Merger Arbitrage Strategy” fund (returning 2%), nearly half of the fund (and most of the new investment) is now in assets which are expected to fail to meet the 4% pa return target.

Around 1/3rd of this fund is invested in other managers’ funds, with another 1/3rd in other Baillie Gifford funds. These funds have their own benchmarks and objectives, which may differ from that of Diversified Growth, causing contradictions and adding to risk, while the other managers’ funds (notably hedge and PE) also add to total charges.

“Active Currency” is reported at “-0.2% of assets”, and “5% of predicted volatility”. But they report “gross long positions of 42%” in FX, which means gross long and short are 84% - suggesting net FX bets are >60% of the fund. This implies FX risk is understated.

Their “predicted volatility” is still 6.6% - with around half of this from (listed and private) equities and 5% FX. Targeted maximum volatility is 10%. (cf global equities are 16.6%).

Key considerations/developments

Baillie Gifford is a long established, reputable partnership. Despite determining £5bn “capacity” end 2012 and “closure to all new clients” in June 2013, **assets** increased in Q2 to £5.56bn on £68m net inflows - making £926m net inflows since June “closure”.

There have been no changes to the organisation, the investment process or the team.

The 2/3rds “**fund of funds**” structure blurs objectives and adds hidden charges. The 1/3rd in Baillie Gifford funds have zero fees but still pay (0.2%) expenses, while the 1/3rd invested in other managers’ funds bear full double-charging.

Newton Global Thematic Equity
(14.6% of Total Fund)

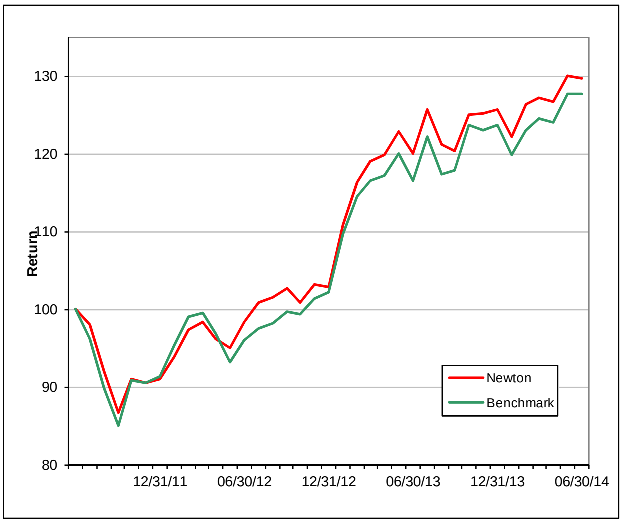
Investment Approach:

Newton identifies structural trends to gain perspective on the important risks and opportunities in investment markets. This thematic framework drives stock selection, which results in a concentrated portfolio.

Investment Objective:

To outperform FTSE All World Index by 3% per annum (net of fees) over rolling 5 year periods (inception date 30 June 2006)

3 Year Performance to 30 June 2014



Q2 2014	: - 0.7% excess return
5 Years	: + 0.3% p.a. excess return
Since inception	: + 0.9% p.a. excess return

Summary

Portfolio not achieving objective, but is ahead of benchmark since inception. It has been constructed to take advantage of weak equity markets.

Portfolio

The portfolio is genuinely unconstrained (45 stocks), indicating that it should be able to achieve its objectives. This is an equity portfolio, but the manager is able to hold up to 10% in cash. The manager continues to take a very defensive stance and cash (mostly short term US Treasuries) was 9% at quarter end.

Stock ideas flow from Newton's themes, which include deleveraging, financial concentration and growing Chinese influence. The portfolio is characterised by companies with stable earnings, strong cash flows, competitive advantages, inflation linkage, innovation, exposure to growth economies, good management & governance and attractive valuation.

The portfolio is overweight Europe/UK (+12%) equities, and underweight North America (-6%), Japan (-4%), Pacific (-4.5%) and other/emerging markets (-6%). It has high exposure to companies in the healthcare and consumer goods sectors, while financials, industrials and oil and gas companies with cyclical earnings are under-represented. The portfolio is likely to perform relatively poorly during strong equity markets, but its defensive tilt and high cash position should protect it if equity markets fall.

The portfolio underperformed in Q2 as strong performance in Europe was offset by weakness from holdings in/allocations to N. America, Emerging Markets and cash/bonds. There were positive contributions from consumer goods (tobacco) holdings, industrials (CH Robinson) and financials (underweight allocation), but these were more than offset by poor stock selection in healthcare (Express Scripts), technology (EMC, SAP) and consumer services, telecoms (Vodafone) and utilities.

During the quarter, three new stocks were introduced and six stocks sold outright

Key considerations/developments

Newton remains one of Bank of New York Mellon's asset management subsidiaries based in London; in the face of weak relative returns, management reassessed the **investment process** in 2011/12 and made some personnel changes to improve rigour, but did so without changing the key elements of the global thematic strategy; the **client base** is stable (no flows in or out).

Schroders UK Equity

(14.2% of Total Fund)

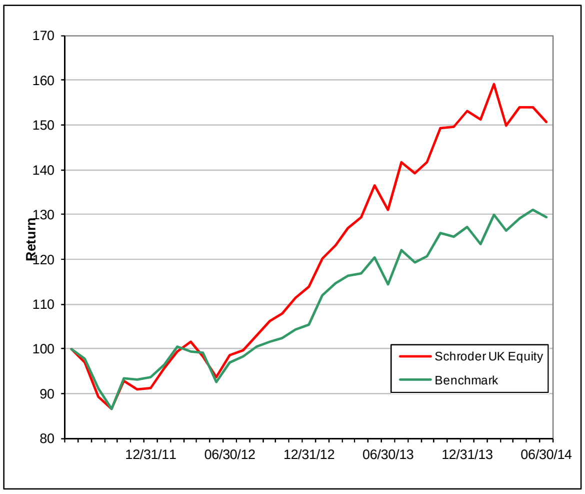
Investment Approach:

Schroder seek to identify stocks which trade at a substantial discount to their intrinsic value and where they believe that profits will surpass expectations. The investment style can be categorised as "value".

Investment Objective:

To outperform FTSE All Share Index by 1.25% per annum (net of fees) over 3 year rolling periods (inception date 30 September 2001)

3 Year Performance to 30 June 2014



Q2 2014	: -1.6% excess return
3 Year	: +5.7% p.a. excess return
Since inception	: +2.4% p.a. excess return

Summary

Short term underperformance (Q2 and Q1) though manager comfortably ahead of the objective on all timeframes. Clearly articulated strategy with stable ownership, client base and investment team.

Portfolio

The portfolio of 37 stocks deviates from the benchmark meaningfully, which means that the objective should be achievable, but the return profile is likely to be highly variable. Active sector positions are very similar to last quarter. The portfolio retains an overweight position in the life insurance and general retailers sectors, mining is the biggest underweight.

Relative returns in the second quarter were negative (-1.6%), however, the portfolio is still +1.9% over the most recent 12 months. Profit-taking was noticeable amongst names that had performed strongly over the preceding 12 months, this included Rentokil Initial, Trinity Mirror, and a number of the high street retailers. More positively, Astrazeneca shares continued to be buoyed by interest from Pfizer, while the insurance names rebounded from a difficult prior quarter where share prices were impacted by the Budget changes to the structure of the annuity market.

Once again, the team has continued to trim the winners in the portfolio where the gap between fundamental value and share price has narrowed. Interestingly, this is not something they have done with Astrazeneca, where 8% of the Fund is invested. The reason for this is the ongoing lack of attractive new ideas. They have taken advantage of weakness to add to existing holdings in Morrisons and Pearson, and initiated a new position in Centrica where market mistrust and new management allows an attractive entry point.

The team continue to caution with regards to market valuations, suggesting they are "operating conservatively and prudently to defend...capital gains". Pockets of value can be found in banks and other financials but new ideas have less upside than they did a few years ago. Suggestions that they are "clustering in big cap, blue-chip names...with a bit more of a buffer" and looking for things that "aren't expensive" rather than outright cheap further highlight their cautionary tone.

Key considerations/developments

Schroders is a publicly listed asset management company, which is still controlled by the family; the **client base** is fairly stable and the **investment process** has not changed. The UK Value product, in which Falkirk is invested, runs approximately £5.3bn in assets split roughly 1/3rd institutional and 2/3rd retail. The **investment team** appears to be stable and demonstrates high conviction in its investment approach.

Schroders Property Multi-Manager

(7.3% of Total Fund)

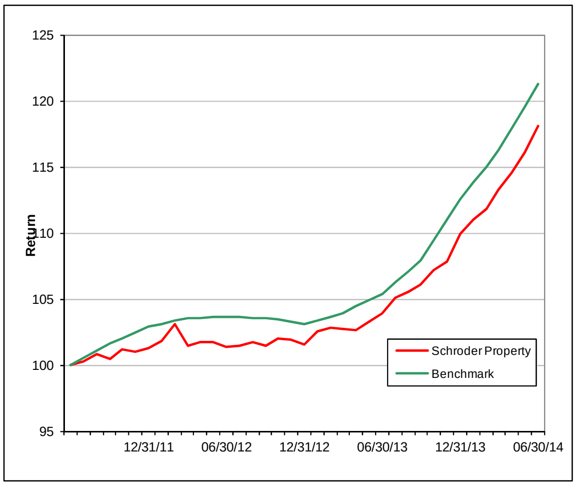
Investment Approach:

Schroders runs a segregated mandate providing a multi-manager portfolio of property funds. The manager seeks to identify attractive property markets and property funds with skilled managers, some of which are sector specialists.

Investment Objective:

To outperform IPD UK Pooled / Quarterly Property All Balanced Funds Weighted Average Index by 0.75% per annum (net of fees) over 3 year rolling periods (inception date 30 November 2005)

3 Year Performance to 30 June 2014



Q2 2014	: -0.1% excess return
3 Year	: -1.0% p.a. excess return
Since inception	: +0.0% p.a. excess return

Summary

Latest 3 year performance remains weak (-1.0%pa relative). Since inception the performance is in line with the benchmark, but less than the objective. The portfolio has been restructured and is now positioned for the future.

Portfolio

The portfolio is comprised of a diverse group of 15 funds investing in property assets largely in the UK. The portfolio is valued at £118m. Activity was fairly significant from 2009-2013, with over £80m of property transactions taking place, replacing 6 holdings with 6 new funds.

There is now expected to be low levels of future transaction activity. The manager plans to reallocate a small amount c3% from London offices to industrial property (in a new partnership to be managed by a specialist at Jones Lang).

Continental European exposure amounts to approximately 6% of the portfolio. The poor three year relative performance has been dominated by exposure to Continental Europe, which is not in the benchmark. (Recap in '06-07, 10% of the portfolio was committed to Europe.)
In addition, transaction costs and cash drag in a rising market affected performance.

The portfolio's risk profile has been rebalanced through greater investment in low geared, core balanced property funds and those funds targeting an income focussed approach. As a result, the manager believes the portfolio is well positioned for the current investment environment, in which the income yield on property is very competitive with government bonds.

The portfolio now targets to hold minimal amounts of cash - which now represents 1.1%.

Key considerations/developments

Schroders is a publicly listed asset management company, which is still controlled by the family; the **client base** is fairly stable and the **investment process** has not changed. The **investment team** appears to be stable, but the poor performance has put it on the defensive.

APPENDIX 3 – GLOSSARY

Benchmark - The yardstick used to measure the success and structure of a portfolio. All managers are measured against benchmarks. Passive managers are tasked with producing returns that are the same as the benchmark. Active managers are tasked with producing returns that are higher than the benchmark.

Benchmark return - Identifies the total return of the benchmark for the identified period. Return numbers for periods of one year or less show the actual return over the period. Returns for periods of greater than one year are annualised returns - they show the return per annum (%pa).

Dividend Yield - The dividend a company pays divided by its current price.

Duration - A measure of the sensitivity to interest rates of bonds. It identifies the approximate percentage change in a bond's price for a 100 basis point change in yield

Excess Return - Is the out / underperformance of the portfolio relative to the benchmark for the identified period. Return numbers for periods of one year or less show the actual return over the period. Returns for periods of greater than one year are annualised returns - they show the return per annum (%pa).

Investment Objective – All managers (and the Fund) are set investment objectives, which are related to a specific benchmark. The investment objective for a passive manager is to match the returns of the benchmark. The investment objective for an active manager is to exceed the returns of the benchmark by a pre-determined percentage per annum over a pre-determined period.

Market value (£) - Identifies the total market value of the portfolio / Fund

Portfolio return - Identifies the total time weighted rate of return of the assets of the portfolio for the identified period. Returns for periods up to 12 months are the return over that period. Returns for periods longer than 12 months are annualised returns – they show the return per annum (%pa).

Turnover - Is the level of purchases and sales for the period. High turnover is generally regarded as bad because trading costs are incurred.

AGENDA ITEM 12

FALKIRK COUNCIL

Subject:	**PRIVATE EQUITY AND ALTERNATIVES UPDATE**
Meeting:	**PENSIONS COMMITTEE**
Date:	**25 SEPTEMBER 2014**
Author:	**CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 This report updates the Committee on the progress and key events arising from each Manager's investment programme for the three months to 30 June 2014.

1.2 The Fund's private equity and alternatives programme is managed as follows:

SL Capital (Standard Life)	-	European Private Equity
Wilshire Associates	-	Global Private Equity
Grosvenor Capital	-	Global Infrastructure
M&G	-	Credit Markets

1.3 The Fund's strategic allocation to private equity and alternatives (excluding the allocation to the Baillie Gifford Diversified Growth Fund) is set at 10% of total fund assets. This is split 5% to private equity and 5% to infrastructure.

1.4 The attached schedule gives details of the current valuations and commitment levels.

2. SL CAPITAL PARTNERS

2.1 SL Capital is a subsidiary of Standard Life Investments, who in turn own 60% of the business. The remaining 40% is owned by 8 partners.

2.2 The Fund's overall commitment to SL Capital is **€102m (£82m)**, spread across four European Investment Funds – ESP 2004, ESP 2006, ESP 2008 and ESF 1 – all being fund of fund structures.

2.3 The second quarter of 2014 has seen the manager remain reasonably active. The Fund continues to benefit from its maturing investments in the 2004 and 2006 ESP funds, receiving **distributions of €2.1m** during the quarter. The Fund's strategy of investing in a range of vintages means these distributions have been complimented by **€1.4m of calls**, the majority of which relate to the ESP 2008 and ESF 1 funds, which are in the seed/growth stage of their investment lifecycles.

2.4 All funds, except ESF 1 outperformed the MSCI Europe Index of 2.2% for the quarter. Highlights included the Saga IPO, helping boost the value of the Acromas fund in ESP 2004 and rises in the value of various co-investments Freescale, HSS Hire and Solina.

2.5 In terms of market outlook, the manager remains optimistic about the northern part of the Eurozone, seeing a gradual increase in consumer spending and corporate earnings. Escalating tensions over the Ukraine, however, and the risk of further trade sanctions with Russia are reasons to be wary.

2.6 SL Capital have a pipeline of products available for investment, however as the Fund's current allocation to private equity is broadly in line with its strategic allocation, there is no pressing need to make a further commitment at this stage.

3. WILSHIRE ASSOCIATES

3.1 During the period from 2004, the Fund has made various commitments to Wilshire Associates covering several geographical areas as follows:

European Funds	-	€10.9m
US Funds	-	$53.2m
Asian Funds	-	$ 3.8m
Global (Fund IX)	-	$15.0m
		$72.0m
Total Commitment		£52.0m

3.2 In their quarterly update, Wilshire remain optimistic about the global macroeconomic backdrop but, echoing SL Capital, have concerns about rising geopolitical tensions.

3.3 During the quarter, **€767k was distributed** from the Euro funds while **€16k was called**. As one would expect, given the larger allocation to dollar funds, **$2m was distributed** and **$1.8m called**.

3.4 Investment activity has commenced in Wilshire Fund IX – the Falkirk Fund's most recent Wilshire commitment - with initial positions being taken in a US Buyout Fund, a European Buyout Fund and an Asia-Pacific Special Situations Fund.

4. GROSVENOR CAPITAL

4.1 The Fund's global infrastructure investments are made via an **$80m commitment** to the Customised Infrastructure Strategies (CIS) Fund managed by the Grosvenor Capital Customised Fund Investment Group (CFIG). The Fund has funded over 75% of its commitments.

4.2 The CIS Fund seeks to generate attractive risk-adjusted returns by investing in a diversified range of infrastructure funds, co-investments and secondaries. These focus on brownfield and greenfield assets, encompassing a broad range of infrastructure markets.

4.3 Although no distributions were made during the quarter, healthy investment activity was evidenced by CFIG calling in **$3.1m.** Total value to paid-in capital stands at 1.20. New commitments were made recently to InfraCapital Partners - a fund focusing on the energy, water and transportation utilities in Western Europe – and Project Metropolis, a portfolio of secondary US energy funds.

4.4 Grosvenor's investments to date mean that the Falkirk Fund's allocation to Infrastructure stands at 3% against a strategic allocation of 5%. This position should improve with the Falkirk Fund's arrangement to invest in UK infrastructure in conjunction with Lothian Pension Fund.

5. M&G UK COMPANIES FINANCING FUNDS

5.1 The M&G UK Companies Financing Funds provide the pension fund with exposure to UK credit markets. The Funds play a valuable economic role in providing debt financing to UK companies facing refinancing obstacles. The aim of the Funds is to create attractive levels of income for investors - LIBOR plus 3%-6% - with a low level of risk.

5.2 Falkirk's commitment to the M&G Funds is **£11.8m to Fund I** and **£10m to Fund II.** Fund I has been fully invested and Fund II is in the process of being drawn down.

5.3 For Fund 1, the portfolio consists of 8 loans with an average repayment period of 5.3 years and average credit rating of BB+. This includes loans of between £30m and £100m made to companies such as Hogg Robinson, Taylor Wimpey and Provident Financial.

5.4 For Fund II, the portfolio so far consists of 6 loans with an average repayment period of 6.3 years. Loans of between £10m and £45m have been made to companies including Caffe Nero and Hall & Woodhouse Ltd.

5.5 All loans continue to be paid in accordance with their covenants.

6. CONCLUSION

6.1 The investment experience of the Fund's private equity managers is generally optimistic, subject to concerns about rising tensions in Ukraine and the Middle East. The infrastructure and credit market managers continue to source deals at an acceptable pace.

6.2 The forthcoming review of the Fund's investment strategy will be an opportunity to consider the merits of private equity given the recent criticism of Fund of Fund structures by the Department of Communities and Local Government.

7. RECOMMENDATION

7.1 **The Committee is asked to note the progress of the Private Equity, Infrastructure and Credit Markets Programmes as at 30 June 2014.**

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

NIL

Appendix A

Falkirk Council Pension Fund
Alternative Markets Update - 30/06/2014

Exchange Rates	
$	1.6687
€	1.2461

Alternative Assets Summary - Approx Sterling Value

Manager	Fund	Commitment £,000	Unfunded £,000	(a) Cost £,000	(b) Return of Cost £,000	(c) Distrbtn Gains £,000	(d) Market Value £,000	(b + c + d) Total Value £,000	Total Value to Paid in Cap.	Inception Rate of Return
Private Equity										
SL Capital Partners	European Strategic Partners 2004	24,075	2,782	21,293	7,344	5,945	12,875	26,163	1.23	6.0%
SL Capital Partners	European Strategic Partners 2006	24,075	3,220	20,855	5,419	1,696	17,064	24,179	1.16	3.0%
SL Capital Partners	European Strategic Partners 2008	21,668	8,972	12,696	1,091	108	12,900	14,100	1.11	0.4%
SL Capital Partners	European Smaller Funds I	12,038	9,601	2,437	-	-	2,049	2,049	0.84	N/A
	SL Capital Partners Total	81,855	24,575	57,281	13,854	7,750	44,887	66,491		
Wilshire Associates	Fund VI - Europe	2,889	222	2,667	1,468	1,000	1,282	3,749	1.41	7.3%
Wilshire Associates	Fund VII - Europe	2,889	273	2,616	549	308	2,149	3,006	1.15	0.5%
Wilshire Associates	Fund VIII - Europe	2,969	706	2,263	566	327	2,032	2,925	1.29	33.2%
Wilshire Associates	Fund VI - US	8,390	492	7,898	2,773	2,593	5,643	11,010	1.39	4.9%
Wilshire Associates	Fund VII - US	6,892	439	6,453	1,797	1,572	5,360	8,730	1.35	4.7%
Wilshire Associates	Fund VIII - US	7,611	873	6,738	1,956	944	6,188	9,088	1.35	8.5%
Wilshire Associates	Fund VII - Asia	1,079	108	971	491	261	584	1,336	1.38	5.1%
Wilshire Associates	Fund VIII - Asia	1,199	706	493	143	35	481	659	1.34	-16.0%
Wilshire Associates	Opportunities Fund II-B	8,989	2,050	6,939	3,649	1,334	4,040	9,023	1.30	9.2%
Wilshire Associates	Fund IX	8,989	8,510	479	0	0	413	413		
	Wilshire Associates Total	51,895	14,379	37,517	13,391	8,374	28,174	49,939		
	Private Equity Total	**133,750**	**38,953**	**94,798**	**27,245**	**16,124**	**73,061**	**116,430**		
Infrastructure										
Credit Suisse/Grosvenor	Customised Infrastructure Strategies	47,942	11,662	36,279	3,496	1,919	37,951	43,366	1.20	5.0%
	Infrastructure Total	**47,942**	**11,662**	**36,279**	**3,496**	**1,919**	**37,951**	**43,366**		
Credit Markets										
Prudential/M&G	UK Companies Financing Fund	11,835	0	11,835	4,747	0	8,727	13,474	1.14	4.4%
Prudential/M&G	UK Companies Financing Fund II	10,000	7,081	2,919	0	89	2,917	3,006	1.03	2.5%
	Credit Market Total	**21,835**	**7,081**	**14,754**	**4,747**	**89**	**11,644**	**16,480**		
	Total Alternative Fund Value	**203,527**	**57,697**	**145,831**	**35,488**	**18,133**	**122,656**	**176,276**		