

The background of the slide features the coat of arms of the Government of Nunavut. It is a shield divided into four quadrants. The top-left quadrant shows a yellow diagonal band with a black cross. The top-right quadrant depicts a white caribou head with large antlers. The bottom-left quadrant shows a white sailing ship on blue wavy lines representing water. The bottom-right quadrant features a white eagle with spread wings perched on a branch. Above the shield is a crown with four white maple leaves. A white banner at the bottom contains the text "ANE FOR A'".

## **Agenda Item 6**

### **Statement of Investment Principles**

**Falkirk Council**

**Subject: Statement of Investment Principles**

**Meeting: Joint Meeting of Pensions Committee and Pension Board**

**Date: 21 March 2019**

**Submitted by: Director of Corporate and Housing Services**

**1. Purpose of Report**

- 1.1 The purpose of this report is to seek the approval of the Pensions Committee for a revised Statement of Investment Principles (SIP).
- 1.2 This replaces the SIP agreed by Committee in August 2017.
- 1.3 The revised SIP has been developed in conjunction with the Fife and Lothian Pension Funds and, subject to the approval of the Falkirk Pensions Committee, will harmonise the investment beliefs and principles in a common document applicable to the three Funds. With common beliefs and principles, there will be greater scope for collaborative investing and investment oversight.

**2. Recommendations**

**(1) The Pensions Committee and Pension Board are invited to comment on the revised Statement of Investment Principles.**

**(2) The Pensions Committee is asked to approve the adoption of the revised Statement of Investment Principles.**

**3. Statement of Investment Principles**

- 3.1 The Pension Fund is required to maintain and publish a Statement of Investment Principles setting out the beliefs and principles it intends to adopt in investing fund monies.
- 3.2 Good governance of the Fund requires that the SIP is reviewed from time to time e.g. when a review of investment strategy has been undertaken.
- 3.3 The revised SIP, which is attached as Appendix 1 to the report, has been reviewed by officers and by the Joint Investment Strategy Panel (JISP) which consists of FCA accredited officers and independent external advisers. A workshop for the Committees and Boards of the three Funds was held on 19<sup>th</sup> November. The purpose of the workshop was to help identify a set of draft investment principles that would be potentially acceptable to the three Funds.

3.4 The SIP makes a number of changes from the 2017 version, including:

- a. the incorporation of high level principles/beliefs which emerged from the November workshop;
- b. an updated section showing the Fund's target asset allocation across the newly agreed policy groups (Equities, Other Real Assets, Non Gilt Debt, Gilts and Cash) and the permitted ranges for each group (see SIP Appendix A);
- c. a statement recording how the Fund will comply with the UK Stewardship Code (see SIP Appendix C); and, overall,
- d. a simplification of content and format to improve readability.

#### 4. Monitoring and Reporting

- 4.1 The SIP is an important part of the Fund's governance arrangements and provides the framework within which the Fund sets its investment strategy.
- 4.2 The Fund's governance arrangements involve Committee delegating the implementation of the investment strategy to the CFO who in turn takes advice from the Joint Investment Strategy Panel. The Committee retains the key responsibility of setting the investment strategy across high level asset categories (i.e. policy groups) and for the monitoring and scrutiny of Fund investments.
- 4.3 The intended monitoring and scrutiny of investment activity is outlined below, under the headings of Governance Arrangements and Investment Outcomes.

##### Governance Arrangements

Aspect	Current Assurance (frequency)
Are Investment Strategy Panel meetings being held regularly?	<ul style="list-style-type: none"><li>• Update of Joint Investment Strategy Panel meetings/activity given to Committee (quarterly)</li></ul>
Is the Investment Strategy Panel addressing relevant issues?	<ul style="list-style-type: none"><li>• Visibility of agenda plan for Joint Investment Strategy Panel (to be reported to Committee annually)</li><li>• Investment manager mandates (incl. objectives and controls) discussed at Joint Investment Strategy Panel with CFO</li><li>• Traffic light monitoring of investment managers by LPF team with oversight of Panel (at least quarterly or as required)</li></ul>
Advice and scrutiny by external independent advisers	<ul style="list-style-type: none"><li>• Minutes of the meeting (with confirmation of attendees) is accessible to the Convener of the Committee (quarterly)</li><li>• External advisers attend Committee meeting and training events (at least annually)</li><li>• Regular tendering of advisers (contracts are 5 years plus one 2 year extension)</li></ul>
All of the above	<ul style="list-style-type: none"><li>• External and Internal audit scrutiny</li></ul>

## Investment Outcomes

Aspect	Current Assurance (frequency)
Are investments invested in line with strategy?	<ul style="list-style-type: none"><li>• Update on implementation of investment strategy with reporting on actual asset allocation to Committee (quarterly)</li></ul>
Funding update	<ul style="list-style-type: none"><li>• Actuarial valuation reported to Committee (every 3 years and annual updates from Actuary)</li><li>• Monitoring by Investment Strategy Panel and internal team (annually or more frequent as required)</li></ul>
Investment managers	<ul style="list-style-type: none"><li>• Traffic light monitoring of investment managers by internal team with Panel oversight (quarterly or more frequently as required)</li></ul>
Investment performance	<ul style="list-style-type: none"><li>• Performance of Fund reported to Committee (quarterly)</li></ul>
All of the above	<ul style="list-style-type: none"><li>• Briefings at Committee training sessions (at least annually or as required)</li></ul>

## 5. Measures of Success

- 5.1 Success of the investment strategy will, among other things, be measured by the achievement of the funding and investment objectives of the Fund.
- 5.2 The funding objective is to achieve a funding level of 100% over a period of 20 years.
- 5.3 The Investment objective needed to meet the funding objective is an annual return of gilts plus 2.8%.

## 6. Implications

### Financial

- 6.1 There are no direct financial implications arising from the report.

### Resources

- 6.2 There are no direct resource implications associated with the report recommendation. It is noted that as the collaboration with Lothian and Fife develops, there will be an increase in the level of internal investment management undertaken on the Funds' behalf by the Lothian Fund, the cost of which will be fully offset (and more) by the reduction in existing external management costs.

### Legal

- 6.3 The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 require administering authorities to prepare, maintain and publish a written Statement of Investment Principles.

## **Risk**

- 6.4 The SIP details how risks, compliance and governance aspects of the Fund in relation to investment matters are managed.

## **Equalities**

- 6.5 There are no equality issues arising from this report.

## **Sustainability/Environmental Impact**

- 6.6 The SIP sets out the approach of the three Funds to responsible ownership and details how voting, engagement and other Environmental, Social and Governance (ESG) activity will be undertaken. Compliance with the Statement is expected to contribute to the sustainability of the Funds' investments.

## **7. Conclusion**

- 7.1 The Statement of Investment Principles is a key document, along with the Funding Strategy and Governance Compliance Statements, within the Fund's over-arching governance framework.
- 7.2 The Fund's Statement of Investment Principles has been revised to take account of the changes arising from the recently concluded Investment Strategy Review and in order to pursue the efficiencies that can be achieved through the Falkirk, Fife and Lothian Pension Funds working collaboratively with a common set of investment principles.

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Date: 6 March 2019

## **Appendices**

Appendix 1 – Statement of Investment Principles including:

- Appendix A – Investment Strategy
- Appendix B – Investment Strategy Implementation
- Appendix C – Statement of Compliance with UK Stewardship Code
- Appendix D – CIPFA Principles for Investment Decision Making and Disclosure

## **List of Background Papers:**

None

## FALKIRK COUNCIL PENSION FUND

## STATEMENT OF INVESTMENT PRINCIPLES

## 1. INTRODUCTION

- 1.1 This Statement of Investment Principles (**SIP**) was agreed by the Pensions Committee (**Committee**) of Falkirk Council on 21 March, 2019. Falkirk Council is the administering authority of the Falkirk Council Pension Fund (“the Fund”).
- 1.2 The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 require administering authorities to prepare, maintain and publish a SIP. The SIP must be reviewed from time to time and revised within six months of any material changes.
- 1.3 In preparing this statement, the Committee has taken professional advice from the Joint Investment Strategy Panel (**JISP**), which includes external advisers and members of the Lothian internal investment team who are FCA authorised individuals.
- 1.4 The SIP describes the objectives, policies and principles adopted by the Pensions Committee in undertaking the investment of fund monies. The SIP also discloses the extent to which the Funds comply with the six “Myners Principles” of investment practice.
- 1.5 The SIP has been devised in conjunction with the Lothian and Fife Pensions Funds as part of the three Funds’ commitment to work collaboratively in order to achieve the efficiencies that come from scale investing.

## 2. GOVERNANCE

- 2.1 Falkirk Council has delegated responsibility for the management of the Fund to its Pensions Committee, which comprises six elected members from Falkirk Council and three co-opted members drawn from Employer, Pensioner and Trade Union interests. The Committee is supported by a statutory Pensions Board, consisting of four Trade Union and four employer representatives, which in turn is responsible for ensuring that the Fund operates in accordance with the applicable laws and regulations. The Committee and Board are supported by officers and advisers.
- 2.2 The Committee determines investment strategy based on proper advice from the Council’s Chief Finance Officer, who in turn takes advice from the JISP.
- 2.3 Responsibility for implementing the strategy is delegated to the Chief Finance Officer who in turn takes advice from the JISP. Day to day management of the Fund’s assets is undertaken by external investment managers whose activities are governed by Investment Management Agreements and the limits set out in Scheme regulations. It is anticipated that some of the Fund’s assets will in future be managed via an Investment Management Agreement with LPFI Ltd – the FCA authorised investment vehicle of Lothian Pension Fund.
- 2.4 The SIP forms part of a governance framework that includes Statutory Regulations, the Pensions Committee, the Pension Board, the Joint Investment Strategy Panel, the Fund’s Advisers and the Fund’s Funding Strategy and Governance Compliance Statements.

### 3. HIGH LEVEL INVESTMENT PRINCIPLES

- 3.1 The following principles agreed by the Committee are designed to guide the Fund's governance, strategies and alignment with its agents and to support consistency in decision-making over the long term.
- 3.2 **Committee believes that their decisions, and those of officers, must give precedence to the fiduciary duty owed to members and employers.** Fiduciary duty is paramount. The Pensions Committee recognises the potential conflicts of interests inherent in a local authority administering a multi-employer pension fund. The objectives of the administering authority, its officials and officers and those of the Fund are not necessarily the same. The primary objective is to ensure solvency so that retirement benefits that employers promise to members under scheme rules can be paid when they fall due. (Legal view on fiduciary duty issued by the Scheme Advisory Board is available at <https://lgpsab.scot/fiduciary-duty-guidance/>.)
- 3.3 **Committee believes that the Fund should mitigate risk by ensuring alignment of interests wherever possible.** Agency costs are high in the financial services industry – agents are often motivated to act in their own best interests rather than those of the principal (the Fund). Alignment of interests and partnering with similarly aligned organisations will help to address the principal-agency problem to the benefit of the Fund and its partners. External resources should, therefore, only be used where internal resources cannot be justified or obtained, and where suitable alignment can be established.
- 3.4 **Committee believes that it should work with like-minded partners to benefit from increased scale and greater resilience.** There are significant economies of scale in the business of managing investments, so working with like-minded partners with similar long-term objectives and liabilities can achieve lower costs and reduce operational risks with increased resilience.
- 3.5 **Committee believes that cost transparency aids decision-making.** The asymmetric structure of incentives in financial markets (upside participation in success without downside participation in failure) encourages strategies that may benefit agents (external managers and other financial intermediaries) and be detrimental to investor (Fund) returns. Agents often present fees and other charges in a way that obscures rather than illuminates. Full cost transparency should aid decision-making and so benefit Fund returns.
- 3.6 **Committee believes it should focus on policy setting, including high-level strategic asset allocation which defines risk and return objectives, with appropriate governance structure and oversight.** Implementation of more granular investment decisions (such as the selection/deselection of individual managers and investments) and regular monitoring should be delegated to suitably qualified and experienced individuals with sufficient time and other resources at their disposal. Appropriate delegation, constraints and reporting requirements should be in place. Reporting to Committee should focus on the long-term objectives of the Fund.
- 3.7 **Given future uncertainties, the funding strategy should be prudent.** The Funding Strategy Statement expresses the funding objective, which informs the invested strategy options. The ultimate objective is to ensure solvency so that retirement benefits that employers promise to members under scheme rules can be paid when they fall due, so full funding should be achieved in a prudent manner to ensure that liquid assets are available at the required time. This is important for members, employers and taxpayers as the scheme is ultimately state-backed.

- 3.8 **Committee believes that the ability of the Fund to pay pension benefits when they fall due is more important than mark-to-market funding levels.** Committee recognises that the measurement of the value of promised benefits in a defined benefit scheme is the subject of controversy. Committee believes that where employer circumstances allow, investment strategy should focus on delivering strong (real) returns that grow to cover cashflows over the longer term rather than focusing on protecting the funding level in the short term.
- 3.9 **Committee believes ‘return-seeking’ assets are likely to outperform ‘risk-free’ assets as the investment horizon lengthens, but this is not guaranteed.** Time horizons matter a great deal. The appropriate horizon for investment risk-taking depends on the duration of the liabilities, the profile of projected cash flows and the deficit recovery and contingency plans for the scheme (the sponsor covenant).
- 3.10 **Committee believes in owning a diversified portfolio of assets so that it is not overly exposed to any particular contingency.** Asset diversification can reduce risk where assets are not correlated. Committee recognises that the future is unpredictable and that real returns from investments are uncertain. Fund returns will be determined primarily by the high-level investment strategy allocation to different asset classes and the timing of material changes. Asset allocation balances diversified risks with the expected additional returns for these risks.
- 3.11 **Committee believes that responsible investment should reduce risk and may improve returns.** The Local Government Pension Scheme (LGPS) was designed with an important social purpose in mind – the provision of retirement income for individuals. The Fund’s fiduciary duty means that the pursuit of financial return is its paramount concern, although it may also take purely non-financial considerations into account provided that doing so would not involve significant risk of financial detriment. Committee believes that investment should involve a holistic approach to analysis and decision-making that considers sustainability and financially material risks, including environmental (such as climate change), social and governance issues.
- 3.12 **Committee believes it should exercise its ownership rights in a responsible way, constructively engaging with companies to reduce risk, rather than divesting.** The Fund’s interests are better protected from adverse impacts by collaborating with like-minded investors to have greater influence in engaging with companies, government and regulators. Engagement is preferred rather than mechanistic divestment because it is consistent with the Fund’s fiduciary duty to members and employers, and it encourages responsible behaviour by companies in relation to environmental, social and governance issues.
- 3.13 **Committee believes that monitoring and assessment of investment success should be viewed on a long-term basis.** No asset mix provides a stream of cash flows that perfectly matches the liability payments of the Fund as they fall due, so monitoring activity is complex. The Fund is long term in nature and the success of a given investment strategy is likely to ebb and flow with changing investment environments in an unpredictable way. Investment monitoring is challenging and should be viewed through a long-term lens.
- 3.14 **Committee believes that peer group comparative analysis needs to be treated with care.** No two pension funds are identical, so peer group analysis should be undertaken with care as different funds hold different investment beliefs, objectives and return and risk appetites.



## 4. RESPONSIBLE INVESTMENT

- 4.1 With liabilities extending decades into the future, it is in the Fund's interests to take its responsibilities as an institutional asset owner seriously. To this end, the Fund's approach to responsible investment centres on effective stewardship of all their assets, with a particular focus on good corporate governance to deliver sustainable investor value.
- 4.2 The Fund's investment managers are required to integrate ESG analysis into their decision-making, including those related to climate change. The way in which managers integrate ESG considerations into their investment processes is a key consideration in the selection and appointment process of any new investment manager. Existing managers are expected to provide regular updates on their approach to ESG matters and towards sustainable investment. These reports are made available to Committee and Board members via the Fund secure portal.
- 4.3 As an institutional shareholder with holdings in numerous listed companies, the Fund recognises its responsibility to exercise its voting rights as part of its fiduciary duty and stewardship responsibilities. The Fund currently engages PIRC Ltd to provide advice and research services on all matters pertaining to corporate governance. This extends to casting votes on the Fund's behalf in relation to the Fund's active equity holdings.
- 4.4 PIRC undertakes its voting responsibilities in accordance with shareholder voting guidelines it has devised to be in line with the UK Corporate Governance Code. The guidelines seek best practice in a variety of areas including Report and Accounts; Dividends; Role of Directors and Directors Remuneration; Auditors and Shareholder Accountability and Corporate, Social and Environmental Accountability.
- 4.5 PIRC are responsible for reporting, on a quarterly basis, how votes were cast and whether there were any significant company issues during the quarter. Details can be found on the Fund website at [www.falkirk.gov.uk](http://www.falkirk.gov.uk).
- 4.6 The Fund is a member of Local Authority Pension Fund Forum (LAPFF). LAPFF exists to promote the investment interests of local authority pension funds, and to maximise their influence as shareholders while promoting social responsibility and high standards of corporate governance at the companies in which they invest. Formed in 1990, the Forum brings together a diverse range of around 80 local authority pension funds with combined assets of over £230 billion.
- 4.7 The Fund is committed to engaging with and influencing companies, governments and regulators as appropriate. The Fund does not follow a policy of exclusion or automatic divestment, as such a policy has the potential to transfer ownership rights to investors without responsible investment policies.
- 4.8 The Fund will consider joining campaigns /action groups involving other institutional investors to ensure that sustainability and financially material risks, including environmental social and governance issues are being adequately addressed by investee companies.
- 4.9 The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting high quality corporate governance and reporting. As long-term investors, the Fund recognises the importance of promoting responsible stewardship and long-term decision making. The Fund seeks to adhere to the FRC'S UK Stewardship Code, and encourages its appointed asset managers to do so too. Details of adherence to the Code are provided in Appendix B.

## 5. FUND OBJECTIVES

- 5.1 The **primary objective** of the Fund is to ensure that there are sufficient funds available to meet all pension and lump sum liabilities as they fall due for payment.
- 5.2 The **funding objectives** for the Fund are documented in the Committee's Funding Strategy Statement, which is reviewed at least triennially. The funding objectives, together with the rates of return being targeted and levels of risk to be tolerated, are central to each Fund's investment strategy, and governs the allocation across various asset classes.
- 5.3 The **investment objective** of the Fund is to achieve a return on Fund assets which is sufficient over the long term to meet the funding objectives as outlined in the Funding Strategy Statement. Investment returns are generated by a combination of income (from dividends, interest and rents) and gains or losses on capital.
- 5.4 In effect, the Fund's objective is to generate sufficient long term returns to pay promised pensions and to make the scheme affordable to employers now and in the future, while minimising the risk of having to increase contribution rates in the future.
- 5.5 Committee has set investment strategy with reference to the following **policy groups**, which are regarded as the key determinants of risk and return. The policy groups condense the vast array of investment choices into a manageable number of investment groups with broadly similar characteristics:
- **Equities** provide an equitable share in the assets and profits of companies. Income is provided through discretionary share dividends. Equities are listed in the UK or overseas, or are unlisted (private equity). Equities have historically produced returns above inflation.
  - **Gilts** are debt instruments issued by the UK Government. Typically, these provide interest payments on a regular basis over the life of the loan until capital is repaid at maturity. Some gilts provide interest payments and capital repayment value that is directly linked to price inflation (the Retail Price Index (RPI)). These are known as Index Linked Gilts and they provide the closest match to the Fund's liabilities, most of which are inflation-linked. Some other governments also issue this type of debt, but in different currencies tied to price inflation in their own countries.
  - **Non-Gilt Debt** instruments are issued by a range of borrowers to finance their activities in various sectors of the economy, which means that they carry varying degrees of credit risk. Income is provided through interest, which is typically paid to the lender on a regular basis until the loan capital is repaid, generally at par by the issuer at a pre-determined date. Bonds can pay a fixed, variable or inflation-linked rate of interest. Bonds are listed in the UK or overseas, or are unlisted (private debt).
  - **Other Real Assets** are typically investments in a share of income and capital appreciation of tangible assets, including **property** (land and/or buildings for commercial or residential use), **infrastructure** (assets deemed essential to the orderly functioning of daily life, such as renewable energy generation and transmission assets, water utilities, airports and toll roads) and **timberlands**. Income comes from dividends and rents.
  - **Cash** is also a form of investment used to provide instant or short-term liquidity, and can be held in both sterling and foreign currencies (including Treasury Bills, Money Market Funds

and Secured Investments). Cash generates interest income, but typically a lower rate than bonds and other debt.

- 5.6 As the returns of the above investments are not completely correlated, the Fund expects to achieve diversification and better risk-adjusted returns by investing in assets from each policy group.
- 5.7 In order to maximise the opportunities for collaborative investing, the policy groups set out in 5.5 match those used by the Lothian and Fife Pension Funds.

## 6. FUND STRATEGY AND IMPLEMENTATION

- 6.1 The Committee's agreed investment strategy (see Appendix A) is expressed in terms of allocations to various policy groups (or asset classes). These reference portfolios are expected to generate the required return with a reasonable probability of success. The rate of return being targeted and the level of risk to be tolerated are central to the determination of the investment strategy (or asset mix) of the Fund.
- 6.2 The overall Fund strategy is measured against a specific benchmark by an independent performance measurement specialist, and this is reported to the Committee. The Chief Finance Officer is responsible for monitoring investments and investment activity taking due advice from the JISP, which meets at least quarterly.
- 6.3 The Committee has delegated the implementation of strategy to the Chief Finance Officer, taking advice from the Joint Investment Strategy Panel (JISP). The Chief Finance Officer operates within the parameters agreed by the Committee, investing the Fund's assets in the policy groups within the permitted ranges.
- 6.4 The Chief Finance Officer, advised by the JISP, identifies the combination of investment managers and mandates within the policy groups in order to deliver the objectives of the Fund. The investment managers and mandates are listed in Appendix A. The Fund employs external managers, but also works collaboratively with the Lothian Fund in house investment team in recognition of the cost and alignment advantages of doing so.
- 6.5 To reduce the risk that a Fund does not deliver its objective, controls are set for each manager. These are detailed in formal Investment Management Agreements. Where the Fund's assets are managed internally (i.e through an investment management agreement with Lothian Pension Fund), then formal investment objectives and constraints will also be set for those mandates. In all cases, investment managers are responsible for the selection of individual holdings.
- 6.6 Whilst overall strategy is measured against a specific benchmark, the performance of individual managers and their mandates are measured against mandate-specific benchmarks of risk and return. Performance is undertaken by an independent performance measurement specialist and the results monitored by the JISP on a quarterly basis.
- 6.7 The Fund collaborates with other investors (i.e. Lothian and Fife) to benefit from increased scale and cost sharing arrangements.

## 7. OTHER INVESTMENT CONSIDERATIONS

### 7.1 Realisation of investments

Most of the Fund's investments are in liquid markets and can be expected to be sold relatively quickly if required. A proportion of the Fund's investments (such as property, private equity, private debt and infrastructure) have less or limited liquidity and would therefore take longer to be sold. The overall liquidity of the Fund's assets is considered in the light of potential demands for cash.

### 7.2 Stock Lending

The Fund does not participate in stock lending but may do so in the future, subject to appropriate safeguards being in place and Committee approval.

### 7.3 Underwriting

Managers are permitted to underwrite and sub-underwrite stock issues subject to the security being deemed attractive on a medium-term view and subject to the application being limited to an amount the manager would wish to hold over the medium term.

### 7.4 Derivatives

The Committee has approved the use of derivatives, subject to prevailing legislation and control levels outlined in investment manager agreements. A derivative is a security or contract that derives its value from its relationship with another asset. The Fund may make use of contracts for differences and other derivatives either directly or in pooled funds investing in these products for efficient portfolio management or to hedge specific risks. For example, forward currency contracts allows the Fund to reduce risk from currency fluctuations and equity futures allow the Fund to reduce risk during major portfolio rebalances/transitions.

### 7.5 Safekeeping of Assets

A global custodian is employed to ensure the safekeeping of investments.

## 7. COMPLIANCE

### 8.1 Regulations and Investment Limits

The Fund is compliant with the statutory restrictions set out in the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 and the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Amendment Regulations 2016.

8.2 In terms of reporting, the Fund also complies with the Local Authority Accounting (Scotland) Regulations 2014 and the Local Government Pension Scheme (Scotland) Regulations 2018. These require the publication of an Annual Report and Accounts duly approved and audited.

8.3 The Regulations contain limits on the percentage of a pension fund that may be invested in certain asset types. In accordance with the Regulations, the Committee have agreed the limits applicable to the Fund's investments in partnerships to accommodate the allocation to unlisted investments, including infrastructure, timber, property, equity and debt. The limits agreed by Committee are:

- All contributions to any single partnerships: 5% (statutory maximum of 5%)
- Contributions to all partnerships: 20% (statutory maximum of 30%)

The Committee has taken proper advice in respect of these limits from the Joint Investment Strategy Panel and from officers. The limits will apply for the period during which the Fund's strategic allocations include investments in partnerships, unless investment considerations require an earlier review. This decision is compliant with the Regulations.

**8.4 CIPFA Principles for Investment Decision Making**

Regulations require administering authorities to publish the extent to which they comply with guidance issued by Scottish Ministers, which in turn refer to guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Fund's compliance statement is provided in Appendix D.

**8.5 Review of SIP**

The Committee will review this statement annually or more frequently if appropriate. The Committee will consult with such persons as it considers appropriate and take proper advice when revising the statement.

## APPENDIX A – INVESTMENT STRATEGY (6 DECEMBER 2018)

### FALKIRK COUNCIL PENSION FUND: INVESTMENT STRATEGY

Investment Objectives: to achieve a return of at least gilts +2.8% per annum and generate sufficient cash to pay pensions as they fall due.

Policy Group	Reference Portfolio		Permitted Range	Long Term Expected Return
	Current Target 1 December 2018	Target Weight 2019 - 2024		
Equities	60%	60%	45% - 65%	Gilts +3.5% p.a.
Other Real Assets	20%	20%	10% - 25%	Gilts +2.5% p.a.
Non-Gilt Debt	15%	15%	0% - 25%	Gilts +1.0% p.a.
Gilts	5%	5%	0% - 20%	Gilts +0.0% p.a.
Cash	0%	0%	0% - 10%	NA
<b>Total</b>	<b>100%</b>	<b>100%</b>		<b>Gilts +2.8% p.a.</b>

## APPENDIX B: INVESTMENT STRATEGY IMPLEMENTATION (12 DECEMBER 2018)

The investment strategy in Appendix A is implemented by investing in a range of mandates managed by external or potentially internal investment managers. The current mandates and managers for the Fund are presented in the table below:

Policy Group	Mandate	Manager
<b>Equities</b>		<b>External</b>
	UK Value	Schroders
	Global Thematic	Newton
	Global	Aberdeen Standard
	Global Passive	Legal and General
	Global Fundamental Weighting	Legal and General
	Private Equity	Wilshire/SL Capital
<b>Gilts</b>		<b>External</b>
	Gilts	Baillie Gifford
<b>Non Gilt Debt</b>		<b>External</b>
	Non Gilt Bonds	Baillie Gifford
	Private Debt	Various
<b>Other Real Assets</b>		
	UK Property	Schroders
	Global Infrastructure	Internal/GCM
	Affordable Housing	Hearthstone
<b>Cash</b>		<b>Internal and External</b>
	Cash	Various

The Fund also has an allocation to a Diversified Growth Fund managed by Baillie Gifford which contains assets across the 5 policy groups above.

The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting transparency and integrity in business. It sets the UK's Corporate Governance and Stewardship Codes. The Fund's Statement of Compliance with the UK Stewardship Code is presented below:

***Principle 1: Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.***

We acknowledge our role as an asset owner under the UK Stewardship Code and seek to hold to account our fund managers and service providers in respect of their commitments to the Code. In practice, our policy is to apply the Code through the:

- appointment of PIRC Ltd;
- membership of the Local Authority Pension Fund Forum (LAPFF);
- work of our external investment managers;
- participation in class actions; and
- work of the internal team.

We believe that this combination enables us to provide the appropriate standards of stewardship on behalf of the beneficiaries of the Fund through their monitoring of shareholdings, so that we can fulfil our fiduciary responsibilities as long-term shareholders.

Through our engagement of PIRC and our membership of LAPFF, we keep informed of potential issues of concern at both individual companies and across the market as a whole, which leads to collaborative engagements in which the Fund participates.

The various external investment managers we utilise, including Legal and General, Newton and Schroders operate their own stewardship and engagement initiatives in relation to investee companies and provide regular reports on these issues. This information is made available to those responsible for the governance of the Fund.

Where investment management is undertaken by Lothian Pension Fund on behalf of the Fund, environmental, social and governance (ESG) issues are integrated within the Lothian investment decision making process together with direct engagement where feasible with investee companies.

***Principle 2: Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.***

The Fund's efforts to manage its potential conflicts of interest can be summarised below:

- The Fund has a Conflicts of Interest policy which explains the responsibilities of those responsible for Fund governance and describes how conflicts require to be managed. Pensions Committee and Pension Board members are required to make declarations of interest prior to Committee meetings.
- We also encourage the asset managers employed by the Fund's to have effective policies addressing potential conflicts of interest.
- Our policy of constructive engagement with companies is consistent with the Fund's fiduciary responsibilities.

**Principle 3: Institutional investors should monitor their investee companies.**

The Fund monitors the activities of its investee companies by relying on the combined services provided by PIRC, LAPFF and its external investment managers.

- We expect them to monitor companies, intervene where necessary, and report back regularly on activity.
- Activity is reported on the Fund's website quarterly, including the number of company meetings at which the Fund has voted and how the Fund has voted.

LAPFF also monitors and engages with companies and provides an 'Alerts' service, which highlights concerns over corporate governance issues.

**Principle 4: Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.**

As highlighted above, responsibility for interaction with companies is shared with the bulk of interventions being undertaken by external managers and the LAPFF. In general,

- We expect the approach to engagement on our behalf to be value-orientated and focused on long term sustainable profitability.
- The internal team also monitors investee companies and escalates engagement activity directly with investee companies as required.
- We may also propose escalation of activity through the Local Authority Pension Fund Forum.
- Consistent with our fiduciary duty to beneficiaries and in order to encourage improved conduct in future, we consider participating in shareholder litigation where it appears likely that the Fund will recover losses (net of costs) sustained because of inappropriate actions by company directors.

**Principle 5: Institutional investors should be willing to act collectively with other investors where appropriate.**

We seek to work collaboratively with other institutional shareholders in order to maximise the influence that we can have on individual companies. We do this through:

- membership of the Local Authority Pension Fund Forum (LAPFF), which is a collaborative effort of approximately 80 local authority pension funds. LAPFF engages and lobbies for positive changes on environmental, social and governance issues on behalf of its members. See <http://www.lapfforum.org/> for more details.

**Principle 6: Institutional investors should have a clear policy on voting and disclosure of voting activity.**

The emphasis of our voting policy is to promote best practice.

- We seek to vote on all shares held and have appointed PIRC to exercise voting on our behalf in respect of active mandates held. PIRC's voting policy is in accordance with the UK Corporate Governance Code. The guidelines seek best practice in a variety of areas including Report and Accounts; Dividends; Role of Directors and Directors Remuneration; Auditors and Shareholder Accountability and other Corporate, Social and Environmental issues.



- The Fund retains the right to direct PIRC or a manager in a particular way in respect of any corporate governance issue.

**Principle 7: Institutional investors should report periodically on their stewardship and voting activities.**

We do report on our stewardship and voting activities:

- We report annually on stewardship and voting activity in the Fund's annual report and accounts.
- We disclose our historic voting information on our website at <http://www.falkirkpensionfund.org/falkirk-council-pension-fund/about-us/who-runs-the-pension-fund>. This includes the total number of votes cast at which company meetings and whether the votes were cast for or against company management. We disclose this information in arrears so that we are transparent and accountable and dialogue with companies in our portfolios is not compromised.
- We also report annually on stewardship and voting activity directly to the quarterly Pensions Committee and Board.

## APPENDIX D – CIPFA PRINCIPLES FOR INVESTMENT DECISION MAKING AND DISCLOSURE

The Chartered Institute of Public Finance and Accountancy (CIPFA) published six Principles for Investment Decision Making and Disclosure in the Local Governance Pension Scheme in the UK in 2012. Details of the principles and the Fund's compliance are described below.

### **Principle 1 – Effective decision making**

*Administering authorities should ensure that decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to take them effectively and monitor their implementation. Those persons or organisations should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.*

- The Fund's Training Policy (comprising a compulsory training seminar for all new Committee and Board members and ongoing training) provides the knowledge to enable them to evaluate and challenge the advice they receive. Standards relating to the administration of the Committee's business are strictly up-held.
- The Pensions Committee focuses on setting the strategy for the Fund and monitoring performance. The Pension Board also attends Committee meetings and is responsible for assisting the Committee in securing compliance with relevant regulations and other legislation.
- The Chief Finance Officer, supported by the Pensions Manager, is responsible for the day to day running of the Fund. The Chief Finance Officer is also responsible for the provision of the training plan for Committee to help them to make effective decisions to ensure that they are fully aware of their statutory and fiduciary responsibilities, and to regularly remind them of their stewardship role.
- The Joint Investment Strategy Panel advises the Chief Finance Officer on the implementation of the agreed strategies, reviewing structure, funding monitoring, performance and risk and asset allocation. The Joint Investment Strategy Panel meets at least quarterly and is made up of experienced investment professionals, including independent advisers.
- The in-house team undertakes day-to-day monitoring of the Fund. The team includes personnel with suitable professional qualifications and experience to provide the necessary skills, knowledge, advice and resources to support the Joint Investment Strategy Panel and the Pensions Committee.
- Conflicts of interest are managed actively. At each Committee meeting, elected members of the Pensions Committee and Pensions Board are asked to highlight conflicts of interest. A Conflicts of Interest policy applies to members of the Committee and the Pension Board to ensure that conflicts of interest are highlighted and managed appropriately.

## **Principle 2 – Clear Objectives**

*Overall investment objectives should be set out for the fund that take account of the scheme's liabilities, the potential impact on local council tax payers, the strength of the covenant of the participating employers, and the attitude to risk of both the administering authority and the scheme employers, and these should be clearly communicated to advisers and investment managers.*

- The Statement of Investment Principles and the Funding Strategy Statement define the Fund's primary funding objectives.
- Asset-liability modelling is undertaken with the help of external advisers to aid the understanding of risks and the setting of investment strategy.
- Reviews of investment strategy focus on the split between broad asset classes (equities, gilts, other debt, other real assets and cash).
- Investment Management Agreements set clear benchmarks and risk parameters and include the requirement to comply with the Fund's Statement of Investment Principles.
- Appointments of advisers are reviewed regularly. Investment and actuarial advisers are appointed under separate contract. Procurement of advisers is conducted within European Union procurement regulations.
- The setting of the Funding Strategy includes specific consideration of the desire to maintain stability in employer contribution rates.

## **Principle 3 – Risk and liabilities**

*In setting and reviewing their investment strategy, administering authorities should take account of the form and structure of liabilities. These include the implications for council tax payers; the strength of the covenant of participating authorities; the risk of their default, and longevity risk.*

- The Fund takes advice from the scheme's actuary regarding the nature of its liabilities. Asset-liability modelling is undertaken periodically to aid the setting of investment strategy, and these exercises specifically take account of covenant strength and longevity risk.
- The Funding objective for the Fund are expressed in relation to the solvency and employer contribution rates. The Fund monitors the covenants of participating employers on an ongoing basis in the context of overall materiality.
- The Chief Finance Officer is responsible for ensuring the appropriate controls of the Fund. Controls are subject to internal audit, and results of audits are submitted to the Pensions Committee.
- The Fund maintains a Risk Register, which is formally reviewed twice per year with input from Pension Board members.

#### **Principle 4 – Performance assessment**

*Arrangements should be in place for the formal measurement of the performance of the investments, investment managers and advisers. Administering authorities should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.*

- The Fund's performance and risk analysis is produced by an independent external provider.
- The internal investment team monitors the external investment managers' performance and risk on a regular basis and reports this to the Joint Investment Strategy Panel. The Joint Investment Strategy Panel assesses the performance and risk of both internal and external investment managers on a regular basis (typically quarterly).
- The Fund's contracts with its advisers are regularly market tested.
- The Joint Investment Strategy Panel assesses its own performance on a regular basis and reports to Committee on its activities, typically annually.
- Training and attendance of members of the Pensions Committee and the Pensions Board are monitored and reported on a regular basis.

#### **Principle 5 – Responsible ownership**

*Administering authorities should adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholders and agents.*

*A statement of the authority's policy on responsible ownership should be included in the Statement of Investment Principles.*

*Administering authorities should report periodically to members on the discharge of such responsibilities.*

- The Fund's approach to responsible investment is described in the Statement of Investment Principles which is available on the Fund website at <http://www.falkirkpensionfund.org/falkirk-council-pension-fund/about-us/forms-and-publications>.
- The Fund's policy on responsible ownership is included in the statement on the Financial Reporting Council's Stewardship Code (see Appendix C of the Statement of Investment Principles).
- Details of the Fund's voting record is available on the Fund website at <http://www.falkirkpensionfund.org/falkirk-council-pension-fund/about-us/who-runs-the-pension-fund>. Details of voting are provided to the Committee and Board at the quarterly meetings. Information on engagement is also made available to Committee and Board.
- The Fund's annual report and accounts also includes a summary of the Fund's approach to responsible investment. The full report is available on the website and is sent to members on request.

## **Principle 6 – Transparency and reporting**

*Administering authorities should act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives; and provide regular communication to members in the form they consider most appropriate.*

- Meetings of the Pensions Committee are open to the public. Members of the public are entitled to make a deputation at Committee meetings. Committee papers are available on the Falkirk Council website. The Pension Board joins the Committee at all meetings.
- The Committee's remit covers wider pension scheme issues, in addition to the management and investment of funds.
- The Fund's policy statements, including the Statement of Investment Principles, Governance Compliance Statement and Funding Strategy Statement are maintained regularly. Stakeholders are consulted on changes. Documents are available on the Fund's website.
- The Fund produces an Annual Report & Accounts. The full report is available on the website, and is sent to members on request. The Fund also produces an annual newsletter for members as well as an annual benefit statement. Regular briefings are provided to employers. The Fund website is updated regularly.

Chief Finance Officer

Falkirk Council

21 March 2019